Learning. For life.

Pearson

Annual report and accounts 2020

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Our reporting structure

Following the appointment of our new Chief Executive, Pearson has announced a new corporate structure, approved by the Board and coming into effect from 2021. This is outlined in more detail on pp18–25. In this annual report, the forward-looking 'Our strategy' section follows our new structure.

The 'Financial review' and 'Segmental performance' sections continue to use our 2020 reporting structure – Global Online Learning, Global Assessment, North American Courseware and International – as these relate to our 2020 performance. Next year's report will use our new operating structure throughout.

Strategic report

The strategic report, up to and including p64, was approved for issue by the Board on 15 March 2021 and signed on its behalf by:

Sally Johnson
Chief Financial Officer

G Glossary

Across Pearson we have language and terminology that is unique to us and to our sector. To help you navigate this, we have continued to include a glossary of key terms, products and services. Any words or terms marked with the 'G' symbol are defined in the section, found at the back of this report.

Learning. For life.

We are building direct to consumer relationships with millions of people around the world, across a lifetime of learning.

Sidney Taurel, Chair

I believe the pandemic has helped bring us closer together, and I am immensely proud of the way Pearson's employees across the world have united through this difficult situation to support each other and our customers.

Andy Bird, Chief Executive

We intend Pearson to be the world's preeminent learning company, delivering the world's best learning products to more people than ever before. This is good for our business, and it is good for the world. Because, when we demonstrate the value of learning, we grow our business and transform lives.

Sally Johnson, Chief Financial Officer

2020 was a challenging year for society and many businesses, Pearson included. That said, we delivered a resilient sales performance in light of these circumstances and a profit performance in line with revised expectations post COVID-19. In 2021 we expect Group revenue to grow and profit to be in line with market expectations.

Discover more online

pearsonplc.com

Use this QR code to visit our newly launched corporate website, where you can also find the online version of our 2020 annual report and accounts.

Pearson at a glance

We are Pearson. Our purpose is to help everyone achieve their potential through learning.

We are the leading learning company offering end-to-end solutions, enabling greater access to high-quality, affordable learning experiences. We are the global experts in learning.

c.200
countries

20,000+
employees

We enable **tens of millions** of learners per year to maximise their success.

Our businesses

Learn more: Our five new business divisions, p20

Our five new business divisions, coming into effect in 2021, are the foundation for the long-term growth of Pearson, all of which will be supported by our new Direct to Consumer group.

FIVE BUSINESSES TO DRIVE GROWTH

VIRTUAL LEARNING	HIGHER EDUCATION	ENGLISH LANGUAGE LEARNING	WORKFORCE SKILLS	ASSESSMENT & QUALIFICATIONS
p20	p21	p22	p23	p24

Direct to Consumer

Enabling sustainable growth

Driving shareholder value

Contributing to a more equitable world

Our commitment to sustainability and learner outcomes

Learning for a better life, a better world

Our Sustainable Business Plan 2030 supports our business strategy and drives positive outcomes for people from all backgrounds, our global community and planet.

Learn more: Sustainability, p40

Improving learner outcomes

We design our products to drive learning outcomes. When we demonstrate and deliver the value of learning, we can grow our business and help people achieve their potential.

Learn more: Learner outcomes, p26

Key performance indicators (KPIs)

FINANCIAL MEASURES

Sales (R)
£3,397m

£million	
20	3,397
19	3,869
18	4,129
17	4,513
16	4,552

Adjusted operating profit[1] (R)
£313m

£million	
20	313
19	581
18	546
17	576
16	635

Net debt[1]
£463m

£million	
20	463
19	1,016
18	143
17	432
16	1,092

Adjusted earnings per share[1] (R)
28.7p

pence	
20	28.7
19	57.8
18	70.3
17	54.1
16	58.8

Operating profit/loss[2]
£411m

£million	
20	411
19	275
18	553
17	451
16	-2,497

Basic earnings per share[2]
41.0p

pence	
20	41.0
19	34.0
18	75.6
17	49.9
16	-286.8

Operating cash flow and cash conversion[1] (R)
£315m

£million	
20	315 (101%)
19	418 (72%)
18	513 (94%)
17	669 (116%)
16	663 (104%)

Net cash generated from operations[2]
£450m

£million	
20	450
19	480
18	547
17	462
16	522

Dividend per share
19.5p

pence	
20	19.5
19	19.5
18	18.5
17	17.0
16	52.0

Total shareholder returns[3] (R)
10.65%

%	
1-year TSR	10.65%
3-year TSR	0.18%
5-year TSR	13.08%

1 See pp33–35 for an explanation of these alternative performance measures.
2 Equivalent statutory measure.
3 Source: Bloomberg.

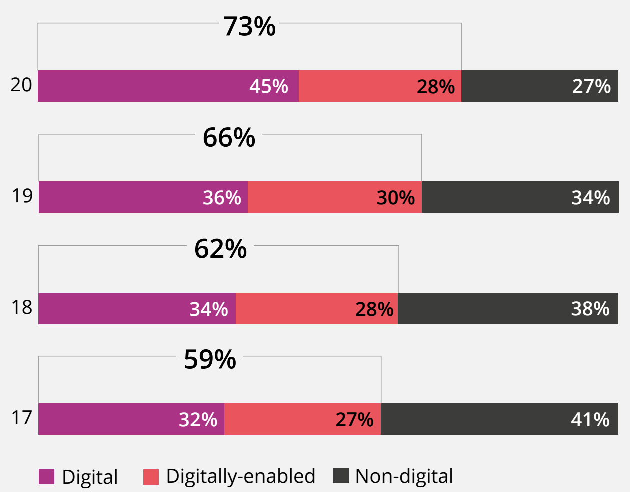
Note: See pp212–216 for full reconciliation of the alternative performance measures to the equivalent statutory measure.
Note: IFRS 16 adopted in 2019 – no KPIs have been restated for historical accounting adoptions.

Read more:
(R) See how we link strategy to management reward p100

Learn more online:
plc.pearson.com/en-GB/purpose/our-targets-kpis

BUSINESS MEASURES

Digital revenue[1]



1 Excludes GEDU, Wall Street English (WSE) and US K-12 Courseware. GEDU was sold in 2017, WSE was sold in 2018; US K-12 Courseware was held for sale in 2018 and was sold in 2019.

Performance in our businesses in 2020

Global Online Learning

18%*	Virtual Schools enrolment growth (new and existing schools)	43%
	OPM G underlying course enrolments growth (excl. discontinued programs)	20%

Global Assessment

(14)%*	Testing volume decline	(22)%
	Online proctoring growth G	1,143%

North American Courseware

(13)%*	Digital registrations growth (including eTexts)	9%
	Inclusive Access G sales growth (to not-for-profit institutions)	29%

International

(19)%*	PTE Academic G test volume	(36)%

* Year-on-year underlying revenue growth for 2020.

NON-FINANCIAL MEASURES

Employee experience and engagement[2]

p49

Employees rating our COVID-19 response on a scale of 1 (poor) to 10 (excellent)[2]	8.6
Employees who would recommend working at Pearson to a friend or colleague	+17 NPS
Employees who have done something to reskill or upskill in 2020	63%
Employees working from home effectively shortly after closing offices due to COVID-19	87%

2 Data from Pearson's employee 2020 quarterly pulse survey.

Reduce our carbon footprint

	2020	2019	2018
Total tCO_2e – Scope 1, 2 (market based) and 3	354,162	580,914	614,380
% reduction vs previous year	39%	5%	
% reduction vs 2018 baseline	42%	5%	

Female representation

	2020	2019
Board of Directors	45%	33%
Senior leadership[3]	36%	34%
All employees	60%	59%
GB median gender pay gap	10%	12%

3 Typically, two reporting lines from the Chief Executive.

Improve racial and ethnic diversity

	2020
Board member – Directors of colour	1
% US black employees at manager level and above	3.3%
% US Hispanic/Latino employees at manager level and above	3.8%
% UK black employees at manager level and above	1.7%

We have enhanced our employee data collection to report on racial and ethnic diversity KPIs in our two largest markets for the first time in 2020 and aim to expand this globally. We will track progress going forward with a target of achieving employee diversity that is representative of the diversity in the countries in which we operate.

Chair's introduction

Our vision is to be the leading learning company in this increasingly interconnected world.

Sidney Taurel
Chair

Dear shareholders,

2020 will go down as one of the most unprecedented and challenging years in modern history. It has impacted us all in ways we would have scarcely imagined possible before. Yet, among the ongoing uncertainty, it is heartening to see so many examples of people supporting one another – from families and local communities through to the broader business world and beyond. I am particularly proud of the way Pearson's employees have supported each other and all our stakeholders through this difficult time.

The pandemic has also acted as a catalyst for driving innovation, as we find new and more efficient ways of working, connecting and communicating. This is characterised by the rapid response from the scientific world in mobilising to provide a world-class testing and vaccination response. It can also be seen in the learning sector, through the speed and scale in which learning has moved online.

In time, I know the world will normalise, but my hope is that the appetite for innovation and technological disruption will continue unabated. This provides opportunities for companies such as Pearson to grow, contribute to society and create shareholder value.

Performance and progress in 2020

In a year that has been incredibly challenging from an operational and financial perspective, I am encouraged that we were able to achieve both sales and adjusted operating profit in line with the revised expectations that we laid out in March in response to the pandemic's impact.

Notably, Global Online Learning sales grew significantly as appetite for, and interest in, online learning surged. The more negative impact of COVID-19 has been seen most keenly in International and Global Assessment due predominantly to test centre and school closures. It is encouraging to see US Higher Education Courseware performing in line with pre-COVID-19 expectations, with digital sales in US Higher Education Courseware now accounting for more than 70% of total sales in this division, and eText growth increases indicating that we are recapturing sales that were lost to the secondhand book market.

Uncertainty persists into 2021 due to COVID-19 but, given progress with the global roll-out of vaccines, we are currently planning on the basis that test centres will reopen, in a socially distanced fashion, during April, and that normal operations will resume in H2 2021, including borders reopening. As such, we expect to deliver financial results broadly consistent with market expectations.

COVID-19 response and engaging with our stakeholders

We are proud to have played our part in supporting our employees, customers, partners and broader stakeholders during the pandemic. The Board held an additional unscheduled meeting in mid-April to consider financial scenario planning and the company's broader response to the pandemic. We responded in four key ways:

Supporting employees

The Board discussed the potential to access government funding and take advantage of the furloughing programme. We ultimately decided against this option, knowing others were in more acute need of support. Although areas of our business were impacted by school and centre closures, we eschewed layoffs and instead, where possible, we redeployed our employees to high-growth areas of the business, such as online learning. We fostered employee engagement and support groups and aimed to support our employees across the world as best we could. You can read more on this approach in our stakeholder engagement section on p27

Supporting customers

Our customers around the world were required to move rapidly online, in many cases in just a matter of days. We made the decision early on to make some of our popular digital materials and content available for free to them in the early months of the pandemic, to help enable the process of moving to digital learning. The feedback we received was highly positive and we believe this will lead to deeper, more durable long-term relationships. Read more on p13

Supporting shareholders

In April, the Board felt it appropriate to pause the share buyback that launched at the beginning of the year, given the deeply uncertain times ahead. Another key decision for us was whether to pay the final 2019 dividend. Ultimately, the Board and I decided that, due to the strength of our balance sheet, our strong financial position and liquidity and our confidence in the outlook in the post-pandemic world, the right decision was to proceed with a recommendation to pay it. We performed financial stress testing and scenario planning and concluded that, even in a worst-case scenario, we would still have sufficient liquidity. Our shareholders rely on dividends and we strongly believed it was the responsible thing to do, as a reward for your support and loyalty.

Supporting broader stakeholders

The Board and I recognised there were many in society in urgent need of direct help and we came to the decision that myself, the Board and Executive Directors would take a temporary, voluntary reduction in pay and fees. This was then donated to charities engaged in COVID-19-related activities.

This package of support was the right thing to do, reflecting the financial strength of the business, and it was also a demonstration of the capabilities that Pearson has successfully created as we have transitioned from print to digital.

I believe that, long after this dreadful pandemic has passed, there will continue to be sustainable interest in online learning globally, and we are well placed given our investment and global leadership in this area.

New leadership for the next phase of Pearson's story

Further to our announcement at the end of 2019, John Fallon retired from the role of Chief Executive in 2020. John's career with Pearson spanned over two decades, including seven years as Chief Executive, and his passion and commitment to the business was evident to all of us.

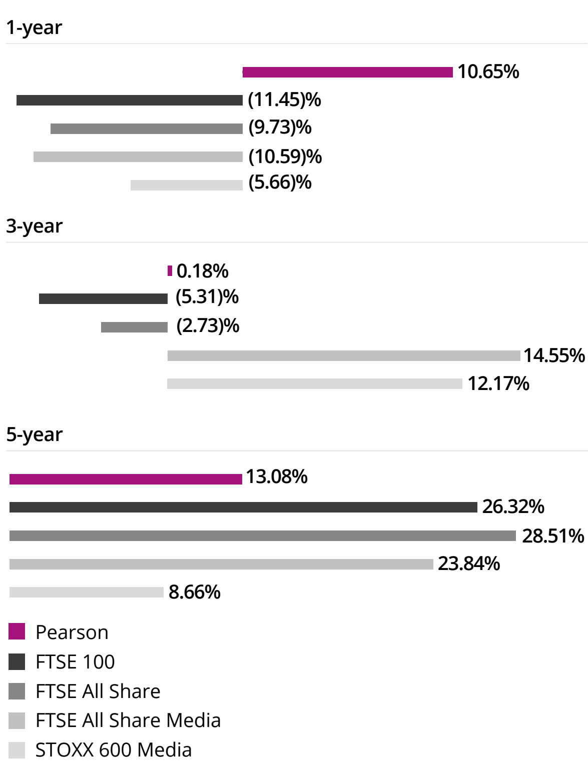
As Chief Executive, John worked tirelessly leading Pearson through a period of significant change and led its transformation from a media conglomerate to a single focused learning company with a strong technology platform.

John's hard work and vision established the foundations for Pearson's next chapter. On behalf of the Board, I would like to thank him for his considerable contribution and dedication to Pearson and wish him well for the future.

KEY PERFORMANCE INDICATOR | FINANCIAL MEASURES

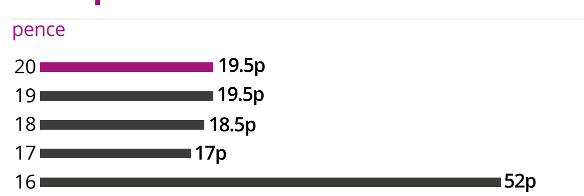
Deliver sustainable returns

Total shareholder returns



Dividend per share

19.5p



Chair's introduction

The Board ran a thorough and rigorous search process for John's successor, with strong governance, interviewing a broad range of very high-calibre candidates. We were delighted that this resulted in the appointment of Andy Bird, who became Chief Executive in October 2020.

Andy was the standout candidate from a very strong field given his wealth of international consumer experience, digital and brand-building expertise, excellent people engagement and leadership skills, proven ability to create value – and his affinity to Pearson's culture and values.

He is a proven, visionary leader of a large, complex and diverse business, and an outstanding executive who is well placed to build on the foundations laid at Pearson, to enhance long-term value for all our shareholders. Further, as an existing Board member who joined us in May 2020, his knowledge of Pearson meant he has been able to hit the ground running.

We are very grateful and appreciative for the engagement, time and support of our shareholders in ensuring we were able to appoint the right candidate. You can read more directly from Andy in the following pages, and more on the process of appointing Andy in the Nomination & Governance Committee report on p84

Our strategic direction

The Board and I have been impressed with the early impact that Andy has made and we are optimistic regarding the future growth prospects of the company, noting the sense of pace and momentum that is building.

We believe that the accelerating consumer demand for new digital forms of learning provides a real opportunity for us and we are supportive of management's focus on the direct to consumer market.

The Board supports the reorganisation of Pearson into five global business divisions, recognising that this will help drive our future growth and build on the structure we had in place throughout 2020. The Board and I are also supportive of actions announced to hold a review of our portfolio to focus on the priorities in these five new divisions.

As management articulates this strategy and executes on it over time, I believe there is a big opportunity to grow our business in exciting new areas, while also continuing to focus on existing products and services that are either growing quickly or now stabilising after several years of transition.

You can read more on this in Andy's overview, as well as the business model pages of this document found on p16

Underpinned by a strong financial position

To achieve our strategy and to endure into the future, it is vital to have a strong balance sheet. Despite challenging macro conditions, the Board is confident about Pearson's medium- and long-term prospects, and the opportunities that exist in our business, particularly viewed through the lens of our evolving strategy, putting consumers at the heart of all we do.

Our capital allocation policy remains unchanged – to maintain a healthy balance sheet, invest in the business both organically and inorganically, pay a progressive and sustainable dividend and return any remaining funds to shareholders.

In terms of any investments we make, we will always be disciplined and focused on the returns profile, and under the Board's direction, we have introduced enhanced internal processes to measure and manage organic returns. Any future inorganic investment will have equal discipline and scrutiny.

Shareholders will be aware that, as a result of the uncertainty due to the pandemic, we took the decision in March 2020 to pause the £350m share buyback programme that we launched in January last year, with around £176m of the shares on offer completed. This decision, taken by the Board, reflected the fact that, while we do have a strong balance sheet with good headroom in liquidity, in unprecedented times we must make prudent decisions for the long term. At this point we believe maintaining a very strong balance sheet is appropriate. As such we are not planning to reinitiate the buyback. We will keep our balance sheet strength and potential for surplus cash returns under review, but do not see this in the immediate horizon.

We have proposed a final 2020 dividend of 13.5p, resulting in a full year dividend of 19.5p. This is reflective of the strength of our balance sheet, consistent with our approach to maintain a sustainable dividend, and our confidence in the future growth potential of the business.

Pearson retains significant financial headroom with net debt of £463m and immediately available liquidity of £1.9bn through committed facilities and cash balances.

ESG, diversity and building a sustainable business

Our historic commitment to embed sustainability into all business functions and operations remains unchanged. Since launching our Sustainable Business Plan 2030 last year, we are focused on the most material environmental, social and governance (ESG) issues and know this work will only bolster our strategic objectives.

The Board has been engaged on overseeing plans and progress towards our sustainability ambitions. I am pleased with the progress we made last year, particularly in advancing equity through the launch of our social bond (see p44 for more on this) and our ambitious goals on reducing emissions.

We are also strengthening our approach to reporting and transparency by undertaking work towards the Task Force on Climate-related Financial Disclosures (TCFD) and the Sustainability Accounting Standards Board (SASB). You can read more about our approach in the sustainability section on p47 and p54

The Board is committed to improving our focus on Diversity, Equity & Inclusion (DE&I). In this annual report we have expanded our reporting to include not just gender diversity but also ethnic diversity at company and Board level, as we commit to trying to continually strengthen this vital area. We know that diverse perspectives help broaden thinking and lead to improved performance and better ways of working.

> **We believe that Pearson's talent and content should reflect the diversity of the markets we serve,** ensuring we create the best products, with the greatest impact, for the greatest number of people in the world. We believe that Pearson must have a positive impact on our customers' lives, on the communities that we serve, and on the world of learning globally.

Specifically, the Board and I were supportive of the formation of a DE&I task force of employees and leadership, with the aim of coming together to identify concrete, actionable ways to improve recruitment, retention and inclusion, and to ensure our products and services help build a more inclusive society. We have adopted a set of stretching goals around representation, company culture, product, and our role in society. An action plan comprising goals, pillars for action and initiatives for implementation over the next 12 to 18 months underpins our commitment. You can read more on this on p50

Board composition and engagement

It has clearly been a difficult year for in-person stakeholder engagement in 2020, given the pandemic. However, our Board continued to engage virtually with, and encourage participation from, employees, educators, learners, community and thought leaders, as well as other stakeholders to ensure the company is contributing to wider society. More broadly, the Board remains fully committed to shareholder and broader stakeholder engagement and we welcome ongoing dialogue with all of our investors. Read more on our stakeholder engagement response in the S172 section on p30

The Board continues to benefit from a diverse and wide range of backgrounds, skills and experience. You can read more about this in the Governance report p73

As noted in last year's report, 2020 also saw a change of Chief Financial Officer at Pearson. Sally Johnson, our former Deputy CFO, was appointed CFO in April 2020 following our Annual General Meeting (AGM). Sally has had an immediately positive impact with her deep knowledge of the business and the markets we operate in, her financial acumen, her leadership skills, and her incredible work ethic. I am delighted to have her on our management team and Board.

We have also had further changes to the makeup of the Board which you can read about on p67

Achieving our vision and delivering on our strategy

Our vision is to be the world's leading learning company. In the increasingly interconnected world we live in, this vision is highly relevant and the products and services we offer are increasingly in demand. This heightened demand is being seen from consumers around the world who want access to high-quality digital learning experiences to help them progress in the next stage of their lives – whether that be formal education, upskilling or changing career path.

As you will hear from Andy later in these pages, and from the updated strategy that is articulated in the strategy section on pp18–25, we believe learning is fundamental to everything we do as humans and that we continue learning across our lifetimes, increasingly via direct to consumer means. We believe that everyone in the world should have the opportunity to learn, because learning transforms lives and societies. Pearson has long understood the value of learning and we believe we have a unique opportunity to enable greater access to high-quality, affordable learning experiences – and we are supportive of management's determination to realise that ambition.

The Board and I are keen to engage with our shareholders as circumstances allow.

Thank you for your ongoing support.

Sidney Taurel
Chair

Chief Executive's strategic overview

> We believe that everyone in the world should have the opportunity to learn, because learning transforms lives and societies.

Andy Bird
Chief Executive

Dear shareholders,

I am delighted to be writing to you as Pearson's new Chief Executive, a journey that started in May 2020 after joining the Board as a Non-Executive Director. I am fortunate to have had such a comprehensive induction to the business before taking over the reins from John Fallon. I would like to express my sincere gratitude to John, for his help in ensuring a smooth transition, for all that he did for Pearson, and for the strong foundations that he has laid for our future.

Pearson understands the value that learning brings to people's lives and the profound impact it has on the world; I have a deep passion for learning and am enormously excited about the opportunity ahead, particularly Pearson's potential to reach many more people. My experience, at consumer-focused companies such as Walt Disney and Time Warner, has equipped me with the expertise to lead Pearson through the next chapter, as it accelerates its transition to becoming a digital-first company with the consumer at the heart of everything we do.

Since joining Pearson, I have immersed myself in every conceivable aspect of the business and have been impressed by the progress that has been made over the last five years. Disappointing financial results during this time, and the complexity of the company and our operating model have obscured the vital purpose and true strengths of Pearson, and of the talented people who work here. There is still much to do but I am confident that we have a strategy that will return this business to sustainable, long-term growth.

Our market

As we embark on the fourth industrial revolution, learning is more vital than it has ever been. We believe that everyone in the world should have the opportunity to learn, because learning transforms lives and societies. Pearson is well positioned to support people in developing the skills they need to participate in the new economy, to support this unprecedented societal shift, and therefore to capture the enormous growth potential in the market.

The global learning market is vast – at around £5tn today, growing to over £7tn by 2030. Formal primary, secondary and tertiary education is 75% of that market and will remain the vast majority – we expect over a billion more learners to have moved through formal education by 2030. A growing global middle class and longer careers are also driving lifelong and informal learning, particularly for reskilling and upskilling, a trend that has been accelerated over the past year. This all adds up to huge structural tailwinds in our industry, and great opportunity for companies that can innovate and scale to meet the growing and changing demands of learners globally. There is a huge opportunity for Pearson, as only 3% of the £5tn learning market is currently digital.

COVID-19 has accelerated the trend to digital-first in every part of our lives. Millions more people are connected to the internet. There's been massive disruption to the world's workforce. Governments and businesses need their people to learn new skills to survive and thrive. And learning is the key to that change, and to the new opportunities it creates.

Also, how we learn is changing, driven by technology and new consumer habits. Consumers now focus on quality, accessibility and the return on their time. They want personalised, enjoyable experiences, on demand, wherever they are. They want to track and prove what they've learned, and to realise its value in their careers and lives. And, just as consumer habits have changed in other industries such as music and television, so, the business of learning is also changing: more direct to consumer, more unbundled, and more skills-based.

This does not mean that we will be abandoning our traditional markets in education, or our deep relationships with institutions. Those will remain the foundations of our business and of our future. Those markets and institutions themselves are changing to meet the needs of their consumers – and doing so in partnership with us. But we must also go where consumers want to go: into a lifetime of learning that helps them to keep pace in a rapidly changing world.

Our strategy

The market drivers outlined above create three big global opportunities for Pearson – the rise in online and digital tools for schools and education, the workforce skills gap, and the growing need for accreditation and certification – and we are strategically well placed to capitalise on these opportunities. To achieve this, we are reorganising our business and operations to focus on five business divisions to release untapped value and potential within the company.

Direct to Consumer group

Our new Direct to Consumer group will act as Pearson's in-house centre of excellence for the delivery of our consumer strategy.

The group sits across all five divisions and will be the delivery of our consumer strategy going forward. It will enable the constant flow of new products across our business moving forward which will drive a significant part of our future growth.

Five business divisions to release untapped value and potential within the company

Our five new business divisions are Virtual Learning, Higher Education, English Language Learning, Workforce Skills, and Assessment & Qualifications – all of which will be supported by our new Direct to Consumer group.
Read more on this in our strategy pages on pp18–25

These five divisions will form the foundation of the company. They are great businesses with excellent growth potential. They reinforce each other and will be the platform on which we build our direct to consumer vision. We want everyone in the world to realise the value and joy of learning. And we will help the world's learners at every stage of life to unlock their potential in a rapidly changing world.

Streamlining our portfolio to become a truly digital company

Pearson has made good progress in rationalising its portfolio over recent years but there is still some way to go. We will therefore streamline our portfolio to focus on the priorities of our five new businesses, and on our mission to become a globally scalable digital company. This will not happen overnight. We will ensure that any disposals or new acquisitions support the strategic focus of the company, maintain the health of our balance sheet and deliver the best return for our shareholders. We are currently launching a strategic review of our international courseware local publishing businesses. We will report back on this later in the year.

Drivers for success

There are six key reasons why I believe we will succeed:

1. The value of our recent investments, including in the Pearson Learning Platform (PLP) G, can now be realised.
2. We are the global experts in learning. Nobody else has the breadth and depth of experience, expertise and relationships across the entire lifelong learning spectrum.
3. We are home to the best talent, from our amazing, passionate and dedicated employees to our brilliant authors.
4. We are one of the few companies who can offer end-to-end learning solutions.
5. We have a competitive advantage in the integration of our intellectual property, content, products and assessment tools.
6. Our response to the pandemic demonstrated how agile Pearson can be. The company responded rapidly to the needs of people, schools and governments around the world.

Chief Executive's strategic overview

Strengthening our culture

In any organisation, the internal always determines the external. At Pearson we have committed employees who really care about education and learners, who understand every dimension of learning and who understand how learning improves people's lives. We see exciting opportunities to evolve our culture to capture the full potential of the talented people who work at Pearson, based around the four key themes of: putting the consumer at the centre of everything we do; embracing diversity, equity & inclusion; collaborating across businesses and territories as one global company; and increasing our speed, agility and focus on quality.

Increasing our societal impact

Pearson has an important role to play when it comes to helping address the inequality of opportunity in learning around the world. Our recent work to promote access and inclusion in learning includes the launch of our social bond earlier this year, tied to improving learning outcomes for people across the world who need it most. We are continuing our efforts to achieve diversity across both our employee base and within our content through representation. We have developed a roadmap to become net carbon zero; and we are also enhancing our reporting structures and are reporting according to Sustainability Accounting Standards Board (SASB) for the first time this year.

Being a sustainable business will contribute to Pearson's future growth and we are committed to making a positive impact. Read more on our approach and our Sustainable Business Plan 2030 in the Sustainability section of this report, on pp40–55

Andy Bird discusses Pearson's strategy at the full year 2020 results

MARKET OPPORTUNITIES

The rise in online and digital tools for schools and education	The workforce skills gap	The growing need for accreditation and certification

Our guiding principles

Our strategy reflects a new vision for Pearson and incorporates a simpler, more agile operating model focused on three global market opportunities where we can leverage our existing expertise, build on our investments in technology, and strengthen our areas of competitive advantage to reposition Pearson towards sectors and opportunities that offer strong inherent growth characteristics. All of this will be achieved with our new guiding principles:

- We will put the consumer at the centre of everything we do and provide them with the highest quality and best value products
- We will only be in businesses that will drive growth, scale, profitability and shareholder value
- We will have the capabilities to deliver, including an entrepreneurial culture, diverse talent and effective technology
- And finally, we will move with speed and agility

What the future holds

This is an exciting time for Pearson and I believe that our future success will be driven by the following five things:

1. The learning market is vast and growing, and 2020 was the catalyst to help both individuals and organisations change the way they saw the need to learn and change how they learn
2. Pearson has great assets, and the investments we have made in our technology will enable us to grow our existing businesses and make them even more valuable
3. We will build direct relationships with our consumers that allow us to support them across their entire lifetime of learning
4. We can help companies address the persistent skills gaps and massive shifts in the workforce that they face, which opens up a huge new market for us
5. We have a unique competitive advantage. No one else can offer the highest quality content, the best digital products and delivery, and the world-leading assessment capability that the market and our consumers demand

Simply put, we intend Pearson to be the world's preeminent learning company, delivering world-class learning products to more people than ever before. This is good for our business, and it is good for the world. Because, when we demonstrate the value of learning, we grow our business and transform lives.

I look forward to the journey ahead and sharing our progress with you as we go.

Thank you for your support of Pearson.

Andy Bird
Chief Executive

Our strategy and business model

Use this QR code to visit our strategy and business model page on our newly-launched corporate website.

Living our values: our response to COVID-19

Supporting our customers

We made the decision early on that it was the right course of action to help customers the best we could by taking their courses and classes online – on a free bases initially – to help cope with the crisis and help keep them learning.

We increased the safety of our test centres by following social distancing measures.

We believe that our early decision to help our customers in their time of need will lead to strengthened, more durable long-term relationships with our customers.

UK

3.6m+

school children accessed subscriptions to **ActiveLearn** online resources

480,000+

parents accessed Carol Vorderman's **'The Maths Factor'**

500,000+

people accessed upskilling and reskilling opportunities on **UK Learns**

US

100,000

K-12 students were offered free access to our online courseware and learning platform through state-level district partnerships

1.5m

people viewed our **online learning hub** to help adjust to online learning

Global

500+

Pearson VUE G -owned **professional testing centres** opened to help thousands of key workers qualify and provide front-line healthcare support

Supporting our people

With the onset of the pandemic in early 2020, we acted quickly to support our 20,000+ employees, helping them feel connected and safe as the majority of them found themselves suddenly working from home full time.

People of **Pearson**

We launched an employee engagement community for employees to connect, share stories and support one another.

You can meet some of our talented colleagues throughout this report in the **People of Pearson** callouts.

COVID-19 Online Community

We launched an online community to help employees navigate their 'new normal'. Events included:

- Regular virtual town halls and leadership engagement events
- Weekly virtual coffees and manager meet-ups

Our new quarterly pulse survey found that employees appreciated our response and support during the year.

Learning at Work Week

More than 11,000 employees took part in our first global Learning at Work Week, during which we hosted a virtual programme of speakers and seminars.

Employee value proposition

We are currently focusing on embedding our employee value proposition in everything we do, with the aim of building a more inclusive learning culture in order to attract and retain the world's best talent.

Market context

A vast, expanding market

The fundamental growth drivers of the education market remain robust

- Accelerating adoption of digitally enabled learning across all lifelong learning journeys
- Increased attention on employee training, upskilling and reskilling to meet evolving labour market needs, often with government-led initiatives
- Emerging trend of people looking for alternative credentials
- Parents spending more on direct to consumer education services

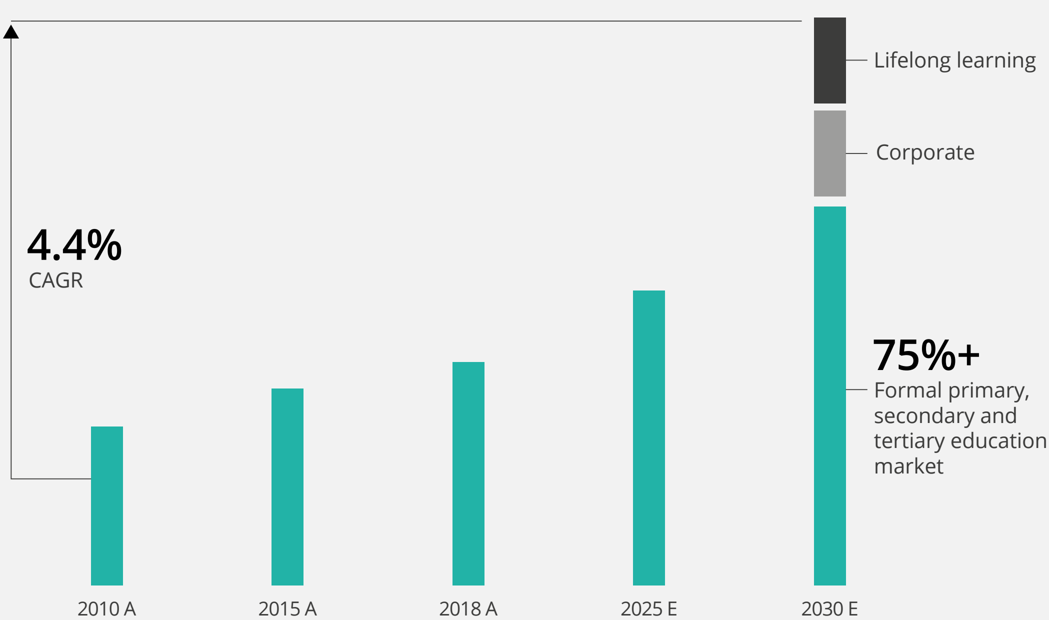
The global learning opportunity

£7tn
expected size of the learning market by 2030

2nd
largest component of GDP in most countries

+1bn
We expect over a billion learners to have moved through formal education by 2030

The £5tn global learning market



Global Learner Survey 2020

Pearson's Global Learner Survey reveals that people see longevity in online learning, increasing demand for digital skills and equity as one of education's biggest issues

Learning is forever changed

77%

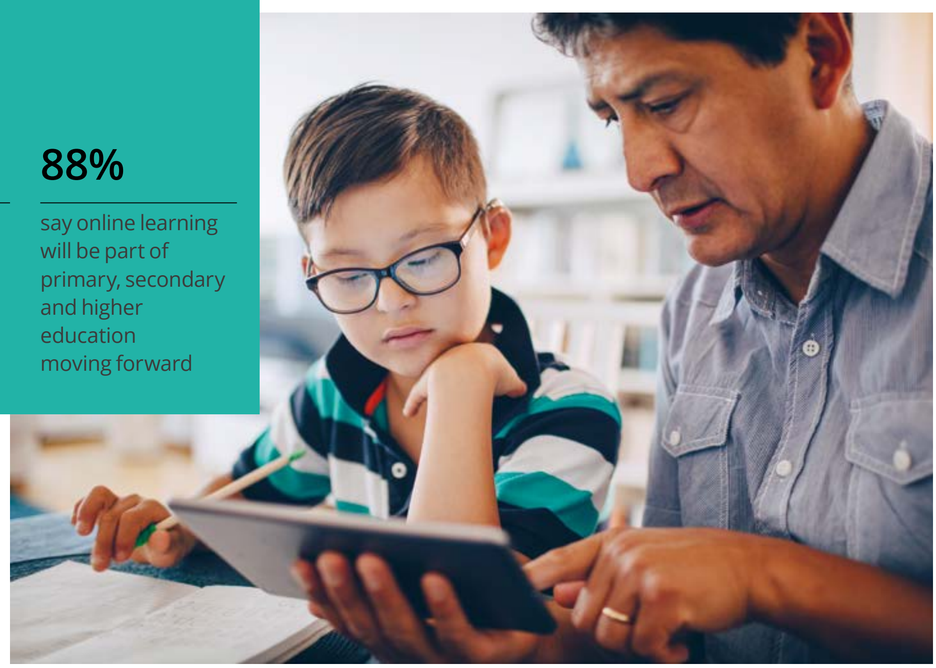
of learners believe that education will fundamentally change because of COVID-19

66%

agree that the education system in their country has done a good job adapting during the pandemic

88%

say online learning will be part of primary, secondary and higher education moving forward



Getting schooled on the new economy

77%

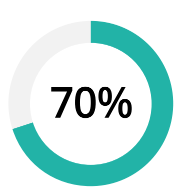
say teleworking has taught them that digital work requires new skill sets

- Virtual collaboration
- Communication
- Analysing data
- Managing remote teams

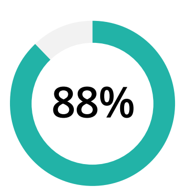
87%

agree that colleges and universities should offer shorter courses or lower-cost options to help those who are unemployed

Learners demand equity now



believe that the pandemic will deepen education inequality, especially among young students



want schools to do more to address equality issues

- More tech for underserved learners
- Better prep for emergency use of online learning
- More academic resources
- More remote learning solutions

Our business model

Our value creation model

Our foundations

Committed people and partners

From our amazing, passionate and dedicated employees to our brilliant authors, we are the home for the best talent. We have a broad range of partners across our business who we expect to share our Pearson values. Our relationships with governments, customers, non-governmental organisations (NGOs) and other global organisations help us to increase our impact on consumers around the world.

R&D and product innovation

Our global product team, with expertise in learning science, has a focus on learning outcomes. Through ongoing innovation and Research and Development (R&D) we are committed to creating learning products which offer a great user experience (UX) and that demonstrate measurable learning progress.

Financial assets

Our shareholders entrust us with their capital in order to invest on their behalf for the long term.

Our physical footprint

We have a presence in c.200 countries around the world and are focusing on simplifying our property portfolio to enable digital and flexible ways of working.

What we do

We're the **global experts** in learning

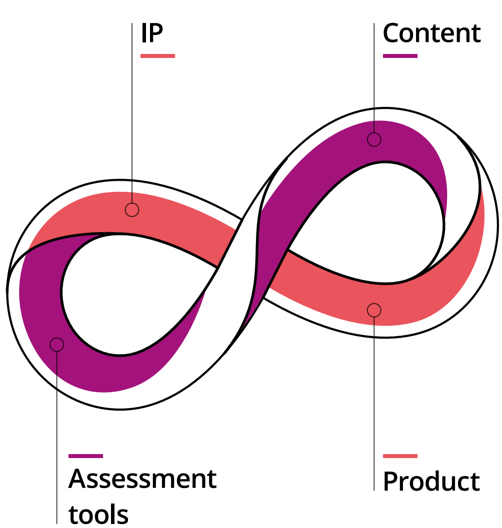
Nobody else has the breadth and depth of experience, expertise and relationships in learning. We enable tens of millions of learners per year across the world and the entire learning spectrum.

We're the only company to offer **end-to-end learning solutions**

From identifying a person's learning needs and helping them to achieve them, to assessing their performance and granting credentials. We create Intellectual Property (IP), turn it into compelling content, and then leverage it as we build the tools for teaching and assessment.

An **integrated** business

Our competitive advantage is the integration of our IP, content, products and assessment tools across our five businesses – a continuous flywheel that makes each part of our business more valuable. For example, we create the most effective and valuable learning tools and experiences for learners of all ages. We develop the exams and assessments to test their performance and then we certify their achievement so that they can prove what they've learned.



Learn more:
Our strategy and five new business divisions, pp18–25

Value we create

Consumers
We provide superior learning products and services to meet the needs of consumers all over the world.

Employees
We intend to maximise the value of Pearson's own human capital, by giving our people as many opportunities to learn as possible, enabling our employees to grow, develop and succeed.

Employers
Companies are the universities of the future. Our aim is to partner with more employers to create shared success and to ensure more people succeed in the future world of work.

Educators
We work with teachers, instructors, faculty and educators across all stages of education to improve outcomes, grow and succeed together.

Governments
We partner with governments at a local, federal and national level to create learning solutions for people around the world.

Shareholders
We aim to provide long-term shareholder value creation.

Business partners
Our long-term business partnerships are built on shared values, deep relationships and mutual trust.

Learn more:
Creating value for our stakeholders, pp27–29

Society
Education plays a crucial role in society and Pearson is a driving force behind the evolving education market as we look to meet the changing needs of today's learners, not just in this moment but for the foreseeable future.

Planet
We have a roadmap to become net carbon zero across our global business and we are enhancing our reporting structures, reporting according to Sustainability Accounting Standards Board (SASB) principles for the first time this year.

Learn more:
Sustainability, pp40–55

Our strategy

Repositioning Pearson for growth to seize the global opportunity

MARKET OPPORTUNITIES

- The rise in online and digital tools for schools and education
- The workforce skills gap
- The growing need for accreditation and certification

THREE PRIORITIES TO UNLOCK GROWTH

- Consumer focused & data-led approach
- Portfolio & Organisational structure
- Talent & culture

FIVE BUSINESSES TO DRIVE GROWTH

- VIRTUAL LEARNING p20
- HIGHER EDUCATION p21
- ENGLISH LANGUAGE LEARNING p22
- WORKFORCE SKILLS p23
- ASSESSMENT & QUALIFICATIONS p24

Direct to Consumer

Enabling **sustainable growth**

Driving **shareholder value**

Contributing to a more **equitable world**

GUIDING PRINCIPLES TO BENCHMARK SUCCESS

- Consumer at the centre of everything we do
- High-quality, affordable products leading to better access and outcomes
- Scalable, global and digital-first businesses that are profitable and will drive shareholder value
- Entrepreneurial culture, diverse talent and effective technology
- Speed and agility

Our five new business divisions

We are reorganising Pearson to focus on five new business divisions[1], all supported by our Direct to Consumer group. Each division will have full responsibility for its overheads, product development, and operations to enable a more agile and transparent operating model, and each will be linked to the others through our shared IP and capabilities.

Divisions	VIRTUAL LEARNING	HIGHER EDUCATION	ENGLISH LANGUAGE LEARNING	WORKFORCE SKILLS	ASSESSMENT & QUALIFICATIONS
Units	Virtual Schools Online Program Management (OPM) G	US Higher Education Courseware Canadian Higher Education Courseware International Higher Education Courseware	Pearson Test of English G Institutional Courseware English Online Solutions	BTEC G Pearson College Apprenticeships	Pearson VUE US School Assessment G Clinical Assessment UK GCSE and A Level International academic qualifications

Direct to Consumer

Virtual Learning

Pearson's Virtual Schools are an accredited, online public and private school programme providing personalised learning and a high-quality alternative to bricks and mortar schools.

Our OPM business helps people choose and study the right course to enhance their employability prospects, and universities and colleges to expand their reach by taking courses online.

Revenue

£0.7bn

2020 revenue

Market size

£1.5bn

Virtual Schools, US market

£2.8bn

OPM global market, 2021

Virtual schooling is a £1.5bn market in the United States alone, with market growth of high single digits pre-COVID-19. In 2019, the total US virtual school enrollment was around 400,000 students, which represented only 1% of the entire K-12 population. We believe the total addressable market will continue to show good growth as more school districts retain online schooling post-COVID-19 and as more parents opt for virtual schooling permanently, growing that market size beyond the 1% that it is today. We have a 17% share of the market today and are present in 29 of the 34 states that currently allow virtual public schools. In 2020 our Virtual Schools revenue was £413m following significant growth of 29%, driven by COVID-19.

In OPM we continue to expand our relationships with institutions to be broader in scope; we will leverage our in-house digital marketing agency across other parts of the business; and, we will accelerate our Pearson Pathways strategy to grow our presence in lifelong learning. The global OPM market, at £2.8bn today, is expected to grow to over £7bn as consumers increasingly turn to online course solutions in 2020 our revenue in OPM was £0.3bn.

1 The divisions presented here exclude the international courseware local publishing businesses which are under strategic review.

Higher Education

We offer high-quality digital content to college students focusing on experience, outcomes and affordability.

Revenue

£0.9bn

2020 global revenue

Market size

£4–5bn

US Courseware market

The US higher education courseware market is valued between £4bn and £5bn, and we are the leading player with revenue of £0.8bn in 2020. We partner with thousands of leading authors, across multiple subjects, with a very strong focus on science, technology, engineering and mathematics (STEM). We're accelerating our move to digital and we have an opportunity to recapture the secondary market in Pearson textbooks. The PLP and the products we are developing on it will drive digital growth. To accelerate recapture from the secondary market and build direct relationships with consumers, we are going to launch a new college study app in the autumn of 2021 which will be competitively priced, flexible, and a tiered service, which will enable us to shift consumer purchasing preference to our own platform.

PEARSON REVEL **OUR FOCUS ON LEARNER OUTCOMES**

Essential programming

Improving outcomes through Revel G: Introduction to Java Programming

Learn more online:

Pearson Revel

Mark Armstrong – a computer science instructor at the University of North Carolina at Greensboro (UNCG) – teaches an introductory computer science course emphasising problem-solving and software design principles. Mark chose to teach Java based on employability trends as job descriptions consistently list Java as an essential requirement for programmers.

Revel for programming is designed to gently scaffold users from reading about programming to writing their programmes from scratch. Immediate feedback helps students persist productively, especially when coupled with unlimited attempts in an authentic real-world programming environment. Using a sample of UNCG students who took the course using Revel, our recent study shows that this focus on the design of Revel paid off as students were persistent on the challenging programming tasks.

Our five new business divisions

English Language Learning

We help people achieve their full potential in life through improved English proficiency, by providing engaging and personalised learning and assessment experiences.

Revenue

£0.2bn

2020 revenue

Market size

£5bn[1]

Global market

1 Pearson estimate.

We aspire to become the world's leading brand for people who need to learn or improve their English. There are over 1.5bn adults learning English today in a market we estimate is sized at c.£5.0bn and set to grow to £7.3bn by 2025. Our revenue was modest in 2020 but we own assets which we are confident we can quickly scale. The Global Scale of English, a leading global measurement standard, enables people to gauge and track their progress in English. The Pearson Test of English, a digital test with AI scoring that provides fast, accurate, secure and unbiased results, leverages the global footprint of our VUE test centres and is a trusted brand for entry into higher education and a gateway to immigration recognised by regulators in the main receiving countries.

PEARSON TEST OF ENGLISH – ACADEMIC | DIRECT TO LEARNER EXPERIENCES

The gateway to a new life

For Mary Adam, a teacher from Scotland, taking the Pearson Test of English – Academic has been the gateway to a new life down under

Learn more online:

Pearson Test of English – Academic

Mary chose to take PTE as her English language test as it was such a seamless online experience, from booking the test through to taking it. Having got the result she needed, using lots of tips from the PTE practice app, Mary can now focus purely on getting ready for her move to Western Australia.

Speaking about her hopes for her new life, Mary said: "I hope to get a full-time job teaching in a primary school, a lovely apartment with a balcony, spend lots of time outdoors with friends and gain lots of new experiences. I hope to feel settled and happy building a life for myself around sunny Perth."

Pearson | PTE

Workforce Skills

This business will focus on partnering with companies to provide education and qualifications to maximise the value of human capital in the workplace.

Revenue

£0.1bn

2020 revenue

Market size

£280bn+

Global workforce learning market

£100bn+

US market

Currently Pearson has a nascent presence in this sector with revenue of just over £0.1bn but our ambition is to become a leader in high-quality learning and assessment that supports career progression, helps people unlock their talent and drives growth for our customers' businesses.

We are forging new partnerships with corporations and other learning providers that apply our deep expertise in learning design and assessment to create learning solutions that truly meet employers' and employees' needs.

BTEC | **DIRECT TO LEARNER EXPERIENCES**

The sky's the limit

BTEC qualification has helped Marium to reach new heights

Learn more online:

BTEC

Marium Shafique took a BTEC Level 3 G Extended Diploma in Business at Nelson & Colne College achieving a triple distinction. Marium arrived in the UK from Italy in 2015 with limited spoken and next to no written English. Her journey to Lancashire School of Business and Enterprise has been meteoric, testament to her intelligence, passion and devotion.

Marium proactively pleaded with her college to skip BTEC Business at Level 2, to progress faster. Given her chance, she excelled at Level 3, achieving distinction grades in every unit of study.

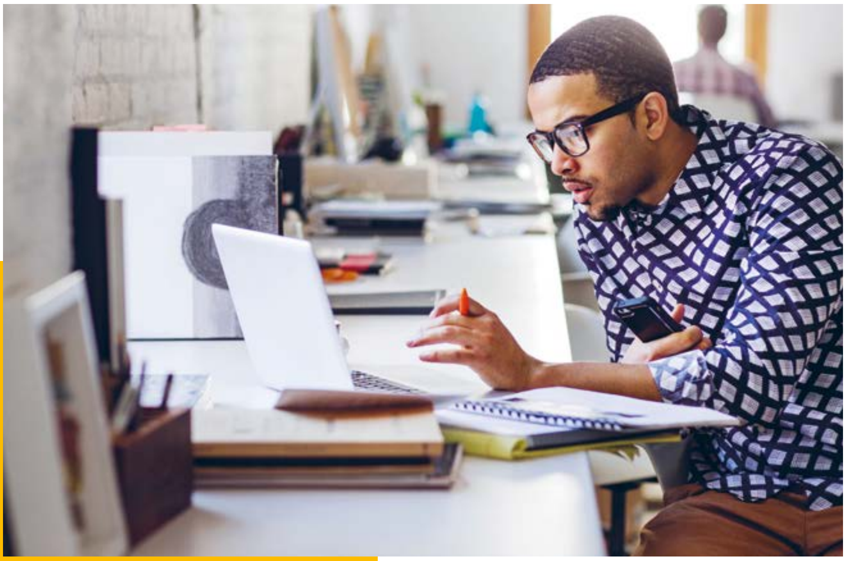
Her fierce passion for business started at an early age. "Helping my father out on my family's jewellery stall was where my love for enterprise started," explains Marium. "I've always loved the idea of studying business because it has so many areas, so I loved everything about my BTEC."

BTEC has reshaped Marium's career focus. This exceptional student now hopes to pursue a career in the banking and finance sector in a strategic managerial position with the ambition to go "as high as I can".

Our five new business divisions

Assessment & Qualifications

We partner with governments, schools, employers and professional bodies to deliver high-stakes testing and qualifications.



Revenue

£1.1bn

2020 revenue

Market size

£25bn

Global assessment market

Our Assessment & Qualifications business delivered revenue of £1.1bn in 2020 and operates in a global market of £25bn growing at 5% per year. Everything that we do across the company has the potential to lead to some form of assessment, qualification or certification, and this continues to be a significant opportunity for Pearson. Our US School Assessment business continues to win new contracts and maintain a strong market position. Pearson VUE develops, manages and delivers computer-based testing programmes for nearly every industry. Our investment in remote and online proctoring services enabled tenfold growth in 2020 to 2.1m assessments. We provide technology certification exams in the academic, career and technical education space. We are also the market leader in clinical assessment.

Furthermore, we develop and award highly sought-after UK academic and vocational qualifications, with leading brands such as Pearson Edexcel.

PEARSON VUE | DIRECT TO LEARNER EXPERIENCES

Supporting the front line

Delivering safe exams for much-needed nursing candidates during COVID-19

Learn more online:

Pearson VUE

When the COVID-19 pandemic began overwhelming healthcare facilities, affecting nurses and doctors in the field, a brave generation of aspiring healthcare professionals stepped up to join their overworked colleagues on the front lines.

Pearson VUE and the National Council of State Boards of Nursing (NCSBN) came together to help thousands of candidates move into the field quickly. By implementing new health and safety protocols at all Pearson VUE owned test centres, nursing candidates were able to gain their licensures during the pandemic and begin work to save lives in their communities.

“We needed more nurses in the workforce to meet the needs at the front line, without compromising patient safety. Pearson VUE helped ensure that we delivered a valid and secure exam in a safe environment,” says NCSBN Test Development Director Jason A. Schwartz, MS. “Pearson VUE hired and trained more than 700 new staff and opened 10 high-capacity temporary test centres to accommodate a larger number of candidates.”

Pearson VUE continues to practise strict COVID-19 protection policies for test takers that follow government guidance, while delivering licensures and certifications for healthcare workers globally.

PEARSON LEARNING PLATFORM | DIRECT TO LEARNER EXPERIENCES

Cutting-edge technology

Reinventing learning experiences to impact outcomes throughout life

Consumers of all types want engaging learning experiences that positively impact outcomes that matter to them, whatever the subject or topic at hand. The Pearson Learning Platform (PLP), a foundational platform that Pearson products sit on, is the technology solution that is delivering next-generation digital experiences, as part of our digital-first, customer-focused strategy.

For example, the new Revel application that launched on the platform has enhanced capabilities for higher education instructors while improving the overall experience for students. Specifically, the Enhanced Revel experience provides assignments and assessments that are more flexible and easier to implement, and performance dashboards and insights that allow instructors to focus on challenging concepts for individual students.

In addition, the PLP has supported the transformation of Pearson.com into a direct to consumer destination that now offers a variety of learning products and services. Now, higher education students have direct access to hundreds of Pearson eTexts with refined digital features. The site also has one-click, end-to-end technology training courses for aspiring or experienced technology professionals, to start or advance their careers.

"Pearson's many technology systems, products and services have been brought together under the PLP to achieve a common goal – the creation of consumer-focused learning experiences that will open opportunities and transform lives," said Ishantha Lokuge, Pearson Chief Global Product Officer and Co-President, Direct to Consumer. "We're off to a tremendous start and will continue building our consumer relationships and inventing learning experiences."

Learner outcomes

At Pearson we understand that, in a year where education has been turned on its head, our commitment to and focus on learner outcomes has never been more important.

Continuously improving our impact on outcomes

In practice, when we talk about our 'focus on learner outcomes', this refers to our commitment to identifying the outcomes that matter most to consumers, designing products to improve those outcomes, measuring and continuously improving the impact that using our products can have.

Our commitment to efficacy in learning is part of how we fulfil our mission as a company: to help people make progress in their lives through learning.

Commitment to learner outcomes

In 2013, we made a public commitment to start reporting on the impact on learner outcomes of our products and services. To date, we have published a total of 16 independently assured and peer-reviewed Efficacy Reports and a further seven Assessment Efficacy Reports focusing on the fitness of our assessments for a given purpose. These reports set the standard for transparent reporting across the sector.

At the same time, we have been expanding our focus on outcomes to include the product design process – ensuring that we design for efficacy from the inception of a product. This means: specifying the learner outcomes for new products and services; studying related learner science evidence of what works to improve learning; and using that evidence to inform the design of the product or service.

Activity this year

We have released a number of Efficacy Reports this year covering a range of our key products, including a focus on Revel, our market-leading product for US college students. In the Revel report, we were able to use a bigger data set than in previous Efficacy Reports to demonstrate the impact of using the product on nearly 7,500 students across 321 different courses. This allows us to generalise the results of the study with greater confidence and gives a real sense of our aspiration to complete impact evaluation at increasing scale.

Our approach

You can see examples of our approach to learner outcomes in our strategic report.

Pearson Revel, p21

Connections Academy, p37

Watson-Glaser Critical Thinking Appraisal, p38

BTEC, p39

Investing in scales and frameworks

In addition, we continued to invest this year in further developing scales and frameworks to support designing for outcomes that matter most to learners and educators. These tools, in combination with our outcomes-focused approach to product development, enable us to design quality products that stand out in the market. These tools include:

- Global Scale of English, which helps English language learners understand the level of their language and the progress they are making with their learning
- Personal and Social Capabilities framework, which supports our product development teams to create content to teach and assess essential 'soft' skills such as collaboration, critical thinking, leadership and social responsibility (see pp40–55 for our sustainability section)

Supporting new product development

In 2020, we also supported the learning design underpinning new products in development, including Career Courses which offer early-career professionals affordable access to the skills and experiences they need to stand out, secure high-value jobs and progress faster in their careers.

Plans for 2021

We want to build on this year's work by integrating learner outcomes even more deeply into our product design approach, especially with any new direct to consumer offerings. We will also continue to increase the scale of our impact measurement by using bigger data sets to examine what is working for more consumers of our products.

In addition, we will publish another Efficacy Report focusing on Connections Academy G. This builds on the findings from the original report in 2018. Other planned Efficacy Reports will cover products from our Clinical, Assessment, and UK Qualifications businesses.

We are continuously seeking ways to improve and evolve everything we do by listening to feedback and being open to revising our own approach. We welcome feedback to efficacy@pearson.com.

Learn more online:

plc.pearson.com/en-GB/purpose/improving-outcomes-for-life

Creating value for our stakeholders

Strengthening the link with our stakeholders during challenging times.

An unprecedented year

The world of education has changed rapidly as a result of the COVID-19 pandemic, while awareness of Diversity, Equity & Inclusion (DE&I) issues has increasingly been elevated in the public eye. This has served to highlight the critical role education plays in society – and the important role of technology in helping provide continuity, opportunity and access to learning. Pearson is a driving force behind the evolving education market as we look to meet the changing needs of today's learners, not just in this moment but for the foreseeable future.

Turning points in engagement

From a stakeholder engagement perspective, we see the COVID-19 pandemic and the rising social justice movement as turning points, heightening the link between society and the corporate world. Companies and individuals will be remembered for what they did during this unprecedented time in history. Our approach has been informed by this philosophy in terms of behaving responsibly and being a good corporate citizen.

The select examples on the following pages highlight our approach to engaging with stakeholders – to not just respond but to lead and co-create solutions to these complex, unprecedented issues as they evolve. We believe our early decision to help our customers in their time of need will lead to strengthened, more durable, long-term relationships. We also believe this will enable us to meet the accelerating interest in online learning while continuing to meet important societal needs in a valuable, sustainable way.

Engagement and sustainability

Stakeholder engagement always takes place through the lens of sustainability, which informs and influences our approach across our global operations. Our Sustainable Business Plan 2030 focuses on the areas that are most important to our stakeholders – learning for everyone, learning for a better world, and leading responsibly. Our approach on these three foundational pillars has been heavily informed by the stakeholder engagement 'materiality study' undertaken in 2019.

In practice: Our approach to stakeholder engagement

Supporting our employees

At the height of the pandemic, we made the decision to support our employees by not furloughing them, and instead where possible redeploying them to areas of high demand across the business. We also supported our customers by providing them with digital products and services for free to help them move online.

More broadly, as the global social justice movement gained momentum, we wanted to demonstrate our commitment to tackling systemic racism. In addition to town halls and listening sessions to discuss race, we created a task force to articulate our DE&I strategy for our products, employees and broader external stakeholders. We gave our US employees Election Day off as well as volunteer days to help further social justice causes in their communities, made significant changes to our editorial and hiring policies, and set the stage for Pearson's future work in this area. DE&I strategies are intrinsic to creating a stronger, more sustainable business for all our company stakeholders.

Learn more about our integrated approach:

DE&I p50

Directors' duties statement p30

Board engagement with stakeholders p80

People of **Pearson**

I love to express new ideas and **learn from others** who think differently than myself.

Ev Kent
Sales Consultant, Higher Education
Arkansas, USA

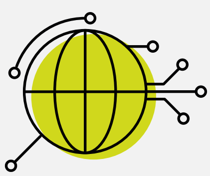
Creating value for our stakeholders

Consumers

Pearson helps tens of millions of people across the world to make progress in their lives through learning. Increasingly, people are taking educational choices into their own hands. We are working to build a direct relationship with them, over a lifetime of learning.

88%

Of respondents in our Global Learner Survey agree that education should take advantage of technology to maximise the learning experience for students of all ages[1]



How we serve and engage

We regularly talk to and survey people of all ages to understand how they are incorporating learning into their lives beyond the traditional classroom.

This allows us to put consumer needs at the centre of what we do, building world-class digital products that not only deliver amazing experiences but also help people learn and thrive in the changing world of work.

Key concerns

Our second Pearson Global Learner Survey shows that learners see COVID-19 as a turning point for modern learning, with online schooling and economic upheaval leaving a lasting mark. In the pandemic-aware world, economic uncertainty will drive more people to upskill and reskill for job security.

Our response

We support people across all ages, stages and backgrounds of education – from schooling through higher education and into employment and employability.

Our focus is on providing high-quality virtual and online learning, enabling learners to gain the credentials and build the skills they need to improve their employability prospects.

1 Source: Pearson Global Learner Survey, 2020

Employees

We are currently focusing on embedding our employee value proposition in everything we do, with the aim of building a more inclusive learning culture in order to attract and retain the world's best talent.

11,000

In 2020 we held our first Global Learning at Work Week. Across the week we delivered 70+ hours of learning to 11,000 employees

How we serve and engage

We're the only global company where our employees can unleash their talent while helping millions of people make progress in their lives through learning.

We believe that DE&I are fundamental to who we are.

Key concerns

In our first quarter employee pulse survey, we heard that employees wanted more support in understanding career pathways, navigating learning resources and making learning part of their work (rather than in addition to their work).

Our response

Global Learning at Work Week was a direct response to this. We offered everyone access to a wide variety of learning opportunities hosted by talented colleagues from across Pearson and external experts.

Shareholders

We have a broad range of investors who entrust their capital with us.

543

investor meetings with

196

institutions in 2020

How we serve and engage

We engage with our investors on an ongoing basis. We communicate with them regularly, including at our financial results presentations, our AGM and at investor meetings and conferences around the globe. We have been able to continue with our engagement virtually during the pandemic.

Key concerns

Our shareholder base has a diverse range of views covering financial and ESG (environmental, social and governance) issues. As well as these areas, in 2020 there has been focus on the impact of the pandemic on Pearson's performance, as well as on the Chief Executive succession process.

Our response

We have a positive, ongoing dialogue with our shareholder base. We aim to deliver long-term sustainable value for our investors and all our company stakeholders. We also respond to surveys and questionnaires to provide information about our ESG practices.

Educational Institutions & Educators

We work with teachers, instructors, faculty and educators across all stages of education.

63%

Of US college faculty delivered their courses entirely online this fall[2]

How we serve and engage

We collaborate with educators and provide them with the tools they need in order to help the next generation of learners to be successful in their education and make progress in their lives.

Key concerns

When the pandemic kicked in, schools, colleges and universities across the world had a matter of days to figure out what the 'new world' of learning would look like – closing physical sites and scrambling to go online.

Our response

We made the decision very early on that it was the right course of action to help our customers – on a free basis initially – to deal with the immediate crisis and take their courses and classes online.

As a result of this, we have seen a large uptake in usage. We believe that helping our customers in their time of need will lead to strengthened, more durable, long-term relationships.

2 Source: Pearson Faculty Tech Study, 2020

As well as the stakeholder groups we have direct dialogue with, outlined below, we are also are aware of our broader responsibilities to our planet and society at large.

Learn more: Sustainability, pp40-55

Employers

Pearson works with employers, trade associations and industry bodies to meet the demands of the workforce and equip learners with the skills they need to thrive.

79%

Of learning and development professionals expect to spend more on online learning[3]

How we serve and engage

We work to increase the link between education and employment in a variety of ways – for example, in our Accelerated Pathways business in the US, we work with employers such as Brinker International and ManpowerGroup to help provide upskilling opportunities for their employees.

We offer nationally recognised assessment and qualifications, micro-certification, online learning, and professional badging to support the efforts of industry to prepare workers for a lifetime of learning.

Key concerns

The pandemic has forced many global employers to rethink ways of working, the relationship they have with their employees, and the speed at which they need to innovate in order to survive and thrive in the future world of work and navigate social and environmental challenges.

Our response

In response to the pandemic, we played a role in the employability challenge by rapidly starting up UK Learns, a carefully curated selection of online courses to help workers learn new skills and earn qualifications to open up new career opportunities and kickstart careers stalled by COVID-19.
We are actively looking to replicate this employability service to other markets.

3 Source: LinkedIn 2020 Workplace Learning Report

Business Partners

From technology providers to suppliers, channel partners to our authors, we have a broad range of partners across our global business.

c.80%

Of Pearson global spend derives from 470 suppliers

How we serve and engage

We are focused on building successful business partnerships across the education ecosystem to ensure joint success and growth.

Through our focus on the DE&I task force, we are working to enhance our DE&I credentials – for example, we have contacted our authors in the US and the UK to ask them to voluntarily disclose their diversity characteristics. This will allow us to set an author diversity baseline which we will track going forward.

Key concerns

We share similar goals with our partners – from driving business transformation to developing world-class products; enhancing customer experience, adherence to data privacy and IT security processes; managing risk; increasing partnership with diverse defined suppliers; promoting supplier social responsibility; developing talent and more. We expect partners to share our values.

Our response

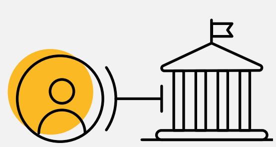
We build relationships with world-class partners and suppliers for the benefit of all our stakeholders. We believe that working with partners who share our commitments not just to best-in-class business practices – but also best practice and international standards for human rights and environmental stewardship – strengthens our value chain and reduces our business costs and risks.

Governments and regulators

We partner with governments (local, state, federal, national) to ensure learners have access to high-quality instruction, materials and assessments linked to beneficial outcomes, including building workforce skills. Engagement with statutory bodies such as listing authorities and financial regulators is key to doing business as a listed global company.

50

US states and a wide range of global markets in which Pearson works with government stakeholders



How we serve and engage

Governments and regulators set policy to ensure that both businesses and consumers are provided with the most effective legislative frameworks that help drive sustainable growth and ensure that learners have access to affordable education and training opportunities.

We are committed to building strong relationships with political and educational leaders at every level across the world. We do not make policy, rather we share best practices and inform the policymaking process through our knowledge gained from our expertise as the world's learning company.

Key concerns

As the COVID-19 pandemic is changing life as we know it around the world, governments are facing new challenges – and potential new opportunities – to address inequities across healthcare, education and the workforce.

As uncertainty around the pandemic's duration continues and countries struggle to stabilise their economies, policymakers across the globe must rise to the occasion to formulate innovative solutions across each of those sectors.

Our response

Pearson is uniquely situated to collaborate with governments worldwide to face the disruption caused by the pandemic and help build innovative solutions to expand equitable access to high-quality education and job training.

We are working with local and national governments to adapt our products and services to still fill the purpose, need and outcomes expected. This includes, for example, our work in the UK where we continue to work closely with the Department for Education and the regulator to ensure schools, teachers and students are supported as Summer exam series have been cancelled due to COVID-19.

Directors' duties statement

The Directors of Pearson plc – and those of all UK companies – must act in accordance with a set of general duties. These duties are detailed in the Companies Act 2006 and include, in Section 172, a duty to promote the success of the company (inset below).

As part of their induction at Pearson, the Directors are briefed on their duties and they can access professional advice on these – either through the company or, if they judge it necessary, from an independent provider. Typically, in large and complex businesses such as Pearson, the Directors fulfil their duties partly through a governance framework that delegates day-to-day decision-making to employees of the Group.

The Board recognises that such delegation needs to be much more than a simple financial authority and, throughout this document, we have summarised: our governance framework; the values and behaviours expected of our employees and business partners, including the standards to which they must adhere; how we engage with stakeholders, including to understand and take into account their views and concerns; and how the Board looks to ensure that we have a robust system of control and assurance processes in place.

In this annual report, we provide examples of how the Directors take into account the likely consequences of decisions in the long term, build relationships with stakeholders, engage with employees, understand the impact of Pearson's operations on communities and the environment, and attribute importance to behaving as an ethical and responsible business. In particular, you are encouraged to read the following sections of this report, which illustrate how the Directors, with the support of the wider business, consider these matters in the course of their duties, although this is not intended to be an exhaustive list as such matters are integrated throughout this report, including:

- Creating value for our stakeholders (pp27–29), which summarises our stakeholder groups, how we serve and engage with them, their key concerns and our response
- The Board's disclosure, Engagement with stakeholders (p80), which summarises:

› how Directors have engaged with employees and had regard to employees' interests

› how Directors have had regard to the need to foster the company's business relationships with suppliers, customers and others. Pearson considers its key customer groups to be Consumers, Educators and Educational Institutions and Employers, and describes its suppliers as Business Partners – we have categorised our engagement with these groups accordingly

- Sustainability (pp40–55), which describes:

› how stakeholders were consulted in the development of our new Sustainable Business Plan 2030, which is ongoing and is overseen by our Reputation & Responsibility Committee. More detail on this process is available in our Sustainability & ESG supplement on our website

› the ways in which we engage in respect of the social, environmental and economic issues that will influence learning

› initiatives through which we strive to improve access to quality education for underserved and underrepresented groups

› our commitment to leading responsibly and creating a culture that prioritises our impact on climate change, human rights, our employees, DE&I, and socially responsible sourcing

› how we align with widely-accepted sustainability frameworks including the SASB and TCFD

A continued understanding of the key issues affecting stakeholders is an integral part of the Board's decision-making process, and the insights that the Board gains through engagement mechanisms form an important part of the context for all of the Board's discussions and decision-making processes.

While the Board has taken all stakeholders' views into account when making decisions during 2020, it is recognised that engagement has been impacted due to COVID-19.
For additional information on the Board's engagement with stakeholders, see p80.
In addition, there is a case study on the Board's engagement with employees (p81), as well as further information on the Board's decision-making with respect to COVID-19 (pp78–79)

Section 172 of the Companies Act

In summary, as required by Section 172 of the Companies Act 2006, a director of a company must act in the way he considers, in good faith, would most likely promote the success of the company for the benefit of its shareholders. In doing this, the director must have regard, among other matters, to:

- the likely consequences of any decisions in the long term
- the interests of the company's employees
- the need to foster the company's business relationships with suppliers, customers and others
- the impact of the company's operations on the community and environment
- the company's reputation for high standards of business conduct, and
- the need to act fairly as between members of the company

Financial review

In 2021, we expect Group revenue to grow and profit to be in line with market expectations.

Sally Johnson
Chief Financial Officer

Profit and loss statement

In 2020, sales decreased by £472m in headline terms to £3,397m (2019: £3,869m) with underlying performance reducing sales by £386m, portfolio changes reducing sales by £55m and currency movements decreasing revenue by £31m. Stripping out the impact of portfolio and currency movements, revenue was down 10% in underlying terms.

2020 adjusted operating profit was £313m (2019: £581m) with portfolio changes, inflation, and the trading impact of COVID-19 partially offset by restructuring savings. Excluding the impact of foreign exchange (FX) and portfolio changes, underlying adjusted operating profit was down 40%.

Net interest payable was £61m, compared to £41m in 2019. The increase is mainly due to interest on tax, with one-off credits recorded in 2019 not repeated in 2020, and interest charges on the bond raised in June 2020.

The effective tax rate on adjusted earnings in 2020 was a charge of 13.7% compared to a charge of 16.5% in 2019. The decrease in the effective tax rate is mainly due to a benefit from the release of tax provisions due to the expiry of the relevant statute of limitation.

Adjusted earnings per share of 28.7p (2019: 57.8p) reflects all the elements above.

Cash generation

Operating cash inflow decreased on a headline basis from £418m in 2019 to £315m in 2020, with cash conversion of 101% versus 72% in 2019. The decrease is largely explained by the drop-through of reduced profit offset by good working capital management. The equivalent statutory measure, net cash generated from operations, was £450m in 2020 compared to £480m in 2019. Compared to operating cash flow, this measure includes restructuring costs but does not include regular dividends from associates. It also excludes capital expenditure on property, plant, equipment and software, and additions to right of use assets as well as disposal proceeds from the sale of property, plant, equipment and right of use assets (including the impacts of transfers to/from investment in finance lease receivable). In 2020 restructuring cash outflow was £38m (2019: £111m).

Statutory results

Our statutory operating profit was £411m in 2020 compared to a profit of £275m in 2019. The increase in 2020 is largely due to the gain on sale of Penguin Random House and the reduction in restructuring costs, which were more than enough to offset the impact of COVID-19 and portfolio changes on trading profits.

Capital allocation

Our capital allocation policy is to maintain a strong balance sheet and a solid investment grade credit rating, to continue to invest in the business, both organically and inorganically, to have a sustainable and progressive dividend policy, and to return surplus cash to our shareholders.

Financial summary

Business performance

£ millions	2020	2019	Headline growth	CER growth	Underlying growth
Sales	**3,397**	3,869	(12)%	(11)%	(10)%
Adjusted operating profit	**313**	581	(46)%	(46)%	(40)%
Operating cash flow	**315**	418			
Adjusted earnings per share	**28.7p**	57.8p			
Net debt	**(463)**	(1,016)			

Statutory results

£ millions	2020	2019	Headline growth	CER growth	Underlying growth
Sales	**3,397**	3,869	(12)%	(11)%	(10)%
Operating profit	**411**	275			
Profit for the year	**310**	266			
Cash generated from operations	**450**	480			
Basic earnings per share	**41.0p**	34.0p			
Dividend per share	**19.5p**	19.5p			

Throughout this section: a) Growth rates are stated on an underlying basis unless otherwise stated. Underlying growth rates exclude currency movements and portfolio changes; b) The 'business performance' measures are non-GAAP measures, and reconciliations to the equivalent statutory heading under IFRS are included in the financial key performance indicators section on pp212–216

Financial review

Balance sheet

Net debt to adjusted EBITDA was 0.8x (2019: 1.3x). Net debt reduced from £1,016m in 2019 to £463m at the end of 2020. Excluding leases, net debt reduced from £374m in 2019 to net cash of £159m in 2020. The decrease is largely due to the receipt of proceeds of £531m from the Penguin Random House sale, the receipt of deferred proceeds of £105m from the US K-12 sale, the £48m repayment of the loan to Penguin Random House and positive operating cash flow of £176m offset by interest and dividend payments and the cash outflow from the Group's share buyback programme. As a result of the COVID-19 pandemic, the Group took action to increase its liquidity including pausing the share buyback programme with £176m of the share buyback completed. The Board considers that maintaining a very strong balance sheet is appropriate, and as such, there are no plans to reinitiate the buyback. On 4 June 2020 the Group also completed the issuance of £350m guaranteed notes maturing on 4 June 2030.

The Group continues to work to protect its cash flow and proactively manage working capital and, at the end of 2020, the Group had approximately £1.9bn (2019: c.£1.1bn) in total liquidity immediately available from cash and its revolving credit facility (RCF).

Pension plan

The overall surplus on UK pension plans of £429m at the end of 2019 has decreased to a surplus of £410m at the end of 2020. The decrease has arisen principally due to an actuarial loss in relation to retirement benefit obligations of the Group.

Dividend

In line with our policy, the Board is proposing a final dividend of 13.5p (2019: 13.5p), flat year-on-year, which results in an overall dividend of 19.5p (2019: 19.5p) subject to shareholder approval. This will be payable on 7 May 2021.

Businesses held for sale

In November 2020, the Group announced the sale of its interests in Pearson Institute of Higher Education (PIHE) G in South Africa. At the end of December 2020 the assets and liabilities of PIHE have been classified as held for sale on the balance sheet. The sale completed on 5 February 2021.

Businesses disposed of

In April 2020, the Group completed the sale of the remaining 25% interest in Penguin Random House to Bertelsmann SE & Co KGaA, generating net proceeds of £531m and resulting in a pre-tax profit of £180m.

Following the decision to sell the US K-12 courseware business, the assets and liabilities of that business were classified as held for sale on the balance sheet at the end of 2018. In March 2019, the Group completed the sale of its K-12 business with total gross proceeds of £200m including £180m of deferred proceeds which included the fair value of an unconditional vendor note for $225m and an entitlement to 20% of future cash flows to equity holders and 20% of net proceeds in the event of a subsequent sale. In 2020, the Group received ($143m) (£105m) as a partial repayment of the vendor note and a payment in respect of the full purchase equity interest such that the Group is no longer entitled to any future cash flows to equity holders or net proceeds in the event of a subsequent sale.

On 5 March 2021, we agreed the sale of our K-12 Sistemas – COC and Dom Bosco – in Brazil to Arco, subject to securing regulatory approval and closing.

2021 outlook

We expect year-on-year revenue growth, with adjusted operating profit to be in line with current market expectations.

- Good growth in Virtual Learning, driven by the Virtual Schools 2020/2021 academic year enrolment growth. Enrolments for the 2021/2022 academic year are expected to be broadly flat, with the 'COVID-19 cohort' partially returning to bricks and mortar schools, offset by underlying growth, and waiting lists. Online Program Management (OPM) is also expected to grow.
- Assessment & Qualifications revenue growth as lockdowns and social distancing ease. Expect impacted test centres to reopen – with social distancing – in April, and normal operations to resume progressively in H2 2021. US school assessments expected to resume, and clinical tests to be taken as schools reopen. UK exams cancelled with modest profit impact as teacher assessment to replace exams
- English Language Learning revenue expected to improve as mobility, migration and school purchasing recover slowly amidst continuing COVID-19 restrictions
- Higher Education revenue to decline, but by less than seen in recent years, as the print base becomes smaller, and as the pricing pressure from the change in mix from print and bundles, to platform and eTexts, is offset by recapture of the secondary market driven by eText growth and the digital-first strategy, and enrolment recovery
- Workforce Skills revenue expected to grow, given the strong business fundamentals and investments made into digital and direct to consumer opportunities
- Revenue phasing will be impacted by current conditions, with Q1 sales behind a challenging 2020 comparative, with growth expected in Q2 and Q3 assuming further pandemic recovery, with the delivery of pent-up testing demand in H2 2020 providing a tougher comparative
- Net interest charge of c.£65m and a tax rate of 18% to 22%
- As previously announced, cost efficiencies expected of c.£50m in 2021

Long term outlook

Segment	Market 5-year CAGR[1]	Long-term growth	Long-term margin[2]
Virtual Learning	High single digit	Strong	Increase
Higher Education	Stabilisation	Recapture of secondary market, International growth	Increase
English Language Learning	Mid to high single digit	At least in line with market growth	Maintain
Workforce Skills	Mid to high single digit	Strong	Maintain
Assessment & Qualifications	Professional Certification low to mid single digit US School Assessment and Clinical Assessment flat	Low to moderate	Maintain

1 Pearson estimates.
2 vs 2019 margin.

Portfolio

In addition to the pending sale of our K-12 Sistemas – COC and Dom Bosco – in Brazil, we will also be strategically reviewing the rest of our international courseware local publishing businesses, including Canada.

Key performance indicators

Our financial KPIs will remain the same, to maintain focus on growth, profitability and cash generation. At our FY 2020 results we announced that our key business and non-financial KPIs will change to reflect the pivot to the new growth strategy, and will focus on:

- Digital growth
- Consumer engagement
- Product effectiveness
- Investing in our talent
- Building an inclusive culture and improving diverse representation
- Accelerating our sustainability strategy

We will also report leading indicators against our five divisions going forward.

Adjusted performance measures

The Group's adjusted performance measures are non-GAAP financial measures and are included as they are key financial measures used by management to evaluate performance and allocate resources to business segments. The measures also enable investors to more easily, and consistently, track the underlying operational performance of the Group and its business segments over time by separating out those items of income and expenditure relating to acquisition and disposal transactions, major restructuring programmes and certain other items that are also not representative of underlying performance.

The Group's definition of adjusted performance measures may not be comparable to other similarly titled measures reported by other companies. A reconciliation of the adjusted measures to their corresponding statutory reported figures is shown in summary below and in more detail on pp212–216

Adjusted operating profit

Adjusted operating profit includes the operating profit from the total business including the results of discontinued operations when relevant. There were no discontinued operations in either 2019 or 2020. A reconciliation of the statutory measure to the adjusted measure is shown below:

£ millions	2020	2019
Operating profit	**411**	275
Add back: cost of major restructuring	**–**	159
Add back: other net (gains) and losses	**(178)**	(16)
Add back: intangible charges	**80**	163
Adjusted operating profit	**313**	581

In May 2017, we announced a restructuring programme, to run between 2017 and 2019, to drive significant cost savings. This programme began in the second half of 2017 and costs incurred relate to delivery of cost efficiencies in our enabling functions and US Higher Education Courseware business together with further rationalisation of the property and supplier portfolio. The restructuring costs in 2019 relate predominantly to staff redundancies. The restructuring programme was largely completed at the end of 2019.

These major restructuring costs are analysed below:

£ millions	2020	2019
Further efficiency improvements in Enabling Functions through back office change programmes in Human Resources, Finance and Technology	**–**	(94)
Adjusting the cost base in our US Higher Education Courseware business	**–**	(34)
Further rationalisation of property, vendor and supplier agreements	**–**	(29)
Associate restructuring	**–**	(2)
Total	**–**	(159)

Other net gains and losses that represent profits and losses on the sale of subsidiaries, joint ventures, associates and other financial assets are excluded from adjusted operating profit. Other net gains included in operating profit of £178m in 2020 largely relate to the sale of the remaining interest in Penguin Random House and impairments of assets and other costs relating to the disposal of Pearson Institute of Higher Education (PIHE). Other net gains included in operating profit of £16m in 2019 mainly relate to the profit on sale of the US K-12 business.

Charges relating to acquired intangibles and acquisitions are also excluded from adjusted operating profit when relevant, as these items reflect past acquisition activity and do not necessarily reflect the current year performance of the Group. Intangible amortisation and impairment charges in 2020 were £80m compared to a charge of £163m in 2019, as although acquisition activity has reduced in recent years and the disposal of Penguin Random House has eliminated the Group's share of associate intangible amortisation, this has been partly offset by accelerated amortisation profiles and impairments recorded mainly relating to content and contract intangibles in the Global Assessments and International businesses. In 2019, there was an additional £65m impairment charge relating to acquired intangibles in the Brazil business following a reassessment of the relative risk in that market (see also note 11 to the financial statements).

Underlying growth rates

Sales decreased on a headline basis by £472m, or 12%, from £3,869m in 2019 to £3,397m in 2020, and adjusted operating profit decreased by £268m, or 46%, from £581m in 2019 to £313m in 2020. The headline basis simply compares the reported results for 2020 with those for 2019. We also present sales and profits on an underlying basis which exclude the effects of exchange, portfolio changes arising from acquisitions and disposals and the impact of adopting new accounting standards that are not retrospectively applied. Our portfolio change is calculated by taking account of the contribution from acquisitions and by excluding sales and profits made by businesses disposed in either 2019 or 2020. Portfolio changes mainly relate to the sale of our US K-12 business in 2019 and the sale of our remaining interest in Penguin Random House in the first half of 2020. Acquisitions, including Lumerit in 2019, had only a small impact on reported sales and profits.

Financial review

On an underlying basis, sales decreased by 10% in 2020 compared to 2019 and adjusted operating profit decreased by 40%. Currency movements decreased sales by £31m and increased adjusted operating profit by £1m. Portfolio changes decreased sales by £55m and decreased adjusted operating profit by £59m. There were no new accounting standards adopted in 2020 that impacted sales or profits.

Adjusted earnings per share

Adjusted earnings includes adjusted operating profit and adjusted finance and tax charges. A reconciliation to the statutory profit is shown below:

£ millions	2020	2019
Profit/(loss) for the year	**310**	266
Non-controlling interest	**–**	(2)
Add back: Cost of major restructuring	**–**	159
Add back: Other net gains	**(178)**	(16)
Add back: Intangible charges	**80**	163
Add back: Other net finance costs	**(4)**	2
Tax benefit relating to items added back	**9**	(123)
Adjusted earnings	**217**	449
Weighted average number of shares (millions)	**755.4**	777.0
Adjusted earnings per share	**28.7p**	57.8p

Net finance income relating to retirement benefits is excluded as it is considered that the presentation does not reflect the economic substance of the underlying assets and liabilities. The Group excludes finance costs relating to acquisition and disposal transactions as these relate to future earn-outs or acquisition expenses and are not part of the underlying financing. In 2020, the fair value remeasurement of disposal proceeds of £26m relates to proceeds from the US K-12 disposal in 2019.

Foreign exchange and other gains and losses are also excluded as they represent short-term fluctuations in market value and are subject to significant volatility. Other gains and losses may not be realised in due course, as it is normally the intention to hold the related instruments to maturity.

In 2020, the total of these items excluded from adjusted earnings was income of £4m compared to a charge of £2m in 2019. Net finance income relating to retirement benefits decreased from £13m in 2019 to £6m in 2020 reflecting the comparative funding position of the plans at the beginning of each year and lower prevailing discount rates. In 2020, finance income relating to the revaluation of the US K-12 disposal proceeds was recorded and there were increases in losses on long-term interest rate hedges and increases in foreign exchange losses on unhedged inter-company loans, cash and cash equivalents in 2020 compared to 2019.

The adjusted income tax charge excludes the tax benefit or charge on items that are excluded from the profit or loss before tax. In addition, the tax benefit from tax deductible goodwill and intangibles is added to the adjusted income tax charge, as this benefit more accurately aligns the adjusted tax charge with the expected rate of cash tax payments.

Operating cash flow

Operating cash flow is an adjusted measure and is presented in order to align the cash flows with corresponding adjusted operating profit measures. A reconciliation to operating cash flow from net cash generated from operations, the equivalent statutory measure, is shown below:

£ millions	2020	2019
Net cash generated from operations	**450**	480
Dividends from joint ventures and associates	**4**	64
Capital expenditure on property, plant, equipment and software (including additions to leased assets)	**(195)**	(257)
Proceeds from sale of property plant, equipment and software (including disposal and transfer of leased assets)	**18**	18
Investment income	**–**	2
Add back: Costs paid/ (proceeds from) major restructuring projects	**38**	111
Operating cash flow	**315**	418

Operating cash inflow decreased on a headline basis by £103m from £418m in 2019 to £315m in 2020. The decrease is largely explained by the drop-through of reduced profit due to COVID-19, offset by improved working capital. In 2020 restructuring cash outflow was £38m compared to £111m in 2019.

Other financial information

Net finance costs

£ millions	2020	2019
Net interest payable	**(61)**	(41)
Finance income in respect of retirement benefits	**6**	13
Fair value remeasurement of disposal proceeds	**26**	–
Other net finance costs	**(28)**	(15)
Net finance costs	**(57)**	(43)

Net interest payable in 2020 was £61m, compared to £41m in 2019. The increase is mainly due to interest on tax, with one-off credits recorded in 2019 not being repeated in 2020, and interest charges on the bond raised in June 2020.

As detailed in the adjusted earnings per share section, finance income in respect of retirement benefits, fair value measurements of disposal proceeds and other net finance costs are excluded from adjusted earnings.

Capital risk

The Group's objectives when managing capital are to:

› maintain a strong balance sheet and a solid investment grade rating

› continue to invest in the business organically and through acquisitions

› have a sustainable and progressive dividend policy

› return surplus cash to our shareholders where appropriate

In response to the COVID-19 outbreak, the Group took the decision to suspend the share buyback programme, which helped to preserve liquidity and maintain the Group's credit metrics.

The Group is currently rated BBB- (stable outlook) with Standard and Poor's and Baa3 (stable outlook) with Moody's.

Net debt

The net debt position of the Group is set out below.

£ millions	2020	2019
Cash and cash equivalents	**1,116**	437
Investment in finance leases	**130**	196
Derivative financial instruments	**11**	15
Bank loans and overdrafts	**(3)**	(3)
Revolving credit facility	**–**	(230)
Bonds	**(965)**	(593)
Lease liabilities	**(752)**	(838)
Net debt	**(463)**	(1,016)

The Group's net debt reduced from £1,016m at the end of 2019 to £463m at the end of 2020. The decrease is largely due to the receipt of proceeds of £531m from the Penguin Random House sale, the receipt of deferred proceeds of £105m from the US K-12 sale, the £48m repayment of the loan to Penguin Random House and positive operating cash flow offset by interest and dividend payments and the cash outflow of £176m from the Group's share buyback programme.

Liquidity and funding

As a result of the COVID-19 pandemic, the Group took action to increase its liquidity, including pausing the share buyback programme, and on 4 June 2020, the Group completed the issuance of £350m guaranteed notes maturing 4 June 2030.

The notes bear a coupon of 3.75% and have been issued in accordance with the ICMA Social Bond Principles 2018. The proceeds will be primarily used to finance and re-finance delivery of education in our Connections Academy, BTEC and GED G businesses to help achieve the United Nations' 4th Sustainable Development Goal (SDG) for a quality education. The social bond framework is a natural progression of Pearson's long-standing commitment to integrating social and environmental sustainability into the business.

In assessing the Group's liquidity, the impact of the COVID-19 pandemic has been modelled under several scenarios to ensure that the likelihood of a prolonged period of disruption has been appropriately considered in assessing the availability of funding to the Group and the ability of the Group to comply with its banking covenants. The Group's base case forecasts include assumptions relating to the COVID-19 pandemic. It is assumed that restrictions ease in Q2 2021 with a phased return to normality in H2 2021 as the vaccine roll-out progresses. The downside case scenario modelling includes a severe reduction in revenue, profit and operating cash flow compared to the base case assumptions that extends through the full three-year period to ensure that the Group has adequate resources to manage for a prolonged period of disruption.

In assessing the Group's viability for the three years to December 2023, the Board analysed a variety of downside scenarios including a severe but plausible scenario where the Group is impacted by all principal risks from 2021 (weighted for probability of occurrence) as well as reverse stress testing to identify what would be required to either breach covenants or run out of liquidity. The severe but plausible scenario modelled an impact from COVID-19 and other risks which in aggregate were significantly greater than seen in 2020 continuing throughout 2021 to 2022.

At 31 December 2020, the Group had available liquidity of c£1.9bn, comprising central cash balances and its undrawn $1.19bn RCF maturing February 2024. Even under a severe downside case where further declines in profitability compared to 2020 are modelled in 2021 and 2022, the Group would maintain liquidity headroom in excess of £700m and sufficient headroom against covenant requirements during the period under assessment, even before modelling the mitigating effect of actions that management would take in the event that these downside risks were to crystallise.

Taxation

The effective tax rate on adjusted earnings in 2020 was a charge of 13.7% compared to an effective tax rate charge of 16.5% in 2019. The decrease in the effective rate is mainly due to a benefit from the release of tax provisions due to the expiry of the relevant statute of limitation.

The reported tax charge on a statutory basis in 2020 was a charge of £44m (12.5%) compared to a credit of £34m (14.7%) in 2019. The statutory tax credit in 2019 was primarily due to US tax losses generated on the disposal of the US K-12 business.

Operating tax paid in 2020 was £10m (2019: £9m). This was impacted by refunds received in the US and UK relating to historical periods. Non-operating tax was a refund of £12m in 2020 (2019: paid £21m) relating to settlement of a historical tax audit and the impact of the disposal of our US K-12 business.

A net deferred tax liability of £30m is recognised in 2020 compared to a net £11m deferred tax asset in 2019, the movement is mainly due to utilisation of tax losses in our US business and the amortisation of tax deductible goodwill in Brazil which reduces the related deferred tax asset. The current tax creditor principally consists of provisions for tax uncertainties. There are contingent liabilities in relation to tax as outlined in note 34 to the financial statements.

Other comprehensive income

Included in other comprehensive income are the net exchange differences on translation of foreign operations. The loss on translation of £109m in 2020 compares to a loss in 2019 of £115m. The loss in 2020 mainly arises from the weakening of the US dollar compared to sterling. A significant proportion of the Group's operations are based in the US, and the US dollar weakened in 2020 from an opening rate of £1:$1.32 to a closing rate at the end of 2020 of £1:$1.37. At the end of 2019 the US dollar had weakened from an opening rate of £1:$1.27 to a closing rate of £1:$1.32 and this movement was the main reason for the loss in 2019.

Also included in other comprehensive income in 2020 is an actuarial loss of £23m in relation to retirement benefit obligations of the Group. The loss arises from the unfavourable impact of changes in the assumptions used to value the liabilities in the plans and, in particular, movements in the discount rate. The actuarial loss in 2020 of £23m compares to an actuarial loss in 2019 of £145m.

In 2020, £70m was recycled from the currency translation reserve to the income statement in relation to the disposal of Penguin Random House.

Post-retirement benefits

Pearson operates a variety of pension and post-retirement plans. Our UK Group pension plan has by far the largest defined benefit section. We have some smaller defined benefit sections in the US and Canada but, outside the UK, most of our companies operate defined contribution plans.

Financial review

The charge to profit in respect of worldwide pensions and post-retirement benefits amounted to £54m in 2020 (2019: £56m), of which a charge of £60m (2019: £69m) was reported in adjusted operating profit and income of £6m (2019: £13m) was reported in other net finance costs. The decrease in the operating charge in 2020 is largely explained by savings in defined contribution plans as a result of recent disposals and restructuring activities.

The overall surplus on UK Group pension plans of £429m at the end of 2019 has decreased to a surplus of £410m at the end of 2020. The decrease has arisen principally due to the actuarial loss noted above in the other comprehensive income section. In total, our worldwide net position in respect of pensions and other post-retirement benefits decreased from a net asset of £337m at the end of 2019 to a net asset of £325m at the end of 2020.

Dividends

The dividend accounted for in our 2020 financial statements totalling £146m represents the final dividend in respect of 2019 (13.5p) and the interim dividend for 2020 (6.0p). We are proposing a final dividend for 2020 of 13.5p, bringing the total paid and payable in respect of 2020 to 19.5p. This final 2020 dividend, which was approved by the Board in March 2021, is subject to approval at the forthcoming AGM and will be charged against 2021 profits. For 2020, the dividend is covered 1.5 times by adjusted earnings.

Share buyback

The share buyback programme, announced in December 2019, commenced on 16 January 2020 and was paused on 23 March 2020 in order to protect liquidity from the impact of COVID-19. The original intention was to buy back approximately £350m of shares and, at the date of pausing the programme, approximately 30 million shares had been bought back and cancelled at a cost of £176m. There are currently no plans to resume the share buyback programme. The nominal value of these shares, £7m, was transferred to the capital redemption reserve.

Acquisitions

There were no significant acquisitions in 2020. In 2019, the Group made some small acquisitions for total consideration of £40m.

COVID-19

The Group has assessed the impact of the uncertainty presented by the COVID-19 pandemic on the Financial Statements, specifically considering the impact on key judgements and significant estimates along with other areas of increased risk, including provisions for bad debt, provisions for inventory obsolescence, valuation of property-related assets and financial instruments. No material accounting impacts relating to the areas assessed were recognised in the year. The Group will continue to monitor these areas of increased judgement, estimation and risk for material changes.

Related party transactions

Transactions with related parties are shown in note 36 of the consolidated financial statements.

Post balance sheet events

On 5 February 2021, the Group completed the sale of its interests in PIHE in South Africa. Consideration received was nominal.

In February 2021, the Group received charging notices requiring payment of materially all of the alleged State Aid (see note 34 in the notes to the consolidated financial statements for further details). A payment of £100m was made on 8 March 2021. The Group expects to recover the funds in due course.

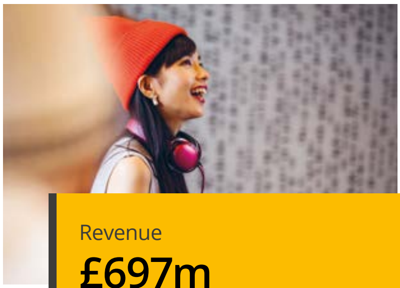
In February 2021, the Group renegotiated its RCF, extending the maturity of $1bn of the facility by one year to 2025.

On 5 March 2021, the Group agreed the disposal of its K-12 Sistemas – COC and Dom Bosco – in Brazil, subject to securing regulatory approval and closing.

On 8 March 2021, the Group announced a new strategy including a new divisional structure. Going forward the new structure will impact segmental reporting and may impact the Group's cash generating units.

Segmental performance[1]

Global Online Learning



Revenue
£697m
+18% 2019: £586m

Adjusted operating profit
£99m
+23% 2019: £84m

CONNECTIONS ACADEMY
OUR FOCUS ON LEARNER OUTCOMES

High performance

Connections outperforms other virtual schools on reading.

In 2021, we will release an update to our 2018 efficacy report for Connections Academy, our full-time virtual school programme in the US. This will take a deeper look at the learner outcomes Connections students achieve. The original study showed that, when adjusted for high student mobility and controlled for prior student achievement, the academic performance of Connections students is better than other virtual schools for reading and equivalent to other virtual schools in mathematics.

Learn more:

Connections Academy

Revenue grew 18% on an underlying basis and 19% on a headline basis reflecting strong enrolment growth in Virtual Schools and good growth in OPM.

Adjusted operating profit grew 23% in underlying terms, due to margin on sales growth more than offsetting the investment in our virtual schools platform and customer care support and margin impact in OPM due to discontinued programs. Headline profit grew 18% with good growth in adjusted operating profit partially offset by FX and portfolio changes.

Virtual Schools

Virtual Schools performed strongly driven by 43% enrolment growth in new and existing schools for the 2020/2021 academic year. We opened three new full-time, state-wide partner schools and, combined with two contract exits, this takes the total partner schools to 43 in 29 states. We are launching two new partner schools in Florida and Oregon for the 2021/2022 academic year.

Online Program Management

In OPM, we saw good sales growth with a strong performance in undergraduate and international, partially offset by discontinued programs. We also saw the benefits of the operational changes made earlier this year, with increased efficiencies in our student recruitment process and student acquisition costs. Underlying course enrolments (excluding discontinued programs) grew 20% and total course enrolments declined 7%. We are delivering 470 programs across 34 partners globally. We launched Pearson Pathways, a digital marketplace that provides learners with tailored recommendations for courses and credentials to help them achieve the skills they require.

People of **Pearson**

As a young black woman and as a part of the LGBTQ+ community, it is important that I am educated, because in many ways the world is built against me. **For me, learning means power, freedom and the breaking of generational curses**. I learn for myself, my family, my ancestors, my future children and the generations to come long after I am gone.

Tori Johnson
Online Program Management
Illinois, USA

Learning can **change who you are**, how you think, and essentially, mould you.

Martha Castro
HR Business Partner, Human Resources
New York, USA

1 For all financial metrics in this section please refer to note 2 of the financial statements on p150 where adjusted measures for each segment are reconciled to the equivalent statutory measures.

Segmental performance

Global Assessment

Revenue
£892m
(14)% 2019: £1,031m

Adjusted operating profit
£245m
(30)% 2019: £351m

In Global Assessment, sales declined 14% on an underlying basis and 13% on a headline basis.

Adjusted operating profit declined 30% in underlying and headline terms due to the COVID-19 impact on trading, partially offset by mitigating actions.

Pearson VUE

Sales declined 10% at Pearson VUE, reflecting the impact of the test centre closures in the first half of the year, with pent-up demand in the second half partially moderated by further lockdowns in Q4. Online proctoring saw strong growth in the year, with volumes up from 0.2 million at the end of 2019 to 2.1 million at the end of 2020, predominantly driven by demand from the IT sector. Overall testing volumes were down 22% to 12.9 million due to test centre closures.

School and Clinical Assessment

In School and Clinical Assessment, cancellation of spring testing and school closures impacted both businesses respectively in H1 with a further modest impact due to COVID-19 in H2.

WATSON-GLASER CRITICAL THINKING APPRAISAL
OUR FOCUS ON LEARNER OUTCOMES

Preparing for success

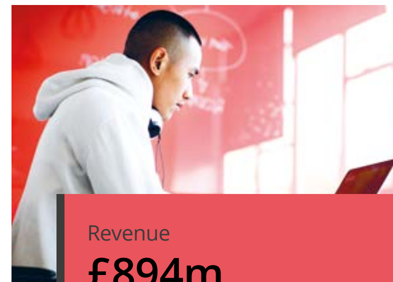
Bringing accurate assessment of critical thinking.

Critical thinking is essential for success in education and the workplace. Mentions of critical thinking in job postings in the US more than doubled between 2009 and 2014. The Watson-Glaser Critical Thinking Appraisal – part of Clinical Assessment – assesses information, interprets it and draws logical conclusions.

Thousands of organisations, colleges and schools use this to hire great managers, develop high-potential employees and admit students into challenging programmes. Studies comparing Watson-Glaser scores with a number of on-the-job performance indicators have found positive correlations suggesting that test-takers who perform well on the Watson-Glaser are also likely to perform well at work.

Learn more:
Watson-Glaser

North American Courseware



Revenue
£894m
(13)% 2019: £1,091m

Adjusted operating profit
£190m
(20)% 2019: £231m

In North American Courseware, sales declined 13% for the full year on an underlying basis and 18% on a headline basis, reflecting the sale of US K-12 Courseware.

Adjusted operating profit declined 20% in underlying terms, due to the impact of trading partially offset by restructuring and discretionary savings. Headline profit was down 18% on last year due to the underlying profit reduction partially offset by the disposal of our US K-12 Courseware business in 2019.

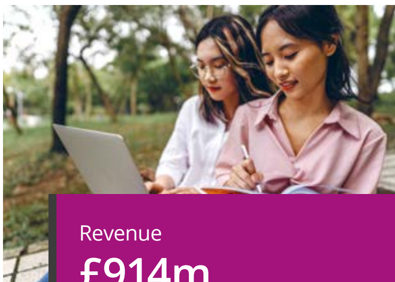
US Higher Education Courseware

US Higher Education Courseware sales declined 12% with total unit sales increasing slightly and digital registrations, including eTexts, growing 9%. In Canada, courseware sales were down significantly due to school and bookstore closures.

We continued to see unbundling of premium priced print and digital products for digital-only formats. In 2020, 2.2m textbooks were sold into US Higher Education colleges, compared with 3.7m in 2019. Sales of standalone eText units into colleges grew 33% to 3.7 million units, showing signs of secondary market recapture.

There has also been continued momentum in Inclusive Access with sales to not-for-profit institutions up 29% on last year, representing 13% of US Higher Education Courseware revenue.

International



Revenue
£914m
(19)% 2019: £1,161m

Adjusted operating profit
£182m
(39)% 2019: £299m

In International, sales were down 19% on an underlying basis due to the interruption of Australian immigration and test centre closures impacting PTE, as well as budgetary pressures caused by the impact of COVID-19 on courseware purchasing. Revenue declined 21% on a headline basis due to foreign exchange and underlying performance.

Adjusted operating profit declined 39% in underlying and headline terms due to the impact of trading partially offset by mitigating actions.

For School & HE Courseware, budget constraints and school closures have led to fewer purchases. In the UK, qualifications revenue was impacted, as expected, by the cancellation of exams in 2020, as well as the end of the NCT contract. In our franchise business in Brazil and across courseware, we have seen market contraction as a result of the pandemic.

PTE volumes were down 36% with declines in all key markets, except China where we saw 17% growth due to an improved competitive performance.

BTEC
OUR FOCUS ON LEARNER OUTCOMES

Job satisfaction

Health and Social Care BTEC is a favoured route for the key workers of the future.

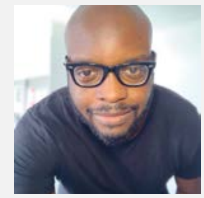
Since the initial development of the BTEC Nationals in Health and Social Care, the evidence has been strong that these qualifications are fulfilling their purpose: to help people get ready for a role in the health and social care sector. These qualifications allow people to select optional areas of study, build up to a larger qualification and keep options for progression open. Students can seek employment after achieving the qualification or use it as a stepping stone into higher education. In 2019, 92% of those taking the qualifications agreed or strongly agreed that they enable them to keep their career options open for the future.

Learn more:
BTEC

Enabling Functions

Enabling Functions costs were 10% lower in headline terms and 9% in underlying terms due to restructuring and discretionary savings.

People of **Pearson**

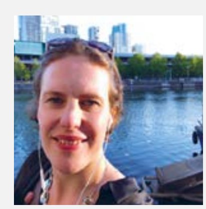


“**My curiosity and appetite to learn and experience new places and cultures** has taken me to over 30 different countries.

Emeka Ibeakanma
Director of Project Management
Melbourne, Australia

“There’s no better way to live than to **live to change someone’s life for the better**, and the only way to do that is to learn.

Rhea Mathur
Pearson Campus Ambassador

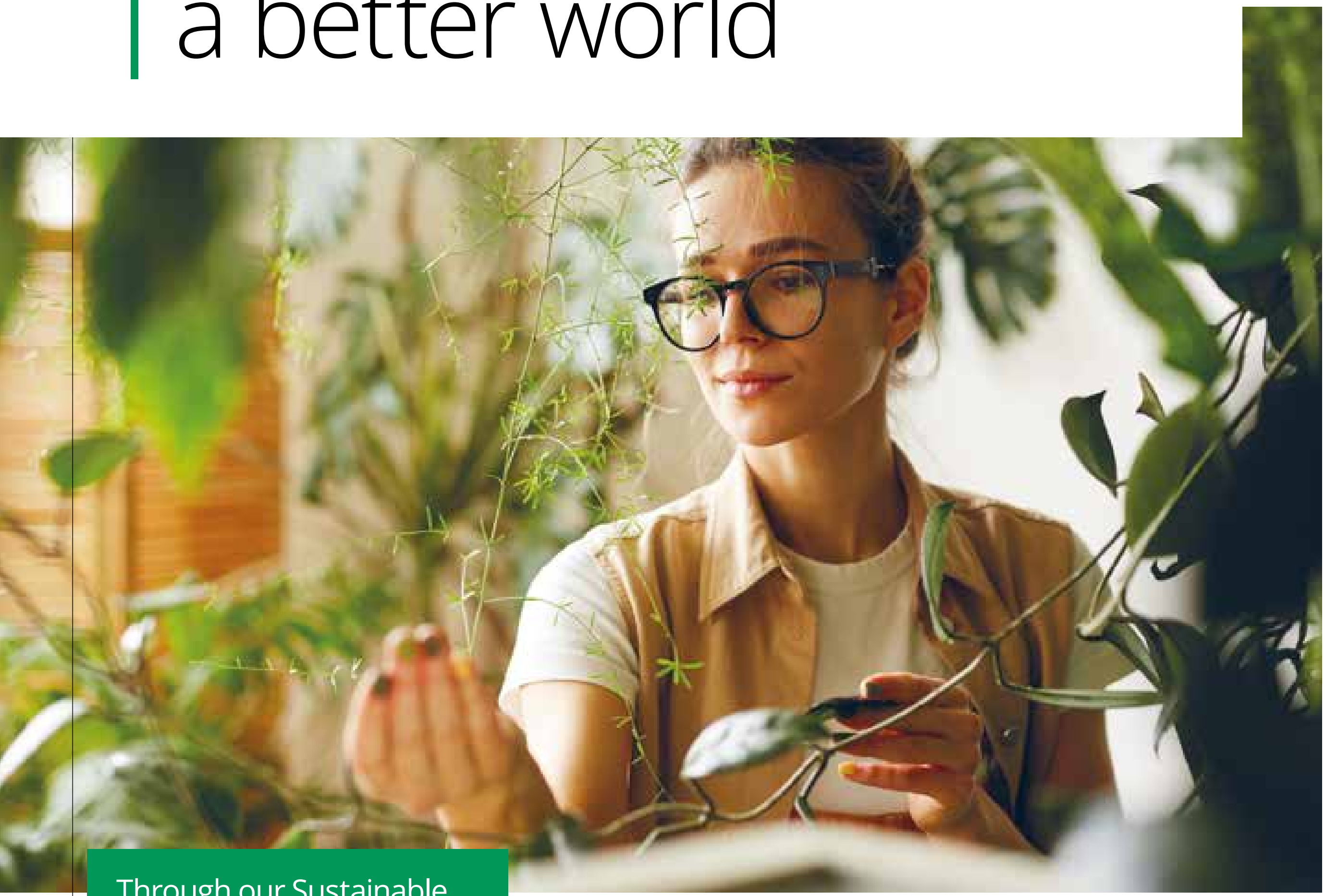


“**It matters that I learn more in my role at Pearson**, as a parent and about things that interest me. Learning sustains my career, my family life, my interest and imagination.

Freya Thomas Monk
Senior Vice President, English Assessment
London, UK

Sustainability

Learning for a better life, a better world



Through our Sustainable Business Plan 2030, we are using our assets as the world's learning company to help more people create a better life for themselves and a better world.

Today, individuals, communities and the planet face existential crises requiring urgent attention. From inequality in education and civil unrest to pandemic and climate crisis, our planet and our society need an all-hands-on-deck approach to address these challenges.

At Pearson, we have a long history of contributing to addressing social and environmental challenges and upholding high standards of ethics and governance. From being a founding signatory of the UN Global Compact in 2000 to the progress we made at the conclusion of our 2020 Sustainability Plan, addressing environmental, social and governance (ESG) issues is part of who we are.

The historic events of 2020 have made our commitment to sustainability more important than ever. Our work to support our consumers and employees throughout the COVID-19 pandemic demonstrates who we are as company (see p27). The year was also marked by an enormous grassroots call for social justice and to recover from COVID-19 with a focus on social equity and the environment (see more from our Global Learner Survey on p15)

Following these pivotal events, we are sharing an evolved articulation of the 2030 sustainability strategy announced last year to expand our commitments and ensure we are focusing on the areas most important to our stakeholders and where we can drive the most impact. As part of this evolution, we have renamed our pillars to better articulate our objectives, though our focus areas remain the same.

Our Sustainable Business Plan 2030 outlines our renewed vision: a world of opportunity, where every person on the planet has access to quality education and lifelong learning that empowers them to improve their own lives, their communities and the planet. We will achieve the better world we envision and contribute to long-term business growth through focus and tenacious commitment to advancing:

- **Learning for everyone:** reducing barriers and measurably increasing equity for underserved groups
- **Learning for a better world:** leading the transformation to build the skills to impact society and the planet
- **Leading responsibly:** creating a culture and running a business that prioritises how we improve our impact on climate change and human rights

> The Sustainable Business Plan 2030 creates value for all our stakeholders – consumers, employees, investors, policymakers and others – through our products and services, our partnerships, and how we operate. The Plan and our new corporate strategy reinforce one another, working together to drive both business success and societal impact.
>
> **Erika Webb-Hughes**
> Vice President, Sustainability

2020 highlights

- Introduced a £350m social bond to support education for underserved groups, see p44
- Announced our science-based target to reduce our GHG emissions by a minimum of 50% across scope 1, 2 and 3 by 2030, see p46
- Increased transparency through new reporting on racial and ethnic diversity, Task Force on Climate-related Financial Disclosures (TCFD), which we have also joined as supporters, and Sustainability Accounting Standards Board (SASB), see p47 and 54
- Created a 'report potential bias' portal on Pearson.com to encourage dialogue about diversity in products and services, see p45
- Added new sustainability-related units in BTEC qualifications, see p45

Our strategy and targets

Our sustainability framework was developed based on a materiality analysis that considered how Pearson's business priorities and stakeholder expectations have changed and are likely to evolve. Our materiality analysis was undertaken in consultation with Forum for the Future, a well-respected sustainability charity. Read more about our materiality analysis, as well as additional Key Performance Indicators (KPIs), in our Sustainability & ESG supplement on our website at plc.pearson.com/en-GB/purpose/esg-reporting.

As we approached this work, we have taken several key considerations into account:

- Linking to business priorities: our process was designed to align with and support our corporate and brand strategy
- Engaging with our stakeholders: we engaged with key stakeholders to understand the issues most important to them and where they expect Pearson to play a role
- Identifying current and future trends: we conducted futures research to help identify the social, environmental and economic issues that will influence learning, our ecosystem of partners and Pearson's business in the years to come
- Supporting global goals: we will continue our commitment to advancing the UN SDGs (especially 4, 8 and 10) and leverage their targets and indicators in our goal-setting

Since the launch of the sustainability framework in 2020, we continued to make progress towards our strategic focus areas and collaborated across our company to build targets. By design, our new strategy is integral to Pearson's business, and everyone in the business will need to play a role in achieving the goals. It will require all parts of our company, along with external partners from businesses, NGOs and governments, to achieve our objectives.

Note: As we embark on a new corporate strategy with our five new divisions, our approach to sustainability will continue to be dynamic and evolve to align with how we can best deploy our business capabilities for societal impact. Some of our objectives, followed by an asterisk (*), are commitments to areas we will advance. While we are already progressing work in these areas, as outlined in this section, we are also working internally in 2021 to set measurable and timebound targets that will be aligned in scale and match the focus areas of our new corporate strategy. We will release targets in these areas in our 2021 annual report or before.

See table overleaf

Sustainability

Pearson's Sustainable Business Plan 2030

Learning for everyone

Reducing barriers and measurably increasing equity in learning.

Learning for a better world

Leading the transformation to build the skills to impact society and the planet.

Product

Access and inclusion

- We will increase access to learning for underserved groups through new and existing products and partnerships, identifying strategies to overcome barriers. These groups include, but are not limited to, women, racial minorities, low-income groups and people with disabilities*

Representation in content

- We will strengthen existing and create new processes, Editorial Policy, and partnerships to eliminate bias and represent the consumers we serve, including based on race, ethnicity and gender, in our products and through our content providers by 2025

Sustainability and social responsibility in content

- We will integrate sustainability, social responsibility and Diversity, Equity & Inclusion (DE&I) knowledge and skills into our content, qualifications and online programmes, preparing people to make an impact in their jobs and lives*

Empowering educators, employees and suppliers

- We will develop and disseminate tools and resources to help educators bring sustainability into their classes*
- We will provide opportunities to all employees and suppliers to access content, courses and training to explore sustainability, social responsibility and DE&I issues by 2023

Leading responsibly

Creating a culture and running a business that prioritises our impact on climate change and human rights.

People

Human rights

- We respect the rights of consumers, employees, suppliers and communities, and we consider the human rights impact of our business decisions
- It is important that Pearson maintains safeguards of our customer data while also working with our customers to develop products tailored to their needs

Diversity, Equity & Inclusion

- We are committed to representation at management levels of the company that reflects the racial, ethnic and gender diversity of the geographies where we operate by 2025
- We will source £500m from suppliers who are diverse accredited by 2030

- We will work exclusively with suppliers who respect human rights and promote suppliers who champion DE&I

Employees & communities

- Provide opportunities for employees to use their talent to contribute to sustainability objectives through both their business roles and volunteering

Planet

Net carbon zero

- We will reduce scope 1, 2 and 3 emissions by 50% against a 2018 baseline as approved by the Science Based Targets Initiative by 2030
- We will be net zero across scope 1, 2 and 3 by 2030

Environmental footprint of products

- 100% of paper products will be Forest Stewardship Council (FSC) certified by 2025
- We will ensure all products and packaging are widely recycled or covered by a take-back programme by 2025
- We will design digital products for energy efficiency

Our priority UN Sustainable Development Goals

* **Note:** While we are already progressing work in these areas, as outlined in this section, we are also working internally in 2021 to set measurable and timebound targets that will be aligned in scale and match the focus areas of our new corporate strategy. We will release targets in these areas in our 2021 annual report or before.

Learning for everyone

Reducing barriers and measurably increasing equity in learning.

We want our products and services to help more people make better progress – regardless of their income level, the way they learn or their background. Improving access to quality education for more people from all backgrounds helps us to grow our business and supports our commitment to quality education for all, decent jobs and equality in line with the UN SDGs.

2020 has been a seminal year for improving diversity as events in the US and other parts of the world brought race and ethnicity into sharp focus. Pearson listened and engaged frequently with our employees and customers. We also convened a 30+ person task force on race and ethnicity to help us identify concrete actions to improve recruitment, retention and inclusion, and to ensure our products and services build a more inclusive society. We brought these important challenging issues to life through global town halls and ongoing discussions with employees across the company, featuring our own employees, students and leadership. The recommendation of this task force has been built into our strategy pillar on learning for everyone.

Learn more online:

plc.pearson.com/en-GB/purpose/learning-for-everyone

Access and inclusion

→ We will increase access to learning for underserved groups through new and existing products and partnerships, identifying strategies to overcome barriers. These groups include, but are not limited to, women, racial minorities, low-income groups and people with disabilities

We know that our business focus on delivering content direct to consumers is an opportunity to impact people from all backgrounds globally and improve outcomes. We are taking steps to better understand the barriers underserved groups are facing and foster innovation to refine or create new products and delivery channels that will help people of all stages and backgrounds overcome their learning challenges. We will work to remove barriers to education for those most in need, both through our core business offering and our partnerships, to enable people to reach their full potential.

Some of these groups include people from low-income or rural backgrounds, first-generation college students, people who do not speak an area's dominant language, people with disabilities, underrepresented minorities, and adult learners and others facing personal constraints, such as the need to balance education with work and family responsibilities. Supporting these groups is central to advancing SDG 4 on education and SDG 10 on reducing inequality.

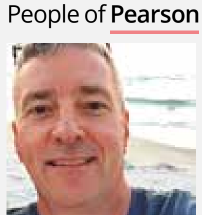
We have a number of products and services that are making a difference for key groups. Three of these are the focus of our social bond launched in 2020 (see p44). Another example is Accelerated Pathways, which partners with employers to implement educational benefits programmes that provide our clients' employees with lifelong learning opportunities. These solutions may include foundational education skills (including reading, writing, English, core job and work skills), pathway to a GED, college advising, accredited courses, degrees and industry or trade certifications. It drives our sustainability objective to advance equity by addressing many of the unique challenges faced by adult learners without adequate and responsive educational opportunities. We are leveraging the research we already do on learner outcomes (see p26) to better understand our impact on people from underserved groups.

We are committed to increasing the number of BTEC registrations outside the UK, particularly in markets where vocational education is developing. In 2020, the Group had 31,112 registrations outside of the UK, which decreased from 43,906 in 2019. The decrease in learner registrations is due to COVID-19 related institutional closures and governments in certain jurisdictions cancelling all academic and vocational assessments in 2020 including BTECs. We recently launched our first sustainability-backed loan, linking to our progress in increasing access to quality vocational education for learners in international markets.

Because equity in access to education is a massive global challenge, collaborating with external partners is critical to making an impact. Our strategic partnerships focus on combining our business assets and capabilities with an external organisation's expertise and reach to create shared value for both our business and society.

In 2019, Pearson and CAMFED (Campaign for Female Education) adapted our vocational BTEC qualification for Learner Guides to make it accessible to all the young women acting as volunteer 'Guides' in CAMFED's programme: not just Guides working in schools but also those supporting girls as they graduate school, and those mentoring young women to set up and grow local enterprises. The revisions also reflect a greater emphasis on employability skills, and new content has been introduced on topics such as sexual and reproductive health and information technology. In 2020 we awarded 1,225 BTEC certificates to Learner Guides, who successfully completed the programme.

People of **Pearson**



I am learning about what I can do to support people who have been marginalised by racism, and support real change. I know that I cannot personally understand many aspects of this movement, but I would like to do this in a way that does not just give lip-service to the issue of systemic racism.

James Reeve
Managing Director, Accelerated Pathways
Toronto, Canada

Sustainability

PEARSON SOCIAL BOND
LINK TO STRATEGY

Investing in equality and sustainability

Pearson issues first-of-its-kind social bond, to benefit underserved learners through ESG-focused initiatives

In June, Pearson borrowed £350m in public markets through the issuance of a social bond – the first to be solely linked to education and used globally for virtual learning and teaching for underserved learners and communities, including those from low-income backgrounds, with disabilities, and the unemployed.

The net proceeds will be used exclusively on sustainability-focused initiatives including: Connections Academy, our full-time virtual schools network; BTEC, which provides vocational qualifications and technical training to help learners progress into the world of work; and the GED which provides the opportunity for US students who did not complete high school to earn a high school equivalency certificate to make further progress in their lives.

The bond refinanced maturities in 2021 and 2022, as well as strengthening the Group's liquidity during a period where lockdowns were in place in many of the Group's major markets. Issuing as a social bond allowed the Group to attract a wider range of investors and demonstrate the Group's strong ESG credentials.

James Kelly, Senior Vice President and Group Treasurer said: "We are committed to helping equip learners with the skills they need to enhance their employability prospects and to succeed in the changing world of work. The social bond is an important measure to further strengthen our long-term liquidity and is a natural progression of Pearson's long-standing commitment to integrating social and environmental sustainability into our business."

We also created a new Social Bond Framework, setting out how this bond will meet strict criteria and align to the UN SDGs, which has been assured at the highest level by Vigeo Eiris, a world leader in sustainable bond issuances.

Learn more online:

Social Bond Framework

Representation in content

→ We will strengthen existing and create new processes, Editorial Policy, and partnerships to eliminate bias and represent the consumers we serve, including based on race, ethnicity and gender, in our products and through our content providers by 2025

Editorial policy

To ensure that the content within our products is aligned to Pearson's values, and to prevent inappropriate content from being published, our Global Editorial Policy acts as a guide for content developers to create products that are relevant, appropriate and inclusive.

Our policy is based on principles in the following areas:

1. Respecting human rights including freedom from discrimination and bias
2. Creating content that embeds an awareness for and the promotion of DE&I
3. Demonstrating support for learning that is based on evidence and facts
4. Aligning with legal and ethical obligations of content creation and production
5. Ensuring content respects regional laws and is not locally inappropriate or offensive

The Policy is applied across all markets and business units, and it is overseen by a cross-regional and functional steering committee, newly chaired by a manager with a specific DE&I content focus. A network of policy champions are responsible for implementation and act as a point of escalation for queries in our businesses and markets around the world. The Policy is to be reviewed in 2021, and it will continue to be overseen by a steering committee and implemented by policy champions.

In 2019, we incorporated the Policy into Pearson's Code of Conduct. An online learning module is automatically assigned to new starters in content-facing and support functions and, for external providers, as part of our vendor onboarding process. To date, over 6,000 employees and 1,500 external providers have completed our Global Editorial Policy training. Policy checkpoints are included in our product development processes, and a Policy review of published titles has also been established in relevant business units.

Race, ethnicity and gender in content

Key DE&I discipline leads in our product teams have completed training on content review, and we have released internal guidelines on race and ethnicity and gender equality to further support our content creators to create bias-free content, integrate best practices and escalate issues.

In December 2020 we created a 'report potential bias' portal on Pearson.com to encourage dialogue with students, instructors, parents and other consumers about Pearson products or services that they feel lack diversity, perpetuate stereotypes or present bias against any group.

In 2021, we will continue to scale up our efforts in this area, including the launch of additional training on commissioning and reviewing content for inclusion and incorporation of our anti-racist principles.

Accessibility and disability

Pearson is committed to continual improvement to increase the accessibility of our products. Our Global Accessibility Steering Group drives support for people with disabilities through the intentional integration of accessibility standards into product development. We have recently publicly shared a new Global Accessibility Policy Framework.

Learn more online:

Global Accessibility Policy Framework

Pearson has joined the Valuable 500, a global movement to put disability on the business leadership agenda. As part of our membership, we have committed to publicly disclose a policy framework for product accessibility as well as to build, develop and share a market-leading approach to mentoring people with disabilities. Pearson also announced a formal agreement with the National Federation of the Blind to enhance the accessibility of Pearson's educational products and courses, deepen Pearson's culture of accessibility, and accelerate the effectiveness of Pearson's accessibility efforts broadly.

See p50 for accessibility for our employees.

Learning for a better world

Leading the transformation to build the skills to make an impact.

One of the biggest ways we can impact sustainability and the UN SDGs as a company is through our consumers, employees and suppliers. We have an opportunity to equip people to understand key societal and environmental issues and develop a sense of social responsibility to take action through their careers and in their day-to-day lives.

Beyond having an impact, this is also an area of increased demand from key stakeholders including students, educators, governments, employers and employees. By integrating sustainability-related content into our products, we can explore new opportunities while making a direct contribution to the UN SDGs and inspiring the next generation to improve their world.

Sustainability and social responsibility in content

→ We will integrate sustainability, social responsibility and DE&I knowledge and skills into our content, qualifications and online programmes, preparing people to make an impact in their jobs and lives

Using our internal expertise on learner outcomes (see p26) and external input, we aligned our criteria for products that teach sustainability and social responsibility. This definition aligns with both the social responsibility strand of our Personal and Social Capabilities (PSC) Framework, which includes multicultural, civic, ethical and environmental elements, as well as aligning with external frameworks like the UN SDGs. Importantly, learning about sustainability includes environmental, social and sustainable development subject-matter knowledge delivered with skills needed to take action, and it fosters socially responsible values and behaviours.

In our English Language Learning courseware, we have embedded our PSC Framework in order to equip learners of English with the language and functional skills to build a more sustainable future. For example, iDiscover, our new course for secondary students of English in Italy, developed in partnership with the BBC, contains content with specific focus on social responsibility.

As part of our future product strategy, the BTEC and Apprenticeship team are currently reviewing all existing qualifications and adding or amending content to include relevant sustainability measures and content for each sector. Sustainable content will be added to all UK BTEC qualifications by September 2022. In the UK, we are working with the University Technical Colleges (UTCs), employers and Professional Engineering Institutions (PEIs) to develop a series of units on environmental/sustainable engineering to support the move towards a more sustainable future with new technologies and manufacturing processes. Forthcoming units will focus on sustainable transport, energy management, renewable energy and environmental sustainability. The BTEC International team have mapped units in Construction, Business and Enterprise and Hospitality in their International Level 3 BTEC suite to the UN SDGs, and this can be seen in the specifications for the relevant qualifications.

In Italy, for each level of school, we have incorporated dedicated sections on the SDGs that include content, resources, exercises and in-depth materials in both paper and digital format. We have also produced and distributed promotional materials on the SDGs, for both teachers and students, such as posters, notebooks and bookmarks, and we featured our Towards 2030 campaign, which highlights sustainability prominently in our textbooks. In terms of digital products, we have *Orizzonti sostenibili* (Sustainable Horizons) through which students and teachers read, discuss and comment on pieces taken from books and other sources through the Pearson Social Reading app.

Sustainability

Empowering educators, employees and suppliers

- We will develop and disseminate tools and resources to help educators bring sustainability into their classes
- We will provide opportunity to all employees and suppliers to access content, courses and training to explore sustainability, social responsibility and DE&I issues by 2023

We know that empowering educators, employees and suppliers with sustainability know-how will have an enormous ripple effect. It is an area of interest for these groups as more and more people want to integrate purpose into their careers. And for employees and suppliers especially, it is a key to equipping them to better contribute to achieving all of our sustainability targets.

With regard to educators in our English Language Learning business, 2021 will also see the launch of our DE&I modules for teachers, a key strand of our Teacher Education and Leadership Academy, which contributes to our target for supporting educators to teach sustainability and social responsibility.

For employees, we relaunched our internal approach to employee learning in 2020. One aspect of this was developing a capabilities framework setting out the knowledge, skills, mindsets and experiences needed to support the ongoing transformation of the company. The development of sustainable business knowledge and skills falls within our core business capabilities. This was brought to life during our first-ever global Learning at Work Week (see p49). Developing capabilities related to DE&I was a key learning pathway through this programme. Going forward, we will use this and other formats to increase awareness about sustainability issues among our employees, including through self-service curated pathways about sustainability in our digital content library, available to all employees, and our accelerated learning and career development experiences, available to our talent.

For suppliers, we also commit to providing training material to all suppliers free of charge, using our unique position as the world's learning company to promote good practice across industry.

Leading responsibly

Creating a culture and running a business that prioritises our impact on climate change and human rights.

Just as important as our commitment to delivering positive outcomes for our customers is our commitment to ensure we act ethically and sustainably. We strive to ensure we always act lawfully and with transparency, support human rights and our employees, and minimise our impact on the planet and the societies where we operate or source products and services from.

Net carbon zero

- By 2030, we will reduce scope 1, 2 and 3 emissions by 50% against a 2018 baseline as approved by the Science Based Targets Initiative
- We will be net zero across scope 1, 2 and 3 by 2030

We are committed to becoming net carbon zero by 2030. The first step on this journey is to reduce emissions. Where we are unable to reduce emissions, we will buy suitable carbon capture 'credits' to meet our net zero target for our scope 1,2 and 3 emissions.

In 2020, we completed a project to map our scope 3 GHG emissions and develop a proposal for the Science Based Targets Initiative (SBTi) to establish our new long-term goal for carbon emissions. Our target to reduce our GHG emissions by a minimum of 50% (from a 2018 baseline) across scope 1, 2 and 3 by 2030 was approved by the SBTi in April 2020. This confirmed that our reduction target is in line with the requirements set out in the Paris Agreement, to limit global temperature rises to 1.5 °C above pre-industrial levels.

KEY PERFORMANCE INDICATOR NON-FINANCIAL MEASURE

Global Greenhouse Gas emissions data

Metric tonnes of CO_2e	2018	2019	2020	2020 %UK
Scope 1 – combustion of fuels	13,057	13,251	**7,251**	**14%**
Scope 2 – electricity (location based)	49,920	47,384	**34,997**	**9%**
Scope 2 – electricity (market based)	4,583	418	**529**	**0%**
Scope 3[1]	596,740	567,245	**346,382**	
Total – location based	659,717	627,881	**388,629**	
Total – market based	614,380	580,914	**354,162**	
Energy use				
UK (gas, electricity and transport) MWh		19,312	**18,526**	**17%**
Global (gas, electricity and transport) MWh		152,231	**107,848**	
Intensity ratios				
tCO_2e per employee (scope 1, 2 market and 3)	25.3	25.6	**16.6**	
tCO_2e/sales revenue (scope 1, 2 market and 3)	148.8	150.1	**104.3**	

1 All relevant Scope 3 categories as defined by the GHG protocol have been assessed.

For 10 of our key markets, we buy renewable energy through green energy tariffs or renewable energy certificates (RECs) in the country of consumption. This accounts for 96% of our electricity use.

Methodology: We have reported on all of the emission sources required under the Companies Act 2006. The method we have used to calculate GHG emissions is the GHG Protocol Corporate Accounting and Reporting Standard (revised edition), using the Scope 2 dual reporting methodology, together with the latest emission factors from recognised public sources, including, but not limited to, the UK Department for Business, Energy & Industrial Strategy, the International Energy Agency, the US Energy Information Administration, the US Environmental Protection Agency and the Intergovernmental Panel on Climate Change. The data in the table above has been independently verified by Corporate Citizenship. Energy use includes gas and electricity consumption in MWh and vehicle fuel use converted from mileage into MWh using BIES conversion factor.

This commitment gives us a renewed focus to reduce our operational (Scope 1 and 2) emissions. It also introduces a new challenge to reduce the 90% of our emissions that are produced in our value chain. To do this we need to engage and work with our suppliers to reduce the carbon embedded in the products and services we buy. Going forward, we will report our carbon reduction against a 2018 baseline in line with our new target.

The COVID-19 pandemic impacted our emissions, and we have seen a 40% reduction in overall emissions (vs our 2018 baseline). Given the significant shift to home working, we have estimated the energy consumption and associated carbon emissions from staff working at home, using our own estimations and calculations in 2020 as no standard methodology exists, and included them in our scope 3 emissions. We will shift to industry standard methodologies as and when these become available.

Our target to become net zero is reflected in our Environment Policy, which also sets our commitment to reduce energy consumption in our buildings. In 2020 we started a refurbishment project for our 80 Strand head office, which includes a number of energy reduction measures and technologies.

Where are our emissions from?

Scope	Source	tonnes (to nearest 500)[1]
SCOPE 1	Buildings and company vehicles	13,000
SCOPE 2	Purchased electricity	4,500
SCOPE 3	Manufacturing and distribution of products (books)	256,500
SCOPE 3	Other/indirect spend	212,500
SCOPE 3	Business travel	26,000
SCOPE 3	Employee commuting	29,000
SCOPE 3	Use/disposal	39,500
SCOPE 3	Other	33,500

1 2018 baseline.

TCFD TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES

Task Force on Climate-related Financial Disclosures

In 2020, we became a signatory to the Task Force on Climate-related Financial Disclosures (TCFD).

The disclosure included below outlines the work we have started to align our climate risk disclosure with the TCFD recommendations. Doing so will enable our stakeholders to understand the ways in which climate change is affecting our business now, and in the future.

It is expected that these disclosures will continue to evolve as the company moves towards full alignment this year, which we will report on in the 2021 annual report. As our response to the TCFD guidelines evolves, we will be reviewing our internal governance structures and ensure climate change risks are included in our strategic group risk mechanisms, ensuring they are appropriately managed and opportunities are seized.

In June 2017, the TCFD published recommendations to encourage businesses to increase disclosure of climate-related information. These recommendations focus on: governance; risk management; strategy; and metrics and targets.

Our progress against these recommendations is outlined below:

- **Governance:** The Board Reputation & Responsibility Committee (see p53) has oversight of sustainability, and as we build climate change risks into our wider strategic risk work, the Audit Committee is likely to take an increased role in managing these risks. During 2021 we plan to build responsibility for climate change risks into the remit of the Responsible Business Leadership Council (see p88)
- **Risk management:** In October 2020, we started work to identify climate change risks to the business. We are currently prioritising the most material risks and opportunities. We will report on these risks in the 2021 annual report
- **Strategy:** During 2021 we are building a strategy to manage potential impacts of climate-related risks and opportunities
- **Metrics and targets:** As part of the overall implementation of our Sustainable Business Plan 2030, we have set a net zero carbon target, which covers our scope 1, 2 and 3 emissions (details on these emissions can be found on p46). Going forward we will define and build out reporting targets and metrics relating to climate change risk mitigation and opportunities

Sustainability

Environmental footprint of products

Pearson has a responsibility to ensure that our products are made from sustainable resources, have a minimal environmental impact during the use phase and can be disposed of in a way that minimises their end-of-life impacts. We are making three commitments in relation to our products:

As part of our responsible sourcing programme (see p52), 100% of paper products will be Forest Stewardship Council (FSC) certified by 2025.

We will ensure all products and packaging are widely recycled or covered by a take-back programme. We will use materials that are recyclable, allowing consumers to use existing recycling systems where they exist. Where we need to use specific materials that are not widely collected for recycling, we will build take-back systems.

We will design digital products to be energy efficient. To better understand how our digital products use energy in data centres, transition to the consumer (over internet or mobile telecoms networks) and in consumer devices, we have joined an industry collaboration called DIMPACTS. The work we are undertaking with this group will help us to measure the baseline energy consumption of digital products and services in order to set targets to minimise the impacts.

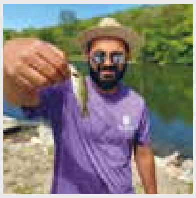
Human rights

- We respect the rights of consumers, employees, suppliers and communities, and we consider the human rights impact of our business decisions
- We are committed to ensuring that Pearson maintains safeguards of our customer data while also working with our customers to develop products tailored to their needs

Our goal is to respect and promote human rights, including the right to education, throughout our operations and with our customers, employees, contractors and supply chain. Our approach is guided by the Universal Declaration of Human Rights, the International Labour Organization's declarations on fundamental principles and rights at work, the UN Guiding Principles on Business and Human Rights, and the UN Global Compact Principles. We are a founding signatory to the UN Global Compact, and we are a member of the Global Compact's UK and USA Local Networks.

People of **Pearson**

We launched an employee engagement community for employees to connect, share stories and support one another. You can meet some of our talented colleagues throughout this report in the People of Pearson callouts.



I firmly believe that learning can have a **transformative effect**, not just on an individual but dozens of family members and future generations.

Haseeb Khan
Director of Digital Platforms, English Assessment
Toronto, Canada

Learning empowers me to be more than a passerby, and to make an impact.

Zerin Anzum Karim
Technology Business Partner, Continental Europe
London, UK

Learning **expands the mind** and creates new opportunities for discussion and growth.

Danette Joslyn-Gaul
Vice President, Global Compliance
Georgia, USA

I truly believe in education as a tool for **changing and impacting** the world.

Lauro Tozetto Neto
Editor & Spectrum Brazil Chair
São Paulo, Brazil

We respect the rights of our employees to freedom of association and representation through trade unions, works councils or any other appropriate forum wherever local laws allow. We have policies and procedures to prevent discriminatory, illegal and inhumane labour practices including child labour, forced labour, slavery and human trafficking, in our places of business, as well as to address violations when they occur.

Representation takes many forms. We support the right to unionise in the UK. Pearson maintains its accreditation by the Living Wage Foundation and has committed to paying employees and regularly contracted staff working in our buildings across the UK and in London the real Living Wage.

We use our influence with our suppliers to improve standards for their employees and commit to ensuring all supplier employees who work for, or on behalf of, Pearson have the ability to report any areas of concern. Read more about supporting our suppliers and our work to prevent modern slavery in the supply chain on p51

Our Human Rights Statement outlines the priority human rights risks and opportunities for Pearson that our programme is taking steps to address. Our approach to human rights covers five areas: customers (pp43–45, p61), content (p44), employees (below), partnerships (p51) and privacy and data (see risk section, p62)

Employees

→ Provide opportunities for employees to use their talent to contribute to sustainability objectives through both their business roles and volunteering

Our employees are central to our purpose of helping people make progress in their lives through learning. As such, we play a crucial role in creating a working environment that enables our employees to learn, grow and succeed. This strategic report describes the numerous ways in which the company engages with, invests in and rewards its employees. The remuneration report also describes the remuneration philosophy which applies to the entire company.

In 2020, we focused on supporting our employees through the pandemic, increasing employee engagement, integrating talent and learning, and expanding benefits. We also expanded our DE&I efforts, outlined on p50.

Employee pulse survey

Survey question	Q1	Q2	Q3	Q4	Average
Ranking of current COVID-19 response on scale of 1–10	9.0	8.3	8.5	8.7	8.6
NPS (recommend working at Pearson to a friend or colleague)	+16	+17	+16	+19	+17
Have taken steps to upskill or reskill in the past quarter	N/A*	71%	60%	57%	63%

* This question was not asked in the Q1 2020 survey.

Employee engagement

Early in 2020, we acted quickly to support our employees around the world and to help them feel safe and connected, as a majority of them began working from home full time. Read more on p13 and pp27–28

Responding to employee feedback helps shape our employee experience, and our new quarterly pulse survey gave us key insights into how our employees were feeling. To support our employees, we launched a new virtual employee community, People of Pearson, where employees can learn about our products and services, share stories and connect with one another.

We established a more frequent cadence of executive communications during the pandemic, with the new Chief Executive holding seven regional town halls in the fourth quarter and sending monthly video updates.

In response to the UK Corporate Governance Code, we are excited to take part in strengthening the voice of our workforce with our Employee Engagement Network (read more on p81)

Aligning talent and learning

In order to deliver on our goal to make the most out of Pearson's world of talent, in 2020, we focused on aligning our approach to talent and learning to the company strategy. This is so that we deliver greater employee and business value. We started by evolving and simplifying our approach to the talent review and designing and integrating a capabilities framework to support upskilling and reskilling led learning.

This spans the core business, leadership and technical knowledge, skills, mindsets and experiences needed to support the ongoing digital transformation of the company. We piloted this with the Pearson Executive Management team and our Pearson Leadership Group, which comprises all Senior Vice Presidents, as well as Vice Presidents that report to the Executive Management team.

Our intention is to expand this to Directors and Managers in 2021. In addition, in our latest pulse survey, 71% of employees who responded shared that they completed quarterly check-ins on performance and learning in the past quarter, and 57% reported doing something to upskill or reskill.

To support employees to upskill and reskill, in the first quarter, we piloted a new early career leadership programme, ILEAD, in International and a new manager programme, Imanage, in the UK. The Wave programme, an initiative to enable experiential, on-the-job learning and employee mobility, was expanded to cover more parts of the business and we made available to employees a further five Pearson Products to support to support upskilling and reskilling – MePro English G, Pearson Prep G, Pearson Writer G, Accelerated Pathways G, Pearson Advance G – and beta tested Pearson Career Courses: project Oz, and ITPro. In the third quarter, we launched our first-ever Global Learning at Work Week, delivering 60 fully online learning sessions delivered by internal and external subject matter experts and Pearson authors, engaging 50% of our employees.

Employee benefits

We offer competitive benefit programmes to support our employees. Our programmes vary globally and include health insurance, disability coverage, retirement savings matching, employee share purchase options, commuter benefits, tuition reimbursement, and programmes that support wellbeing and work–life balance.

In 2020, we expanded US paid parental leave to 16 weeks. All parents, no matter how they become parents, are now eligible for equal parental leave benefits.

Our pandemic response focused on supporting wellbeing, including flexible work from home policies and extending work from home after the pandemic if business needs permit. We announced The Pearson Global WELL programme to provide support, advice and guidance for managing mental and physical wellbeing. We extended the global footprint of our Employee Assistance Programme, expanded our UK network of Mental Health First Aiders, and recruited employee volunteers to act as wellbeing champions.

Sustainability

Diversity, Equity & Inclusion

→ We are committed to representation at management levels of the company that reflects the racial, ethnic and gender diversity of the geographies where we operate by 2025

DE&I has been at the forefront of employees' minds, as social justice became a key theme of the year across the US and globally. A task force of employees across all levels of the company came together to identify concrete, actionable ways to improve recruitment, retention and inclusion, and to ensure our products and services help build a more inclusive society.

As a result of the task force's work, Pearson made a commitment to be an anti-racist company in everything we do. We adopted a set of stretching goals around representation, company culture, product and our role in society. An action plan comprising goals, pillars for action and 50 initiatives for implementation over the next 12 to 18 months underpins our commitment. This includes investment in a new recruitment platform, enhanced leadership development opportunities targeted at Black and ethnically diverse talent, and new guidelines on race and ethnicity to guide our editorial teams. We are also expanding our Global DE&I team under the leadership of a new Chief Diversity Officer, Dr. Florida E. Starks, deepening and widening our investment across the business by adding new people, tools and technology.

A commitment to inclusion and anti-racism is not altruism. A diverse workforce that reflects our customers – whether that be in race, ethnicity, gender, gender identity, religion, disability, sexual orientation, education, learning style, national origin or personality type – means we can better represent and understand the diversity of the communities we serve. We set out the characteristics in our DE&I Statement.

KEY PERFORMANCE INDICATOR | NON-FINANCIAL MEASURE

Women and race and ethnicity in Pearson

Among our seven DE&I priorities is a goal to improve gender representation at the top two levels of the company. At Board level, 45% of our members were female as at the end of 2020.

As a founding member of the 30% Club, we have endorsed and exceeded the target of a minimum of 33% representation of women on the Board and in our Pearson Leadership Group by 2020. The table below sets out our female representation over the past three years. The columns on the right represent male representation. Read more about Board diversity and diversity and talent in executive pipeline on pp86–87.

					Male representation	
Female representation	**2018**	**2019**	**2020**	**2020**	**2020**	**2020**
Board of Directors	30%	33%	**45%**	**5**	**55%**	**6**
Senior leadership[1]	31%	34%	**36%**	**35**	**64%**	**61**
All employees[2]	62%	59%	**60%**	**13,031**	**40%**	**8,810**

While the focus of the gender representation measure is on females, we do recognise that we also have non-binary colleagues in the company. As part of a wider focus on gender identity in 2020, Pearson introduced an option to self-identify as non-binary in our HR systems in the United States. Transparency is a key part of our action plan to meet our goal by 2025 to be representative at management levels of the racial and ethnic diversity of the geographies where we operate. The table below sets out diverse representation, defined as identifying as non-White in the US and UK, and the supplement to this annual report breaks down by ethnicity.

Diverse representation	**US 2020**	**UK 2020**
Senior leadership[1]	**18%**	**10%**
Managers and above	**19%**	**15%**
All employees[2]	**30%**	**17%**

1 Typically, up to two reporting lines from the Chief Executive, the senior leadership are the employee body with responsibility for planning and directing the activities of the company.

2 Total employee figures for composition of workforce are based on a snapshot of employees as at 31 December 2020. Average annual figures for 2020 are used elsewhere in this report and differ due to including seasonal employees at peak periods in our assessment businesses, as well as those who may no longer be employed by the Group at 31 December 2020.

Learn more online:

DE&I statement

We believe everyone in the company plays a part in building a more inclusive culture. Our strategic framework for DE&I helps us harness different perspectives and leverage diversity to spur innovation and growth through an inclusive culture and a working environment in which everyone feels a sense of belonging. Our approach includes:

- a Global DE&I Council led by the Chief Executive to provide strategic oversight and to extend our work into many more markets and countries. The Council includes business leaders, allies and advocates, as well as representatives from our employee resource groups
- a set of seven priorities, which guide our action planning and major initiatives. Our action plan on race and ethnicity adds depth to our efforts
- a global network of DE&I Advocates who provide support to advance our practice in their businesses and geographic locations
- a plan to help our 10 employee resource groups at Pearson evolve and mature. The networks are for women, women in technology, parents, veterans, employees identifying as Hispanic or Latinx, the LGBT+ community, generational differences, people with disabilities, employees of Black and/or African ancestry, and a group representing Black, Asian and minority ethnic people

Disability is an important part of our wider commitment to DE&I (see above). We work to ensure that appropriate procedures, training and support are in place for people with disabilities to ensure fair access to career and progression opportunities. Our Pearson ABLE employee resource group helps improve practice by bringing together people with disabilities in Pearson and accessibility advocates. Pearson is a signatory to Valuable 500, a network of companies committed to disability inclusion through business leadership and opportunity.

In 2020, Pearson received a number of DE&I awards (see p55). Pearson scored 90% in the Disability Equality Index as a 2020 Best Place to Work for Disability Inclusion in the US and achieved a perfect score of 100% in the Corporate Equality Index run by LGBT advocacy group the Human Rights Campaign. We also continued to be recognised as fostering an inclusive culture through our leaders, and Cindy Rampersaud, our Senior Vice President-BTEC and Apprenticeships has, for a second year, been recognised in the 2020 EMpower list of the top 100 ethnic minority business leaders. Cindy also received an award from WeQual which recognises talented women one level below the executive management across the FTSE.

Pearson continues to report on Great Britain gender pay in line with UK regulations. Our work to extend our reporting on gender pay to cover our global operations continues and is on track to report on 2020 later in 2021.

Learn more online:

Gender pay report

Socially responsible procurement

- We will work exclusively with suppliers who respect human rights and promote suppliers who champion DE&I
- We will source £500m from suppliers who are diverse accredited by 2030

At Pearson, we believe in doing business with partners who share our commitment to human rights and the environment – strengthening our supply chain through shared values and commitments.

In 2020, Pearson purchased c.£2bn of goods and services from third parties, from large multinationals to smaller specialist companies and sole traders. Around 80% of Pearson's global spend is represented by 470 suppliers.

The majority of products and services Pearson purchases are sourced from suppliers in OECD countries, predominantly in North America and Europe. Our relationships with suppliers are guided by our commitments to international standards for human rights and environmental responsibility. We are committed to the UN Global Compact and other human rights standards including the Universal Declaration of Human Rights, the International Labour Organization's declarations on fundamental principles and rights at work, and the UN Guiding Principles on Business and Human Rights. The UK Modern Slavery Act also guides our approach.

Learn more online:

Modern Slavery statement

We are a founding member of the Book Chain Project, a partnership between publishers to enhance industry standards relating to labour standards and human rights, product safety, and paper sourcing.

PTNA LINK TO STRATEGY

Awarding commitment

Kirsty Gaythwaite is one of 14 Pearson National Teaching Award Gold Award winners in 2020. Nominated under the 'Outstanding New Teacher of the Year' category, she was selected from thousands of nominations.

Kirsty teaches at Goodwin Academy in Kent, England. Having joined as a learning support assistant to help vulnerable pupils, she was quickly identified as having a talent for teaching mathematics. She continued to work at the school while studying during the evenings and weekends for her diploma in education.

Kirsty was delighted to receive her award: "I feel honoured to have won such a prestigious award for simply doing what I love. Teaching, for me, is a vocation, a passion, a sense of belonging."

Since qualifying as a teacher, Kirsty has continued to put in immense amounts of work to ensure her students succeed. She regularly organises lunchtime revision sessions, afterschool interventions, and constantly communicates with parents, all to make sure her students have the best possible chance when it comes to their exams.

Kirsty added: "Winning this award means so much, not only to me, but to the staff, the students, the parents and carers and the community. Collaboratively, we have worked unbelievably hard to ensure the young people of Deal receive the best education possible."

About the Pearson National Teaching Awards

The Pearson National Teaching Awards are the UK's flagship awards programme for the education community. The awards identify and celebrate leading teachers and organisations from across the UK.

Following a national call for nominations, an in-depth selection process with an experienced judging panel is conducted, including visits to all shortlisted schools. Successful nominees are awarded with a Silver winner status, and ultimately Gold for the national winner.

Gold winners are announced at a national ceremony, broadcast on the BBC and attended by hundreds of guests, including senior politicians and education leaders.

Learn more online:

The Pearson National Teaching Awards

People of **Pearson**

"I'm **always learning** because the culture is always changing.

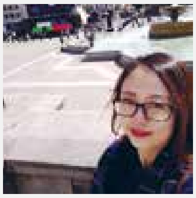
James McKnight
Associate Director, Student Support Services
Florida, USA

Sustainability

People of **Pearson**

Learning can be the only **powerful tool** which can help us navigate the ways in life.

Gracie Zhao
Portfolio Director,
English Henan Province, China



Learning is a tool that helps individuals overcome barriers, seek justice and **reach their full potential**.

Saleem Abu-Tayeh
Pearson Campus Ambassador, Student Programmes
Florida, USA

In 2021, we will be further building on these commitments to establish our Socially Responsible Procurement (SRP) framework. The purpose of this framework is to build a shared set of principles with our supplier partners, to focus on how we can improve global industry standards through education, and ensure joint accountability built on mutual trust. The framework will comprise four pillars and is underpinned by our Responsible Procurement policy.

Learn more online:

Responsible Procurement policy

The four pillars within the framework are:

- Carbon reduction
- Diversity, Equity & Inclusion
- Ethical production
- Modern slavery

Pearson takes reports of ethical concerns within our supply chain seriously. Such issues can be reported through our Pearson Ethics and Compliance Portal – a dedicated service for all employees, suppliers and business partners to report any unethical behaviour for investigation.

It is the duty of our suppliers, contractors, business partners and employees to report any breach of our Code of Conduct, including dishonesty, corruption, fraud, labour and human rights concerns, environmental damage or any other unethical behaviour through the Pearson Ethics and Compliance Portal.

Sourcing policies

Our policies help ensure Pearson's values are reflected and shared with everyone we do business with. The Business Partner Code of Conduct (Partner Code) clarifies the responsibilities and expectations we have of our business partners (which includes joint venture partners, vendors, franchisees, distributors, suppliers, contractors, consultants and agents) for ethical and responsible business practices.

The Partner Code sets out our support for environmental stewardship, universal human rights (including equal employment, freedom of speech and of association, and cultural, economic and social wellbeing), good labour practices, and decent working conditions. It also sets out expectations that our supply partners, and their subcontractors, oppose discriminatory, illegal or inhumane labour practices, including slavery and human trafficking. The Partner Code is present in new contracts and is included when contracts are renewed or updated. Compliance with the principles in our Code is a minimum standard of behaviour outlined in contracts and Pearson is committed to working exclusively with suppliers that share and enhance our values.

Our Business Terms of Reference, specific to Pearson's supply chain contracts, set out the terms and conditions for purchase of goods and services, and are agreed prior to engaging suppliers. This provides Pearson with the power of audit and right to terminate a relationship if we find issues of non-compliance, ensuring our responsible purchasing principles are contractually enforceable.

When working with schools and campuses, suppliers must have an acceptable safeguarding policy which meets or exceeds Pearson's own. Suppliers are also subject to Pearson's Anti-Bribery and Corruption Policy (see p62) and Gifts and Hospitality Policy.

Learn more online:

Anti-Bribery and Corruption Policy

Gifts and Hospitality Policy

In 2021 we will be conducting a full review of our sourcing policies in conjunction with the Socially Responsible Procurement framework to introduce greater weighting for suppliers who contribute to our goals. Suppliers will be asked to disclose more information on their own internal policies, procedures and commitments on all aspects of the framework during the bid process to ensure we select the right partners.

We have committed to providing education content and resources to all suppliers by 2023. As part of the SRP framework, we will be offering targeted resources and support to those supplier partners who need it the most.

Direct supply chain

While we have a growing technology-enabled supply chain reflecting our increasing shift to digital, our traditional paper-based products continue to receive significant focus – reflecting our commitments to sustainability and resilience. Our Global Operations teams manage our purchase of paper for books, our contracts with printers and work with distributors and freight partners who bring our products to market.

Paper sourcing

Pearson has a long-standing Responsible Paper Sourcing Policy supporting management of risks related to human rights and environmental practices in our direct supply chain. This policy sets out our preference for paper suppliers that hold Forest Stewardship Council (FSC) certification. In addition, our Sustainable Business Plan 2030 sets a target for 100% FSC by 2025 (see also p48)

In 2020, we purchased over 35,000 tonnes of paper globally. To help to reduce our impact, we have retained Chain of Custody accreditation from the FSC in the UK, which enables Pearson products to carry the FSC logo. Of the more than 8,000 tonnes of paper we purchased in the UK, 61% was certified to the FSC standard. The overall tonnage is down from 2019 as we have continued our transition from print to digital, sold the Savvas business and experienced short-term impacts during COVID-19.

In the US Higher Education Courseware business, paper procurement, print manufacturing, warehousing and distribution operations are outsourced to LSC Communications, which is subject to our Business Partner Code of Conduct. In 2020 LSC purchased more than 8,000 tonnes of paper in support of Pearson's manufacturing needs, 25% being certified to the FSC standard. Globally 32% of the paper used is certified FSC.

Print production

We rely on third-party suppliers to print our textbooks and course materials. Globally, we have a diverse and resilient supply base of over 160 print partners covering approximately £118m in spend. This decrease in spend from 2019 also reflects our digital transition, sale of Savvas and short-term impacts during COVID-19.

Where Pearson spend with a new supplier will be greater than £100,000 per annum, and the supplier is identified as operating within a higher-risk country (using the Book Chain standard), Pearson will require the supplier to evidence a valid audit from an acceptable independent third-party body. The Book Chain standard is utilised to help publishers identify labour and environmental risks in the supplier chain.

Acceptable third-party audits under the Book Chain standard include, but are not limited to, Sedex Members Ethical Trade Audit (SMETA); ICTI Care process (now the Code of Conduct Audit), and the Social Accountability 8000 certification (SA8000).

Our due diligence process also includes visiting suppliers around the world to assess compliance with our standards, and to ensure suppliers address non-compliance. These visits provide a valuable opportunity to reinforce our commitments to eliminating all forms of child, forced and compulsory labour, as well as promoting environmental stewardship.

In the UK business we had £18m in spend with 34 suppliers in total. Of these, we have identified four suppliers, representing £3m in spend, as high risk based on country of operation (China and Malaysia), guidance from the Book Chain Project and meeting our £100,000 materiality threshold. While none were visited in 2020 due to the impacts of COVID-19, independent audits were conducted for two of the four vendors in 2020, and all four were visited in 2019 to ensure compliance with agreed standards.

Indirect procurement

Following deployment of systems in the UK, US and Canada, new supplier requests are tracked and subject to an auditable risk assessment. Suppliers submit onboarding information directly and securely through our platform, where risk is assessed, as relevant, against: conflict of interest, trade sanctions, sanctioned countries, data privacy, system security, safeguarding, compliance, sustainability, physical security, diversity, and business continuity. During 2020, we deployed systems to Japan, Singapore, Thailand, Malaysia and the Philippines deploying equivalent processes.

Contingent workers

Allegis Global Solutions (AGS) is the major partner supporting Pearson's relationships with our contingent workforce population. Our contingent workers frequently fill roles such as engineers, developers, exam graders and project managers.

AGS, and our other partners, help Pearson ensure our contingent workers receive detailed information outlining how Pearson's people policies apply to them, and help to hold contingent worker agencies accountable for ensuring that workers are informed of these policies.

Supplier diversity

As part of Pearson's commitment to being an anti-racist and anti-discriminatory organisation, we have an established supplier diversity programme focusing on local, small, diverse businesses – such as underutilised, or women, minority, LGBT or veteran-owned businesses. As part of our SRP framework, we are continuously looking for ways we can expand the reach of this programme to our larger suppliers who do not fit the traditional accreditation criteria – but equally have a material part to play in driving change. 2021 will see greater focus on our sourcing policies to ensure we work with suppliers who share and enhance our values and raising industry standards through education and resource.

Supplier risk

Our 2021 supplier risk programme includes the launch of a revised supplier risk framework with focus on: social, ethical and environmental; compliance; operational; financial and business continuity concerns. In parallel with clear supplier segmentation, Pearson is now better placed to execute a sustainable assessment of suppliers and will concentrate on improving the efficiency, effectiveness and breadth of risk assessment through the continued investment in technology and partnerships.

Governance

Sustainability governance

The Reputation & Responsibility Committee, a formal committee of the Board, provides ongoing oversight, scrutiny and challenge on matters relating to our sustainability strategy and our corporate reputation. Learn more on p88

The Pearson Executive Management team oversees implementation of business and sustainability strategy. The Responsible Business Leadership Council drives implementation of the strategy on behalf of the Board. It comprises leaders from across the business. In 2021, we will review the Group's composition in light of our business strategy and build in climate risk oversight in connection with TCFD (see p47)

Code of Conduct

The Pearson Code of Conduct underpins our values by setting out the global ethical, social and environmental standards of behaviour we expect from employees, and we have a companion code for business partners.

Our Code of Conduct was revised and refreshed in 2020, and the course included a focus on raising concerns, a certification to the Code and an overview of our Global Conflicts of Interest Policy and disclosure process. In addition, in 2020 we sought input from our DE&I task force and included language to reaffirm our commitment to being an anti-racist organisation through a number of different amendments to our Code of Conduct.

We make sure all Pearson employees are aware of our Code and affirm that they understand and will comply with it. In 2020, we achieved our target of 100% employee completion and acknowledgement of the Code by all employees. The Code is also assigned as part of the onboarding process for all new Pearson employees.

Raising concerns

We operate a free, confidential telephone helpline and website for anyone who wants to raise a concern, and we have a clear Raising Concerns and Anti-Retaliation Policy in place to encourage honesty and openness. Cases that pose significant risks to our business are reported to the Pearson Audit Committee with ultimate ownership by the Board.

Sustainability

Sustainability Accounting Standards Board (SASB) Index

For the first time, we are providing an index of the metrics we are reporting in response to the SASB standards. Because of the nature of our business, we are reporting metrics from the Media & Entertainment, Internet & Media Services, and Education standards. In some cases, we have omitted metrics, and we will undertake work in 2021 and plan to report additional metrics in our next annual report.

Sustainability disclosure topic	Accounting metric	Code	Response
Media & Entertainment Industry Standards			
Media Pluralism	Percentage of gender and racial/ethnic group representation for (1) management, (2) professionals, and (3) all other employees	V-ME-260a.1	See table on p5 and p50
	Description of policies and procedures to ensuring pluralism in news media content	SV-ME-260a.2	While our content is for learning rather than news media, our approach to pluralism is reflected in our work on representation in content on p44
Journalistic Integrity & Sponsorship Identification	Description of approach for ensuring journalistic integrity of news programming related to: (1) truthfulness, accuracy, objectivity, fairness, and accountability, (2) independence of content and/or transparency of potential bias, and (3) protection of privacy and limitation of harm	SV-ME-270a.3	We have an Editorial Policy that applies these standards to our educational content. See p44
Intellectual Property Protection & Media Piracy	Description of approach to ensuring intellectual property (IP) protection	SV-ME-520a.1	See p62 in the principal risks section
Internet Media & Services Industry Standards			
Environmental Footprint of Hardware Infrastructure	(1) Total energy consumed, (2) percentage grid electricity, (3) percentage renewable	TC-IM-130a.1	See our Sustainability & ESG supplement: plc.pearson.com/en-GB/purpose/esg-reporting
	(1) Total water withdrawn, (2) total water consumed, percentage of each in regions with high or extremely high baseline water stress	TC-IM-130a.2	See our Sustainability & ESG supplement for (2): plc.pearson.com/en-GB/purpose/esg-reporting
Data Privacy, Advertising Standards & Freedom of Expression	Description of policies and practices relating to behavioural advertising and user privacy	TC-IM-220a.1	See p62 for in the principal risks section for a description of privacy
Data Security	Description of approach to identifying and addressing data security risks, including use of third-party cybersecurity standards	TC-IM-230a.2	See p62 in the principal risks section
Employee Recruitment, Inclusion & Performance	Employee engagement as a percentage	TC-IM-330a.2	See KPIs on p5 and p49
	Percentage of gender and racial/ethnic group representation for (1) management, (2) technical staff, and (3) all other employees	TC-IM-330a.3	See KPIs on p5 and p50
Education Industry Standards			
Data Security	Description of approach to identifying and addressing data security risks	SV-ED-230a.1	See p62 in the principal risks section
	Description of policies and practices relating to collection, usage, and retention of student information	SV-ED-230a.2	See p61 in the principal risks section

Non-financial information statement and more information

The following table outlines where the key contents requirements of the non-financial information statement (as required by sections 414CA and 414CB of the Companies Act 2006) can be found in this document.

Visit our website at plc.pearson.com/en-GB/purpose/esg-reporting for a complete set of our environmental, social and governance performance data and information about how we are aligning with the SASB (also see prior page), TCFD (see p47), Global Reporting Initiative (GRI), Carbon Disclosure Project (CDP), UN Global Compact and UN Sustainable Development Goals.

Reporting requirement	Pearson policies and procedures	Section of annual report
Environmental matters	Environmental Policy Paper Policy	Net carbon zero, pp46–47 Environmental footprint of products, p48 Socially responsible sourcing, pp51–53
Employees	Code of Conduct Human Rights Statement Raising Concerns and Anti-Retaliation Policy Health & Safety Policy Diversity, Equity & Inclusion Statement	Our employees, pp49–50 Diversity, equity & inclusion, p50 Code of Conduct, p53
Human rights	Human Rights Statement Editorial Policy Modern Slavery Statement Safeguarding Principles	Human rights, pp48–49 Editorial Policy, p45 Our employees, pp49–50
Social matters	Human Rights Statement	Our Sustainable Business Plan 2030, pp41–42 Learning for everyone, p43 Learning for a better world, p45
Anti-corruption and bribery	Code of Conduct Anti-Bribery and Corruption (ABC) Policy Raising Concerns and Anti-Retaliation Policy Gifts and Hospitality Policy	Legal and compliance, pp62–63
Policy embedding, due diligence and outcomes		Organisational risk management, pp56–64 Sustainability, pp40–55
Description of principal risks and impact of business activity		Organisational risk management, pp56–64
Description of business model		Our business model, pp16–17
Non-financial key performance indicators		Sustainability, pp40–55

Publicly available policies in the list above can be found at plc.pearson.com/en-GB/corporate-policies

Recognition and multi-stakeholder engagement

Awards, ratings and rankings

Initiatives

Organisational risk management

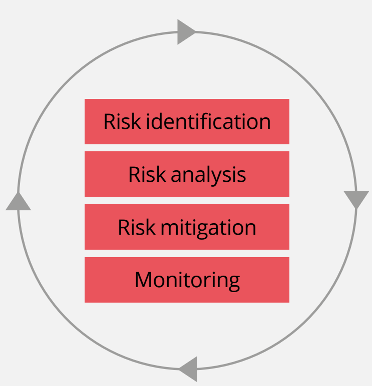
Overview

Our risk management process encompasses the identification, analysis and response to various forms of risk, the establishment of risk thresholds, and the creation of processes intended to mitigate, monitor and manage risks within these thresholds. Across our organisation, we consider risk management an integral part of managing our core businesses and a key element of our approach to corporate governance. The focus is on proactively rather than reactively controlling risk.

We have an integrated process for managing risks throughout our organisation. Our Board of Directors has responsibility for the oversight of risk management, but the required policies, procedures and culture are evidenced by each business unit. A dedicated Organisational Risk and Resilience (ORR) team supervises the risk management activities within each of our business units, providing senior management with a consolidated view of the key risk areas and appropriate responses within the framework provided by the ORR.

ORGANISATIONAL RISK MANAGEMENT

A proactive, pragmatic and proven approach



Understanding current and emerging risks is integral to Pearson's decision-making process. The ORR team supports our businesses by embedding risk management into key processes, supporting the identification, assessment and mitigation of risks taken by the company.

Pearson employs a "Three Lines of Defense" model, with the first line being owned by business leaders, who assume full accountability for the risks in their units. The second line is with the ORR, who review, challenge and report against the risks. The third line is with our Internal Audit (IA) team, who provide independent assurance for the Pearson Board.

Risk governance structure and approach

Our risk governance structure fosters the development and maintenance of a risk and controls culture, encompassing all the significant risk categories impacting our lines of business and functions. The Board of Directors oversees the management of risks through both the Reputation & Responsibility Committee and Audit Committee. Our risk approach aligns to international standards (e.g., COSO and ISO 31000) and aids our continued compliance with the Financial Reporting Council's (FRC) UK Corporate Governance Code guidance on risk management, also enabling us to adapt to any required changes in approach.

In line with evolving good practice, we continue to look at simplifying and clarifying the risks we report. During 2020, the Board of Directors undertook a robust assessment of the current risks facing Pearson, in accordance with provision 28 of the 2018 UK Corporate Governance Code.

Pearson identified 14 principal risks that we rolled forward coming into 2020 and continued to monitor. We expanded this in 2020 in the light of the increased risk presented by COVID-19, making 15 in total. COVID-19 is presented as an exceptional item and the impact it has had on our business is considered across all other risks in the principal risks and uncertainties status table on pp60–63. Pandemic risk remains under constant monitoring with mitigation measures in place. As part of our wider risk efforts, we also consider a range of 'tail' or high-impact, low-probability events that can include: socioeconomic; global recessions/depressions; weather; natural disasters; and long-term global environmental issues.

In addition to the principal risks outlined above, there is an additional set of operational risks which are monitored and reviewed internally throughout the year. The most material are classified as our principal risks and are those which have a higher probability and greater impact on strategy, reputation, operations or a potential fiscal impact.

In 2020, given the exceptional nature of COVID-19, pandemic risk was added and remains under constant monitoring with mitigation measures in place. As part of our wider risk efforts, we also consider a range of 'tail' or high-impact, low-probability events that can include: socioeconomic; global recessions/depressions; weather; natural disasters; and long-term global environmental issues.

Mitigation and controls

Throughout all 15 principal risks, Pearson adopts mitigation activities in the form of internal controls, as part of regular internal meetings and external consultations. These include reviews by the Board, reporting to Pearson's Executive Management team, and monitoring compliance with Pearson policies, international regulations and standards. In addition, there are steering committees and working groups for that meet during the year to ensure compliance and adequate mitigation for a range of risk topics.

The following principal risks also relate to the material issues considered in the sustainability section of this report on p40: Products and services, testing failure, political and regulatory, information security and data privacy, customer experience, and safety and security. The sustainability section also outlines work to strengthen ESG-related risk management through the Task Force on Climate-related Financial Disclosures (TCFD) and Sustainability Accounting Standards Board (SASB), which we are reporting on for the first time.

Principal risks and uncertainties

A fundamental tenet of establishing, prioritising and managing the risk profile of the company is a consistent assessment of the probability and impact of risk occurrence. In common with many organisations and reflecting good practice, Pearson uses a probability versus impact matrix (PI matrix) for this purpose.

Principal risks: status and 2020 change

Net risk

Probability and impact are based on residual risk, i.e. after taking into account controls already in place and assumed to be operating effectively.

The probability of these impacts being realised with current controls and mitigations in place is then considered, to establish an overall impact for each risk, or 'net/residual' risk. This PI matrix and its detailed associated guidance is central to Pearson's risk management framework. Mapping risks in this way helps not only to prioritise the risks and required actions but also to direct the required resource to maintain the effectiveness of controls already in place and mitigate further where required.

The risk reporting process is carried out biannually and reviewed by the Audit Committee and the Board.

The impacts of each risk are assessed across five themes. Executive responsibility for these risks is outlined in alignment with our new organisational structure as of 2021.

			Executive responsibility
Strategy and change	Relates to the key strategic capabilities which underpin our growth and transformation strategy.	1 – Business transformation and change	Chief Executive Chief Strategy Officer Chief Financial Officer
		2 – Products and services	Presidents – Business Divisions Chief Marketing Officer and Co-President, Direct to Consumer Chief Product Office and Co-President, Direct to Consumer
		3 – Talent	Chief Human Resources Officer
		4 – Political and regulatory risk	Chief Legal Officer
Operational	Relates to risks involving people, process, data and systems.	5 – Testing failure	President – Global Assessment
		6 – Safety, safeguarding and corporate security	Chief Financial Officer Chief Human Resources Officer
		7 – Customer experience	Presidents – Business Divisions Chief Marketing Officer and Co-President, Direct to Consumer Chief Product Office and Co-President, Direct to Consumer
		8 – Business resilience	Chief Financial Officer Chief Legal Officer
		9 – Data	Chief Strategy Officer, Chief Legal Officer Chief Product Officer and Co President – Direct to Consumer group
Financial	Relates to risks involving financial planning, investments, budgeting, potential losses of and exposures to Pearson's assets.	10 – Tax	Chief Financial Officer
Legal and compliance	Relates to risks in adhering to applicable laws and regulations.	11 – Information security and data privacy	Chief Strategy Officer Chief Legal Officer
		12 – Intellectual property	Chief Legal Officer
		13 – Compliance	Chief Legal Officer
		14 – Competition law	Chief Legal Officer
Exceptional item	Exposure to the pandemic	15 – Pandemic	Chief Financial Officer, Chief Human Resources Officer

Organisational risk management

COVID-19 impact and efforts

The COVID-19 pandemic has impacted our colleagues, customers and business in terms of revenue and profits. COVID-19 is expected to remain a primary global health and safety concern throughout 2021 and beyond.

Employee impact and response

In 2020, within Pearson, we had a total of 534 infections among our colleagues, which is approximately 2.6% of our global workforce. Sadly, October saw the death of a UK-based Pearson VUE colleague and in February 2021, the death of a finance colleague in South Africa. From the data available, our rate of infection among the workforce is comparable with other multinationals, reflecting both occupational and community-based infection rates. At our half year risk review, our total number of infections was 154. The increase reflects the global and regional trends.

With the health and safety of our employees in mind, Pearson made the early decision to guide employees to work from home (WFH) seven days prior to the official UK Government guidance, in March. As part of our incident management work, we created a range of guidelines based on a three-phase approach. Throughout 2020, Pearson remained in Phase I, with some offices/facilities open with safety measures in place, while the remainder of colleagues worked from home. All company travel was (and remains) suspended, with protective supplies provided to colleagues in Greater China and Hong Kong. Phase II allows for the openings of some premises and movement of staff, as vaccinations increase and reduced the virus spread. Phase III will support post-pandemic measures and new ways of working.

This three-phase model reflects the principles that have guided us through the pandemic, and creates a decision-making framework that allows for a consistent and coordinated approach.

Our response continues to prioritise safety and to ensure mitigating risks. This has required some operational changes to enable continuation of service at our test centres and processing sites. New controls for any return/access to offices, travel and customer engagement activities have been shared in an employee handbook. Work is ongoing to develop future workplace strategies and 'people policies' to reflect new ways of working following the pandemic.

We are also supporting colleagues by raising awareness, sharing resources and promoting wellbeing to help people protect themselves and their families while remaining resilient, regardless of where they are doing their jobs. We continue to develop Group-wide wellbeing initiatives.

PEARSON ACCESS TO OFFICES

Phase I:
Critical operations and access to offices (now)

- Act on medical and government advice/restrictions
- Staff selection and wellbeing (WFH)
- Protective equipment and supplies
- Public transportation
- Measures in an office
- Sales team moves suspended
- Suspension of company travel

Phase II:
Controlled openings (future) – daily measure and behaviours

- Act on medical and government advice/restrictions
- Staff selection and wellbeing (WFH)
- Protective equipment and supplies
- Public transportation
- Measures in an office
- Sales teams and virtual contact
- Suspension of company travel

Phase III:
New norm – agile/blended working, with limited or no measures

- Monitor medical and government advice/restrictions
- Staff selection and wellbeing (WFH)
- Protective equipment and supplies
- Public transportation
- Measures in an office
- Sales team deploy
- Company travel opens, per region

Business impact and response

In 2020 we saw a significant trading impact as a result of COVID-19. The challenging impact of COVID-19 has been felt most acutely across our International and Global Assessment businesses due to test centre and school closures, exam cancellations, reduced global mobility and international economic pressure on spending.

The ongoing uncertainty in 2021 gives rise to potential commercial risks that are actively being monitored by our business and finance teams. The impact from tougher lockdowns, increased infection rates and further operating constraints could restrict access to test centres and affect parts of our International business.

We are actively monitoring our risk assumptions related to COVID-19, including the following:

- We have responded to the UK Government announcements about the cancellation of A Level and GCSE exams in June and July 2021. We continue to work closely with the Department for Education, Ofqual and the other awarding bodies on the teacher-assessed system that is being considered as a replacement for exams and expect any impact on our business to be modest
- Following the decision to cancel international exams, we are working with international partners towards the teacher assessed grades and fairness for those students who were due to take IA Level and IGCSEs
- Additional regional and local lockdowns with stricter social distancing and potentially curfews (in the US) could impact our Pearson VUE business, with test centre operations experiencing pent-up demand and longer timelines to fulfil
- In our Pearson Test of English business, the impact of continued travel restrictions with borders remaining closed will impact both Australian immigration and our UK Secure English Language Test (SELT) offerings, although the longer-term prospects remain strong

Stakeholder impact

In the height of the pandemic, our customers, schools, colleges, universities and learners across the world had little time to adjust to the new world of learning – closing physical sites and quickly moving online. We provided maximum support from the start – on a free basis initially – to deal with the immediate crisis and shift to online courses and classes. We provided access to free content and saw a significant uptake in usage.

We believe that our prompt decision to help our customers in their time of need will lead to strengthened, more durable, long-term relationships.

Looking ahead, our strong customer relationships, the way we supported our customers, and the investments we have made in workplace technologies and remote working have put Pearson in a strong position to continue to navigate and adapt to the ongoing COVID-19 environment.

Brexit

The UK exited the European Union (EU) on 31 January 2020. Given the prolonged negotiation process during the latter part of 2020, we continued our mitigation planning, led by a Steering Committee chaired by the Chief Financial Officer. We worked to identify and mitigate any potential impact on our principal risks, including supply chain and operations (covered in the customer experience risk), tax and data privacy, treasury, workforce mobility and more. By virtue of that analysis and mitigation planning, we have not seen any impact to Pearson operations or colleagues because of Brexit, with no material adverse impact on Pearson as a whole. We continue to have contingency plans in place, as part of normal operational risk measures, to ensure we continue with business as usual.

Principal risks and uncertainties

Principal risks: 2020 status, COVID-19 impact and trend in 2021 change.

Strategy and change

Risk description	2020 activity		COVID-19 impact and 2021 trend
1 Business transformation and change			
The accelerated pace and scope of our transformation initiatives increase our risk to execution timelines and to the business's adoption of change.	As Pearson continues its digital transformation, the efforts to reshape our business processes, systems and operations are making substantial progress. We successfully concluded our major restructuring programme delivering the expected cost efficiencies. We continued to roll out our global Enterprise Resource Planning (ERP) system successfully across our Asia markets.	N ↗	**No impact** – all activities kept on plan. **Trend** – potential for increased risk as new organisational structure and financial reporting processes are realigned in order to pursue the new strategy, as outlined in full year 2020 results and strategy update.
2 Products and services			
Failure to successfully invest, develop and deliver innovative, market-leading global products and services that will have the biggest impact on learners and drive growth.	In our products and services teams, increased provision of digital content, coaching webinars to facilitate the transition to online learning as well as regular dialogues with key customers to identify areas for improvement and opportunities. We also successfully transitioned many students to online and digital solutions to support remote and online learning demands.	M →	**Medium impact** – despite a challenging landscape, we were able to keep pace with the changing needs of our customers' education programmes across our global geographies. **Trend** – constant with matters under good ownership and management.
3 Talent			
Failure to attract and retain the talent we need and to create the conditions in which our people can perform to the best of their ability.	**People development** We continue to monitor retention, workload, morale and our talent succession plans. We created an integrated talent and learning model to help build a more inclusive learning culture for our employees and to realise our ambition of becoming 'the world's leading learning company' inside and out. This included launching our new capabilities framework to support employee upskilling and reskilling, designing a simplified personal development plan for employees, and delivering our first-ever Global Learning at Work Week. **Diversity, Equity & Inclusion (DE&I)** We are committed to being anti-racist and to creating a more inclusive culture where everyone feels a sense of belonging. We created a new Global DE&I task force to help us identify 50 concrete actions to improve recruitment, retention and inclusion, and to ensure our products build a more inclusive society. This included sharing race and ethnicity data for the US and UK to benchmark and measure progress. **Employee engagement** Feedback from employee pulse surveys continues to be encouraging, as we support a focus on learning and development and working flexibly. The arrival of a new Chief Executive will give long-term direction, while simultaneously raising expectations for changes.	M ↗	**Medium impact** – with efforts concentrated on supporting colleagues working from home. New ways, systems, and tools to work virtually, strong line manager support, and frequent communications from the Chief Executive and CHRO, reinforcing the importance of mental and physical wellbeing. **Trend** – potential for increased risk as lockdowns continue to impact physical and mental health of employees. Plans and ownership in place.
4 Political and regulatory risk			
Changes in governments, policy and/or regulations have the potential to impact business models and/or decisions across all markets.	In the UK, we continued to build Pearson's position as a leader, expert and innovator in general qualifications, technical/vocational education and assessment. In the US, we positioned Pearson as an innovator in the education and workforce space, among both parties, in state capitals, on Capitol Hill and with the US administration. Globally, we also maintained positive engagement and dialogues with state, federal and national education bodies.	L →	**Low impact** – we were part of industry representations as the various government relief plans aimed at helping institutional establishments and learners navigate the evolving pandemic restrictions. **Trend** – constant with matters under good ownership and management.

Operational

Risk description	2020 activity		COVID-19 impact and 2021 trend
5 Testing failure			
Failure to deliver tests and assessments (e.g. for UK Qualifications, School Assessments and Pearson VUE) and other related contractual requirements because of operational or technology issues, resulting in negative publicity impacting our brand and reputation.	Our Pearson Performance Centres (PPCs) remained open (where locally permitted) and operational, a testament to our test centre staff. We successfully recertified across a range of regulatory, industry and customer requirements, ensuring our commercial obligations remained fit for purpose. In the UK, the summer exam season for A Level and GCSE exams was cancelled by the Department for Education; as a result we continued to work with regulators and schools towards assisting with the teacher assessment and grading process.	H ↗	**High impact** – significant, with initial restrictions and lockdowns forcing the cancellation of some tests. We pivoted to ensure medical staff were able to take qualifications in support of the pandemic response. **Trend** – potential for increased risk. This is being managed and mitigated as far as possible.
6 Safety, safeguarding and corporate security			
A variety of risks that can cause harm to our people, assets and reputation continue to evolve as our company does. While some risk has reduced due to outsourcing and divestiture, the diverse nature of our people's activities requires continued focus, resource and improvement to reduce the potential for harm. The Pearson H&S policy is approved annually and covers a range of activities, behaviours and requirements across the company.	Throughout 2020, we continued to ensure our colleagues' safety, security and welfare remained a priority. During the year, we transitioned to adopt flexible and remote working practices as the pandemic took hold. Our incident management framework was fully utilised and saw eight regional teams manage day-to-day activities across a range of challenging topics.	M ↗	**Medium impact** – we were able to remain ahead of government announcements and worked through restrictions, with our own phased approach and safe practices put in place. **Trend** – potential for increased risk. This is being managed and mitigated as far as possible.
7 Customer experience			
Failure of either our current (or future) operations, supply chain or customer support to deliver an acceptable service level at any point in the end-to-end journey; or to accelerate Pearson's lifelong consumer, learner strategy.	In 2020, ensuring our customers were able to receive a seamless service and support was a key priority. Despite the changeable working environment, Pearson teams were able to continue supporting learners at home via remote connectivity. Our PPCs and staff were supported and supplied with protective equipment throughout the year.	M →	**Medium impact** – we were able to keep customers informed and supported as the pandemic took hold and delivered new areas of service. Our legacy strength with providers and third parties ensured continued global operations. **Trend** – constant with matters under good ownership and management.
8 Business resilience			
Failure to plan for, recover, test or prevent incidents involving any of our products, customers and our businesses' locations. Incident management and technology disaster recovery plans may vary in ability/comprehensiveness across the Group.	Direct and prolonged incident management support to key office locations following the activation of working from home. Support to business lines as the move to online/digital gained momentum.	L →	**Low impact** – legacy efforts and plans were fit for purpose and agility where challenges presented themselves allowed for a strong response to the pandemic, with positive lessons learned. **Trend** – constant with matters under good ownership and management.
9 Data			
Inability to utilise our data to achieve market intelligence and increase productivity and efficiency, while managing market risk impacts arising from customer concerns around use of student data, may significantly affect management of our core operations and achievement of our strategy objectives.	The introduction of the data-handling model allowed colleagues to enhance our ability to utilise data to achieve market intelligence and increase productivity and efficiency.	N →	**No impact** – all activities kept on plan. **Trend** – constant with matters under good ownership and management.

Principal risks and uncertainties

Financial

Risk description	2020 activity		COVID-19 impact and 2021 trend
10 Tax			
Legislative change caused by the OECD Base Erosion and Profit Shifting initiative, the UK exit from the EU, or other domestic governments' initiatives, including in response to the European Commission state aid decision regarding the UK Controlled Foreign Companies (CFC) exemption, results in a significant change to the effective tax rate, cash tax payments, double taxation and/or negative reputational impact.	State aid – further to the appeal made to the EU General Court, work has continued on the implications of the decision. Post year end Pearson received Charging Notices requiring a payment on account of materially all of the alleged State Aid to be made. A payment of £100m was made on 8 March 2021. The Group expects to recover the funds in due course. The Group continues to be of the view that no provision is required in respect of this issue. Reputational risk – the fourth annual tax report has been published. The GRI 207 Tax Standard is effective for reports and other materials published after 1 January 2021 and we are expanding our tax reporting agenda to reflect this. Legislative changes – the Group continued to assess and monitor proposed changes in the international tax framework, including proposals to address the tax challenges arising from the digitalisation of the economy.	L →	**Low impact** – any tax legislative changes which may occur as a result of the pandemic continue to be monitored. **Trend** – constant with matters under good ownership and management.

Legal and compliance

Risk description	2020 activity		COVID-19 impact and 2021 trend
11 Information security and data privacy			
We have from time to time experienced, and may continue to experience in the future, security breaches of our systems despite our best efforts to prevent them. We also risk failure to comply with data privacy regulations and standards. The above could result in damage to the customer experience, our reputation, and a breach of regulations and financial loss.	**Information security** We continued to review and update security protocols over the data we created, secured, used and stored for adherence to all applicable local and national data requirements. We also evolved and proactively improved our protective cyber capabilities, recognising the increased potential for phishing and other cyber activities/threats detected and warned of during COVID-19. Operating risk saw a reduction as stronger compliance and user control took effect.	L →	**Low impact** – with proven processes and protections in place, allowing colleagues to successfully work from home. Minor system modifications made to ensure controls remain in place and proactive and regular awareness of potential threats shared with colleagues. **Trend** – constant with matters under good ownership and management.
	Data privacy We assessed new laws and regulations that came into being and successfully implemented a readiness plan for the new Brazilian data protection law. We introduced a programme toolkit for use by our Privacy Champions to assess and improve our privacy processes and protocols across the company.	N →	**No impact** – with controls maintained. **Trend** – constant with matters under good ownership and management.
12 Intellectual property			
Failure to adequately manage, procure, protect and/or enforce IP rights (including trademarks, patents, trade secrets and copyright) in our brands, content and technology may impair the value of our core assets, or reduce profits.	In 2020 we continued to reduce our multiple brand identities, streamline and strengthen Pearson's brand, and patent key strategic technology assets. We continued targeted IP enforcement against key third parties of Pearson copyright (piracy), brands and patents.	N →	**No impact** – with controls maintained. **Trend** – constant with matters under good ownership and management.

Legal and compliance continued

Risk description	2020 activity	COVID-19 impact and 2021 trend
13 Compliance		
Failure to effectively manage risks associated with compliance (principally anti-bribery and corruption (ABC) and sanctions risk), including failure to vet third parties, resulting in reputational harm, ABC liability, or sanctions violations. The Compliance & ABC policy is a group wide requirement that ensures colleagues and partners are complaint with our internal guidelines, regulatory and industry standards.	In 2020 we continued to enhance our compliance culture with our annual Code of Conduct being verified by all employees. We saw good improvements across our sanctions compliance, with the risk of exposure reduced as a result. Increased SpeakUp efforts and therefore reporting over the last two years has led us to revise our investigations policy and playbook, and we created a Compliance Council to ensure appropriate governance of decision-making for disciplinary and remedial actions.	N **No impact** – with controls maintained. → **Trend** – constant with matters under good ownership and management.
14 Competition law		
Failure to comply with antitrust and competition legislation could result in costly legal proceedings and fines of up to 10% of global revenue; other financial consequences such as class actions, damages, void contracts could adversely impact our reputation.	We continued to support a global network of Pearson lawyers to ensure continued understanding of and compliance with Pearson's Antitrust Policy, and to spot and escalate antitrust issues in the geographies and businesses they support for purposes of maintaining Pearson's antitrust controls.	N **No impact** – with controls maintained. → **Trend** – constant with matters under good ownership and management.

Risk efforts in 2021 and beyond

We view that managing our Strategic and Change risks are key to the long term viability of the company, provided that we effectively manage our operational, financial, legal and compliance risks.

Reflecting on 2020 and looking ahead to 2021 and beyond, we will refresh our risk landscape to reflect external trends, our own learnings from the pandemic and our new, strategic areas of focus. This will include a refreshed risk profile, continued improvement of our risk management process and developing key risk indicators that support strategic growth and business objectives.

Looking ahead, from 2021 onwards we intend to review our risk landscape and we have identified a series of deep dives that we will be performing that reflect the new direct to consumer and digital company strategy. In undertaking these deep dives we will also use this opportunity to review our principal risks to ensure they continue to reflect our key areas of focus moving forward.

We continue to drive a positive and collaborative risk culture, including improved awareness, key risk indicators and a strong control environment. With a focus that supports our digital transformation and business growth strategies, our risk review programme will continue to partner with accountable business leaders with oversight from our Board.

Risk assessment of prospects and viability

This section should be read together with the full viability statement on p122

Pearson's principal risks, and our ability to manage them, are linked to our viability as a company. These risks have been considered when preparing the viability statement.

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

The Board anticipate the company to continue to trade profitably and retain a strong balance sheet beyond the three-year period, with the ability to meet its obligations as they fall due. This assumption is underpinned by investments made during the three-year plan period which are expected to continue to yield future returns.

The Board discusses the company's three-year plan on an annual basis, taking account of a range of factors including market conditions, the principal risks to the Group, product and capital investment levels, as well as available funding. Pearson's business model and businesses are discussed in more detail on pp16–25

The Group acted in the first half of 2020 to bolster its liquidity, including the issuance of the £350m Social Bond in response to the impact of the COVID-19 pandemic on the business. As a result of the pandemic, the Group anticipates that there will be an impact on profit and cash flows in 2021 due to lockdown and social distancing measures restricting access to Pearson physical locations, including test centres and schools. The impact has been modelled under several scenarios to ensure that the likelihood of a prolonged disruption has been appropriately considered in assessing the availability of funding and our ability to comply with banking covenants. The modelling includes a severe reduction in revenue, profit and operating cash flow to the three-year forecast, to ensure that the Group has adequate resources to manage a prolonged period of disruption.

Principal risks and uncertainties

In considering the viability of the company, the three-year strategic plan has been stressed for a range of negative impacts from the principal risks as set out on pp60–64 of this report.

The key assumptions which underpin our three-year plan are as follows:

1. **Virtual Learning.** Virtual Schools continues to see growth from increased enrolments in new and existing schools. The 'COVID-19 cohort' which drove the 2020 enrolment growth gradually dissipates. Online Program Management grows, with global enrolment in undergraduate and postgraduate online courses accelerating
2. **Higher Education.** There is a continued downward pressure on US Higher Education Courseware from declining enrolments, with a shift in sales mix from print and package to digital impacting pricing. The transition to digital enables recapture of the secondary market, delivering growth from 2022
3. **English Language Learning.** Our businesses are adversely impacted in 2021 by reduced state and private sector spending and lower international migration, but revenues recover from 2022 led by growth in English Assessment
4. **Workforce Skills.** A small division in 2021, workforce is expected to show good growth over the three-year period, driven by strong demand for vocational training and workforce skills
5. **Assessment & Qualifications.** Following a recovery from the impacts of COVID-19 in 2021, our Assessment businesses see growth from contract wins and new digitally delivered products
6. Central functions operate under an environment of continuous improvement in order to reduce costs and offset inflationary increases

At 31 December 2020, the company had available liquidity of c.£1.9bn, comprising central cash balances and its undrawn $1.2bn RCF maturing February 2024. The company does not raise financing through any form of receivables or supply chain financing.

In assessing the company's viability for the three years to December 2023, the Board analysed a variety of downside scenarios, including a severe but plausible scenario where the company is impacted by all principal risks from 2021 (weighted for probability of occurrence) as well as reverse stress testing to identify what would be required to either breach covenants or run out of liquidity.

The severe but plausible scenario modelled an impact from COVID-19 and other risks which in aggregate were significantly greater than seen in 2020 continuing throughout 2021 to 2022.

COVID-19 scenarios included a resurgence, with successive waves leading to retightening of restrictions, social distancing measures restricting access to test centres with potential for exam cancellations, as well as constraints on travel and migration negatively impacting college enrolments and demand for language assessment.

The table below sets out the available liquidity and EBITDA headroom against the Group's tightest covenant in the base case (BC) and the severe but plausible (SBP) model.

Headroom in excess of £bn		H1 2021	H2 2021	H1 2022	H2 2022	H1 2023	H2 2023
BC	EBITDA	0.6	0.6	0.6	0.8	0.7	0.8
BC	Liquidity	1.4	1.3	1.3	1.2	1.3	1.2
SBP	EBITDA	0.5	0.3	0.3	0.4	0.4	0.5
SBP	Liquidity	1.3	1.1	0.9	0.8	0.8	0.7

Further comfort about the viability of the company derives from the assumptions made. Management actions in response to such a downturn were assumed to be limited to the short-term management of direct costs associated with lower sales (e.g. if exams were not taking place, seasonal staff would not be recruited), without assuming reductions in investment in declining business lines or steps to restructure the business which would likely occur in such a significant downturn. Our severe model also assumed that debt repayments due in 2021, 2022 and 2023 would be repaid using cash without refinancing and that dividends would continue at their usual level, which could be cut if absolutely necessary.

The principal risks included in our severe but plausible model included (but were not limited to):

- Reduced sales due to COVID-19 throughout the next three years
- Weaknesses in products and services resulting in lower Group turnover
- Testing failure resulting in penalties and lower Group turnover
- Business transformation failure resulting in increased costs
- Data privacy failure resulting in lower Group turnover and rectification costs
- Breaches of laws and regulations resulting in lower Group turnover and rectification costs
- Tax risks resulting in increased tax payments

Even under a severe downside case where further declines in profitability compared to 2020 are modelled in 2021 and 2022, the Group would maintain liquidity headroom in excess of £700m and comfortable headroom against covenant requirements during the period under assessment. This is before modelling the mitigating effect of actions that management would take in the event that these downside risks were to crystallise.

The Board's confirmation of Pearson's viability for the three years to 2023, based on this assessment, is included alongside the going concern statement on p122

Governance report

In this section

Letter from the Chair

The Board is committed to the highest standards of corporate governance and sustainability, in the interests of all Pearson's stakeholders

Sidney Taurel
Chair

Dear shareholders,

As I have said earlier in this report, 2020 was one of the most challenging years in modern history and I have been particularly proud of the way Pearson colleagues came together to support each other and our learners, customers and other stakeholders.

Undoubtedly, the global pandemic has presented major challenges for travel and physical meetings that the Board would have expected to conduct throughout the year, but I am pleased to report that we were able to continue to operate smoothly and effectively by virtual means. 2020 saw the Board dedicate particular focus to the Chief Executive transition and to supporting both the company's response to the global pandemic and its Diversity, Equity & Inclusion (DE&I) initiatives.

We are committed to the highest standards of corporate governance and the following pages set out further detail on our Board's composition, corporate governance arrangements, processes and activities during 2020, together with our Board Committee reports.

Strategic focus

At the outset of 2020, the Board had reaffirmed its focus on Pearson's three strategic priorities that underpin our vision of being a learner-centric business focused on employability and lifelong learning: the ongoing digital transformation of our traditional courseware and assessment businesses; investing in new structural growth opportunities; and continuing to take steps to be a simpler, more efficient and sustainable business. These were already strategic priorities for the company, which were enhanced and accelerated by the impact of the COVID-19 pandemic.

In 2021, under Andy Bird's leadership, the Board looks forward to supporting the company emerging even stronger from the pandemic to capitalise on the opportunities presented by evolving trends in our markets and the past work undertaken to provide Pearson with the foundation to succeed. To that end, the Board supports the focus on direct to consumer and the plan to reorganise Pearson into five global business divisions, to help drive our future growth.

As part of monitoring performance, the Board regularly receives a dashboard that allows Directors to monitor progress on Pearson's financial and strategic priorities, enabled by critical discussion of these matters at each Board meeting and supported by agreed indicators and milestones which the Board and management have identified as key measures of performance. In 2021, the Board will be working with management on identifying and monitoring new key performance indicators (KPIs) which complement the evolution of the strategy.

The Board's focus on supporting the company and stakeholders through the pandemic included ensuring that the company leveraged its strong balance sheet to retain sufficient liquidity during a period of such unprecedented uncertainty, and maintaining an appropriate capital allocation policy. As I describe elsewhere, the Board views a very strong balance sheet as a priority while uncertainty remains due to the pandemic, and therefore at this stage does not plan to recommence the buyback that was paused in 2020.

During the year, the Board also continued to consider Pearson's portfolio, assessing which businesses are best suited to company strategy, whether to acquire, retain or divest. This included ongoing oversight of the integration of Lumerit Education G and the Smart Sparrow assets acquired in 2019. Separately, the Board approved the divestment of the Pearson Institute of Higher Education G in South Africa, as part of the company's ongoing de-emphasis of physical direct delivery businesses. In addition, we concluded the disposal of our remaining 25% stake in Penguin Random House to Bertelsmann and a partial early exit from consideration arrangements relating to the sale of our US K-12 learning services business in 2019.

The Board supports the plan to review our portfolio further in 2021 to allow greater focus on the priorities of the five new global divisions.

Sustainability, engagement and culture

The importance for all stakeholders in running a sustainable company is a core value for Pearson. Engaging with, and understanding the views of, our stakeholders is imperative to developing and delivering educational products that meet the needs of learners, educators, governments and employers.

Our historic commitment to embed sustainability into all business functions and operations remains unchanged and I have mentioned earlier on in the annual report our Sustainable Business Plan 2030 and our alignment to recommendations from the Task Force on Climate-related Financial Disclosures (TCFD) and the Sustainability Accounting Standards Board (SASB). You can read more on this in our Sustainability section on p40. We are particularly proud of the success of our 2020 social bond and the commitments associated with it – see p44 for more on this.

The Board has always been committed to building on and improving our DE&I. The Board received and inputted to several updates on the work of the DE&I task force formed during 2020 and in 2021 looks forward to supporting its further progress. The Board is committed to driving lasting impact and change through these initiatives and to Pearson setting an example within its industry. You can read more about our action plan over the next 12 to 18 months on p50

The Board remains fully committed to shareholder and broader stakeholder engagement, both through and alongside our Reputation & Responsibility Committee. We very much enjoyed the lunch event held with our largest shareholders in February 2020 and, while engagement has been more challenging in 2020 as a result of the pandemic, the Board feels the company has been successful in maintaining strong stakeholder engagement through virtual channels. You can read more about the Board's engagement with stakeholders in the S172 section on p30

During 2020, Board members continued to engage with the workforce, including considering regular pulse survey reports and meeting with the Employee Engagement Network through our Senior Independent Director, Vivienne Cox. You can read more about our employee engagement initiatives in the Nomination & Governance Committee's report, which begins on p84 and throughout this Governance Report.

Also critical to our success is ensuring a culture that complements the delivery of our strategy. The Board continues to focus on engendering a corporate culture that is inclusive, innovative and meritocratic, and on ensuring that this aligns with the company's purpose, values and strategy. In doing so, all Directors are committed to acting with integrity and leading by example. This report illustrates how the Board has monitored Pearson's culture throughout the year, including through the surveys, Employee Engagement Network discussions and talent initiatives referenced above. I am proud of the ways in which Pearson has sought to support its employees through the many challenges that the pandemic has brought, including new working environments and wellbeing pressures.

Talent, succession and evaluation

Crucial to successful delivery of our strategy is attracting and retaining strong, diverse talent. The Board also considered the wider pool of talent in our senior leadership group, and the themes of talent, succession and DE&I form a continuing thread throughout the Board's and Committees' sessions. The Board conducted a deep dive into the company's new workforce learning and development initiatives, designed to underpin a new talent framework.

At an executive level, under Andy's leadership we recruited a new Chief Strategy Officer, Mike Howells, and a new Chief Marketing Officer, Lynne Frank, who is also serving as Co-President of Pearson's new Direct to Consumer group, alongside Ishantha Lokuge, Pearson's Global Product Officer. These are very strong additions to our executive management team and have already made excellent starts as part of Andy's team, bringing additional energy and expertise.

At Board level, Pearson has a fully engaged Board, including a strong Non-Executive team with a breadth of experience and perspectives, including finance, digital and technology, environmental, social and governance (ESG), education and public sector, direct to consumer and leadership of global organisations through periods of transformation and disruption.

As noted in our 2019 report and elsewhere in this report, following John Fallon's announcement of his intention to retire as Chief Executive during 2020, I promptly accelerated the ongoing succession planning process with the assistance of the Nomination & Governance Committee. Following a thorough selection process, we were delighted to appoint Andy Bird as our new Chief Executive in August 2020 and he succeeded John on 19 October 2020. You can read more about the Nomination & Governance Committee's activities regarding succession planning, and most particularly the Chief Executive search, on p84

In addition to the Chief Executive and Chief Financial Officer appointments in 2020, at the upcoming 2021 Annual General Meeting (AGM) we will bid farewell to both Vivienne Cox, as her nine-year term on the Pearson Board reaches its conclusion, and, as recently announced, Michael Lynton, who will also not be seeking re-election in light of his other commitments. Vivienne and Michael have made tremendous contributions to Pearson, particularly in their respective experience of leading global businesses through times of transformation and digital disruption, for which the Board and I are extremely grateful. They have our very best wishes for their future endeavours.

In relation to our Non-Executive retirements, the Nomination & Governance Committee's established succession plans are well progressed and the Board looks forward to updating shareholders in due course.

Letter from the Chair

The Board evaluation for 2020 was facilitated externally, in accordance with the Code. I am pleased to report that the evaluation found the Board to be well-functioning and operating effectively, with a good quality of relationships between Board members and a strong commitment to Pearson's purpose, backed by sound governance principles and an appropriate level of challenge and support for management. As the Board supports Andy in his early months as Pearson's new Chief Executive, it continues to assess the balance of focus between long-term strategic considerations and near-term delivery, including, for instance, what performance indicators and insights are most effective for monitoring company performance as the strategy develops. You can read more about the Board evaluation process and findings on p82

Audit, Risk and Internal Control

The Board is accountable for Pearson's successes and addressing its challenges. We aim to communicate to you in a transparent manner the steps we have taken to ensure that we have a clear oversight of the business, and the work we have undertaken in respect of Pearson's strategy throughout the year. Our Audit Committee, led by Tim Score, plays a key role in monitoring and evaluating our compliance and risk management processes, providing independent oversight of our external audit and internal control programmes, accounting policies and business transformation projects, and in assisting the Board in reporting in a fair, balanced and understandable manner to our shareholders. You can read more about the Audit Committee's activities and priorities during 2020 on p90

The UK Corporate Governance Code

The principles set out in the UK Corporate Governance Code (the Code) emphasise the value of good corporate governance to the long-term sustainable success of listed companies. These principles, and their supporting provisions, cover five broad themes. The Pearson Board is responsible for ensuring that the Group has in place appropriate frameworks to comply with the Code's requirements.

The five themes are covered in particular on the following pages of the Governance report, with additional information contained in the Strategic report.

This Governance report and the Strategic report set out how Pearson has applied the principles of the Code throughout the year.

Read more	Page
› Board leadership and company purpose	69–70
› Division of responsibilities	77
› Composition, succession and evaluation	73, 76, 82–87
› Audit, risk and internal control	90–99
› Remuneration	100–121

The Board believes that during 2020 the company was in full compliance with all applicable principles and provisions of the Code, save that:

- Pearson is not fully compliant with Provision 36 of the Code on the basis that the shares awarded under the Chief Executive's co-investment award are subject to a post-vesting holding period until 31 December 2023, rather than a total vesting and holding period of five years or more required by the Code
- as described in last year's report, prior to John Fallon's retirement from the Board, the Company had set out a path to align his pension contributions to those available to the workforce

Further detail on both matters is provided in the Directors' Remuneration Report.

UK Corporate Governance Code
The Code can be found on the Financial Reporting Council's website
www.frc.org.uk

Governance on our website
View our compliance schedule on the company website
plc.pearson.com/en-GB/company/business-operations

Remuneration

Following work by the Remuneration Committee to review and update Pearson's remuneration philosophy in light of the company's evolving strategy, 2020 saw the adoption of a new remuneration policy at the AGM, and the Board is grateful for shareholders' support. The Board is also grateful for the support of shareholders for the vote tabled at the company's general meeting in September 2020, although it recognises and respects the concern of some shareholders. The Committee, led by its Chair Elizabeth Corley, has continued to engage with investors on these matters. You can read more about the Committee's activities and Pearson's approach to remuneration in the remuneration section of this report on p100

Conclusion

I hope this report clearly sets out how your company is run, and how we align governance and our Board agenda with the strategic direction of Pearson. We always welcome questions or comments from shareholders, either via our website (plc.pearson.com/en-GB/investors/investor-shareholder-contacts) or at our AGM. While we are unlikely to be able to welcome shareholders in person to our AGM this year, due to ongoing pandemic restrictions, we very much hope that you will participate in our planned shareholder event in advance of the AGM, details of which will be included in our AGM notice.

Sidney Taurel
Chair

Board of Directors

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

All Board members have strong leadership experience at global businesses and institutions. Our Board members' biographies illustrate the contribution each Director makes to the Board by way of their individual experience.

Key to Committees

- A Audit
- N Nomination & Governance
- RR Reputation & Responsibility
- R Remuneration
- ● Committee Chair

Current notable commitments reflect other listed company directorships and full-time or executive roles.

Executive Directors

RR

Andy Bird, CBE Chief Executive

aged 57, first appointed to the Board 1 May 2020, appointed as Chief Executive Officer 19 October 2020

Andy has a long and distinguished career spanning 35 years in the media industry, and is an accomplished, strategic leader of global consumer content businesses. Most recently he spent 14 years working for The Walt Disney Company, joining the business as President of Walt Disney International in 2004, before being appointed Chairman in 2008. He held this role for a decade, during which time he transformed the organisation into a digital-first, direct to consumer business, focused on serving the diverse needs of customers around the world. In addition, Andy worked to establish the iconic brand in China, through the creation of Disney English, teaching the English language to Chinese families through immersive learning experiences.

Prior to Disney, Andy worked in a number of senior positions at AOL Time Warner, and spent the earlier part of his career at Piccadilly Radio, Virgin Broadcasting Company, BSB Music Channel, Big & Good Productions and Unique Broadcasting.

Sally Johnson

Chief Financial Officer

aged 47, appointed 24 April 2020

Sally joined Pearson in 2000, and has held various finance and operations roles across The Penguin Group, the education business and at a corporate level. She brings to the Board extensive commercial and strategic finance experience as well as transformation, treasury, tax, risk management, business and financial operations, investor relations and M&A expertise. She has held various senior level roles across the business, most recently as Deputy CFO of Pearson. Sally is a member of the Institute of Chartered Accountants in England and Wales and trained at PricewaterhouseCoopers. She was also a Trustee for the Pearson Pension Plan from 2012 to 2018.

Chair

N R

Sidney Taurel Chair

aged 72, appointed 1 January 2016

Sidney has over 45 years of experience in business and finance. He is currently a Director of IBM Corporation, a role from which he will be retiring in April 2021. Sidney is an advisory board member at pharmaceutical firm Almirall. He was Chief Executive Officer of global pharmaceutical firm Eli Lilly and Company from 1998 until 2008, Chairman from 1999 until 2008, and has been Chairman Emeritus since 2009. His 37-year career at Eli Lilly included time spent in Brazil, France, Eastern Europe, the US and the UK. He has previously held directorships at McGraw Hill Financial, Inc. and ITT Industries. In 2002, Sidney received three US presidential appointments to: the Homeland Security Advisory Council, the President's Export Council and the Advisory Committee for Trade Policy and Negotiations. Sidney is also an officer of the French Legion of Honour.

Current notable commitments: HIG Acquisition Corporation (Non-Executive Director) and IBM Corporation (Non-Executive Director)

Non-Executive Directors

A N R

Dame Elizabeth Corley, DBE

Non-Executive Director

aged 64, appointed 1 May 2014

Elizabeth has extensive experience in the financial services industry, having been CEO of Allianz Global Investors, initially for Europe then globally, from 2005 to 2016. She continued to act as an adviser to the company until the end of 2019. Previously she was at Merrill Lynch Investment Managers and Coopers & Lybrand. Elizabeth is a Non-Executive Director of BAE Systems plc and Morgan Stanley Inc. Elizabeth is active in representing the investment industry and developing standards within it.

She is chair of the Impact Investing Institute; a director of the Green Finance Institute and serves on the investment committee of the Leverhulme Trust. She was appointed Dame Commander of the Order of the British Empire in the Queen's Birthday Honours in 2019 for her services to the economy and financial services.

Current notable commitments: BAE Systems plc (Non-Executive Director), Morgan Stanley Inc. (Non-Executive Director)

N R

Sherry Coutu, CBE Non-Executive Director

aged 57, appointed 1 May 2019

Sherry has extensive experience in the technology industry. She has also served on the boards of a range of companies and charities, with a focus on working with entrepreneurs and specialising in consumer digital, information services, and education. Sherry is the Chair of Founders4Schools and founder of the Scale-Up Institute. Previously, she was CEO of Interactive Investor International plc, and has served on the boards of Cambridge Assessment, Bloomberg New Energy Finance and the London Stock Exchange plc as well as being SID and Remuneration Committee Chair of RM plc. Sherry has started and/or invested in over 60 technology businesses and served on the boards of Zoopla plc, Raspberry Pi, NESTA, and the Advisory boards of the National Gallery, Royal Society and LinkedIn. She was appointed Commander of the British Empire in the 2013 New Year Honours for her services to entrepreneurship.

Current notable commitments: Reinvent Technology Partners

Board of Directors

Non-Executive Directors

A N RR

Vivienne Cox, CBE
Senior Independent Director
aged 61, appointed 1 January 2012

Vivienne has wide experience in energy, natural resources and business innovation. She worked for BP plc for 28 years in global roles including Executive Vice President and Chief Executive of BP's gas, power and renewables business and its alternative energy unit. She is Chair of the supervisory board of Vallourec S.A., a leader in the seamless steel pipe markets, and a Non-Executive Director at pharmaceutical company GlaxoSmithKline plc, where she also acts as Workforce Engagement Director. She also has a deep understanding of regulatory and government relationships. She serves as Chair of the Rosalind Franklin Institute and Vice Chair of the Saïd Business School (part of Oxford University). She was appointed Commander of the British Empire in the 2016 New Year Honours for her services to the economy and sustainability.

Current notable commitments: GlaxoSmithKline plc (Non-Executive Director), Vallourec S.A. (Chair of the supervisory board)

A RR

Linda Lorimer Non-Executive Director
aged 68, appointed 1 July 2013

Linda has spent almost 40 years serving higher education. She retired from Yale in 2016 after 34 years at the university where she served in an array of senior positions including Vice President for Global & Strategic Initiatives. She oversaw the development of Yale's online education division and the expansion of Yale's international programmes and centres. During her tenure, she was responsible for many administrative services, ranging from Yale's public communications and alumni relations to sustainability, human resources and the university press. She also served on the boards of several public companies, including as Presiding Director of the McGraw-Hill companies. Linda is a member of the board of Yale New Haven Hospital, where she chairs the nominating and governance committee and is a trustee of Hollins University. She also remains on several consequential advisory committees at Yale University.

A RR

Michael Lynton Non-Executive Director
aged 61, appointed 1 February 2018

Michael has more than 30 years of senior-level management experience, including extensive experience in consumer marketing, traditional and digital media, and the adoption of new technologies. He also has broad public company governance experience. Michael served as CEO of Sony Entertainment from 2012 until 2017, overseeing Sony's global entertainment businesses. He was also Chairman and CEO of Sony Pictures Entertainment from 2004. Prior to that, he held senior roles within Time Warner and AOL, and earlier served as Chairman and CEO of Penguin Group where he extended the Penguin brand to music and the internet. Michael is Chairman of Snap, Inc., Schrödinger, Inc. and Warner Music Group, and currently serves on the boards of IEX, Ares Management Corporation LLC and The Boston Beer Company, Inc.

Current notable commitments: Ares Management Corporation LLC (Non-Executive Director), Snap, Inc. (Chairman), Schrödinger, Inc. (Chairman), Warner Music Group (Chairman), The Boston Beer Company, Inc. (Non-Executive Director)

A RR

Graeme Pitkethly Non-Executive Director
aged 54, appointed 1 May 2019

Graeme joined Unilever in 2002 and, prior to being appointed CFO and Board member, was responsible for Unilever's UK and Ireland business. Previously, he had held a number of senior financial and commercial roles within Unilever, including Senior Vice President of Finance for Global Markets, Group Treasurer, Global Head of M&A and Chief Financial Officer of Unilever Indonesia. Graeme spent the earlier part of his career in senior corporate finance roles in the telecommunications industry with FLAG Telecom, and started his career at PricewaterhouseCoopers. Graeme is currently Vice Chair of the Task Force on Climate Related Financial Disclosures, Vice Chair of the 100 Group Main Committee and is a Chartered Accountant.

Current notable commitments: Unilever plc (Chief Financial Officer)

A N R

Tim Score Non-Executive Director
aged 60, appointed 1 January 2015

Tim has extensive experience of the technology sector in both developed and emerging markets, having served as Chief Financial Officer of ARM Holdings plc, the world's leading semiconductor IP company, for 13 years. He is an experienced non-executive director and serves as Chairman of The British Land Company plc, a role to which he was appointed in July 2019, a non-executive director of HM Treasury, and a Trustee of the National Theatre. Tim has garnered extensive financial and listed company experience during previous and current positions. He served on the board of National Express Group plc from 2005 to 2014, including time as interim Chairman and six years as the Senior Independent Director. Earlier in his career Tim held senior finance roles with Rebus Group, William Baird, LucasVarity plc and BTR plc.

Current notable commitments: The British Land Company plc (Chairman)

A RR

Lincoln Wallen Non-Executive Director
aged 60, appointed 1 January 2016

Lincoln has extensive experience in the technology and media industries, and is currently CTO of Improbable, a technology start-up supplying next-generation cloud hosting and networking services to the video game industry. Lincoln was CEO of DWA Nova, a software-as-a-service company spun out of DreamWorks Animation Studios in Los Angeles, a position he held until 2017. He worked at DreamWorks Animation for nine years in a variety of leadership roles including Chief Technology Officer and Head of Animation Technology. He was formerly CTO at Electronic Arts Mobile, leading their entry into the mobile gaming business internationally. Lincoln is a Non-Executive Director of the Smith Institute for Industrial Mathematics and Systems Engineering. His early career involved 20 years of professional IT and mathematics research, including as a reader in Computer Science at Oxford.

Current notable commitments: Improbable (Chief Technology Officer)

Governance at Pearson

Board of Directors

Board Committees

The Board has established four formal Committees. The Committees focus on their own areas of expertise, enabling the Board meetings to focus on strategy, performance, leadership and people, governance and risk, and stakeholder engagement, thereby making the best use of the Board's time together as a whole. The Committee Chairs report to the full Board at each Board meeting following their sessions, ensuring a good communication flow while retaining the ability to escalate items to the full Board's agenda if appropriate.

Audit Committee	Appraises our financial management and reporting and assesses the integrity of our accounting procedures and financial controls. The Committee also oversees risk, compliance and internal audit.
Nomination & Governance Committee	Reviews corporate governance matters, including Code compliance and Board evaluation, considers the appointment of new Directors, Board experience and diversity, and reviews Board induction and succession plans as well as wider workforce engagement.
Remuneration Committee	Determines the remuneration and benefits of the Executive Directors and oversees remuneration arrangements for the Pearson Executive Management team, as well as remuneration policies for the wider workforce.
Reputation & Responsibility Committee	Considers the company's impact on society and the communities in which Pearson operates, including to ensure that strategies are in place to manage and improve Pearson's reputation.

Pearson Executive Management (PEM)

The PEM team consists of Andy Bird (Chief Executive) and his direct reports. They are the executive leadership group for Pearson, responsible for delivering Pearson's strategy under clearly defined accountabilities and in line with agreed governance and processes.

- Chief Executive
- Chief Financial Officer
- Chief Human Resources Officer
- Chief Legal Officer
- Chief Marketing Officer and Co-President, Direct to Consumer
- Chief Product Officer and Co-President, Direct to Consumer
- Chief Strategy Officer and Interim President – Workforce Skills
- Head of Telecom and Technology Partnerships
- President – Assessment & Qualifications
- President – English Language Learning
- President – Higher Education
- President – UK & Global Online Learning (stepping away in 2021)
- President – Virtual Learning

see p72

FLOW OF INFORMATION

Standing Committee

A Standing Committee of the Board is established to approve certain operational and ordinary course of business items such as banking matters, guarantees, intra-Group transactions and to make routine approvals relating to employee share plans.

The Committee has written terms of reference, reviewed and approved each year, which clearly set out its authority and duties. These can be found on the company website at plc.pearson.com/en-GB/company/business-operations.

Pearson Executive Management

The Pearson Executive Management team outlined below is presented under the new organisational structure that comes into effect as of 2021.

Tom ap Simon President – Virtual Learning
aged 42

Tom has 19 years of international business and finance experience. At Pearson, he has led the Virtual Schools business, worked in finance for the emerging markets businesses and led M&A activity in the US. Previously, he worked in investment banking at RW Baird. Tom holds an MA in Economics and Politics from the University of Edinburgh.

Tim Bozik President – Higher Education
aged 59

Tim has more than 30 years of extensive leadership experience in higher education products and the business of delivering them at Pearson. Tim earned a Bachelor's Degree from the University of Notre Dame and currently serves on the Board of Directors for the Association of American Publishers.

Rod Bristow
aged 63

After 35 years' service, Rod Bristow is stepping away from his role as President of Pearson UK and President of Global Online Learning in 2021. Rod has worked in education for more than 30 years in the UK and internationally. Rod is a trustee for the Education and Employers Taskforce, a fellow of the Royal Society for Arts, governor for Harlow College and the BMAT multi-academy trust. Rod is a graduate of University College London.

Lynne Frank Chief Marketing Officer and Co-President, Direct to Consumer
aged 54

Lynne has over 25 years of experience in the media industry. Previously, she has worked in companies such as WarnerMedia, ESPN/Disney and Turner Broadcasting. Lynne holds a degree in economics and business, and a certificate in corporate board governance from the University of California, Los Angeles (UCLA).

Gio Giovannelli President – English Language Learning
aged 48

Gio has over 25 years of international business experience, including four CEO roles in Brazil, one of which was Grupo Multi. Previous board roles include BOVESPA-listed Natura and CVC Viagens. Gio graduated from Bocconi University, holds an Economics Ph.D. and is OPM graduate of Harvard Business School.

Albert Hitchcock Head of Telecom and Technology Partnerships
aged 56

Albert has over 30 years of experience in the technology industry. Previously, Albert was Pearson's Chief Technology and Operations Officer (2014–2021), Group CIO at Vodafone, as well as Global CIO at Nortel Networks. Albert is a Chartered Engineer and a Fellow of the Institute of Engineering & Technology.

Mike Howells Chief Strategy Officer and Interim President – Workforce Skills
aged 44

Mike has more than 20 years of international business experience. Previously, he has worked in the British diplomatic network and the UK Foreign, Commonwealth and Development Office. Mike holds a masters degree in International Law from the University of Nottingham and an Anthropology degree from University College London.

Ishantha Lokuge Chief Product Officer and Co-President, Direct to Consumer
aged 53

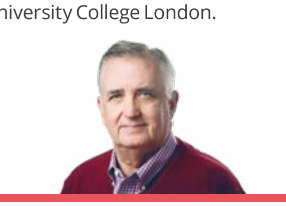
Ishantha has more than 20 years of Silicon Valley experience. Previously, he was at Shutterfly, eBay and Healtheon/WebMD. He holds degrees in computer science from Brandeis and Tufts, as well as a graduate degree in Media Arts and Sciences from the Massachusetts Institute of Technology (MIT) Media Lab.

Cinthia Nespoli Chief Legal Officer
aged 40

Cinthia has 17 years of international legal experience. Previously, she has worked in the manufacturing sector at multinational companies. Cinthia was admitted to the Brazilian bar in 2004 and earned her law degree from Pontifícia Universidade Católica de Campinas and a post-graduate degree in tax law from Pontifícia Universidade Católica de São Paulo.

Anna Vikström Persson Chief Human Resources Officer
aged 51

Anna Vikström Persson has over 20 years of international HR experience. Previously, Anna held executive positions at Sandvik, SSAB and Ericsson. Anna has a certificate in German and a masters in law, as well as professional HR qualifications from both London Business School and Michigan Business School.



Bob Whelan President – Assessment & Qualifications
aged 72

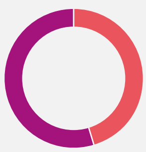
Bob has over 40 years of significant expertise in testing and assessment. Previously, Bob worked at Personnel Decisions International, as well as National Computer Systems (NCS) which Pearson acquired in 2000. Bob earned his BA from the University of Alabama in finance and economics.

Corporate governance review

BOARD AND EXECUTIVE COMPOSITION

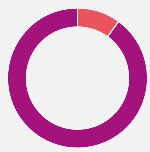
Board of Directors

Gender balance



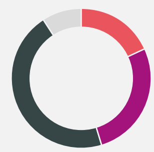
Female	5
Male	6

Ethnicity



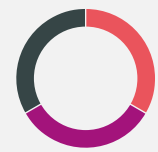
Mixed	1
White	9

Nationality



American	2
American/British (dual)	3
British	5
Canadian	1

Tenure[1]

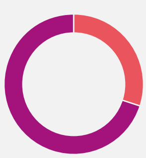


Under 3 years	3
3-6 years	3
Over 6 years	3

1 Chart shows tenure of Chair and Non-Executive Directors.

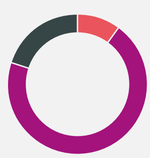
Pearson Executive Management (PEM)

Gender balance



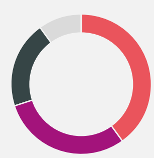
Female	3
Male	7

Ethnicity



Asian	1
White	7
Other	2

Nationality



American	4
British	3
Italian/Brazilian (dual)	2
Swedish	1

This data represents those in office at 31 December 2020.

BOARD SKILLS, EXPERIENCE AND BACKGROUND

Current skills

- Accounting and finance
- Disruption, including
  - talent leadership through change
  - marketing and data insights
  - new business models and innovation
- Direct to consumer business models
- Educational experience
- Focus on people and talent
- Global markets
- Prior leadership experience, particularly of multinational businesses
- Remuneration
- Scale and complexity experience
- Sustainability and ESG
- Transformation
- UK plc experience

Succession planning focus[1]

- Digital and technology
- Diversity
- Educational experience
- Prior leadership experience, particularly of multinational businesses
- Scale and complexity experience
- UK plc experience

For further details on succession planning, see p76

1 These areas of focus reflect priorities for deepening existing skills and experience, or to address upcoming retirements.

Corporate governance review

Board of Directors

Composition of the Board – As at the date of this report, the Board consists of the Chair, Sidney Taurel, two Executive Directors: the Chief Executive, Andy Bird, and Chief Financial Officer, Sally Johnson, and eight independent Non-Executive Directors.

Independence of Directors – All of the Non-Executive Directors who served during 2020 were considered by the Board to be independent for the purposes of the UK Corporate Governance Code (the Code). The Board reviews the independence of each of the Non-Executive Directors annually. This includes reviewing their external appointments and any potential conflicts of interest as well as assessing their individual circumstances in order to ensure that there are no relationships or matters likely to affect their judgement. In addition to this review, each of the Non-Executive Directors is asked annually to complete an independence questionnaire to satisfy requirements arising from Pearson's US listing and the Code. In January 2021, Ms Cox reached nine years' service on the Pearson Board. Upon attainment of nine years' service by any Non-Executive Director, the Board undertakes an assessment in accordance with Provision 10 of the Code to satisfy itself as to the continuing independence of that Director. In addition, we require each Non-Executive Director to provide confirmation of their independence on an annual basis (as defined by the Sarbanes-Oxley Act, the New York Stock Exchange (NYSE) listing rules and the Code). Accordingly, the Board is satisfied that Ms Cox remains independent, and that she continues to provide constructive challenge and hold management to account. Ms Cox will not be seeking re-election at the 2021 AGM.

Directors' commitments and conflicts of interest – Under the Companies Act 2006 (the Act), the Directors have a statutory duty to avoid conflicts of interest with the company. The company's Articles of Association allow the Directors to authorise conflicts of interest. The company has an established procedure to identify actual and potential conflicts of interest, including all directorships or other appointments to, or relationships with, companies that are not part of the Pearson Group and which could give rise to actual or potential conflicts of interest.

Additionally, in response to Provision 15 of the Code, Pearson has developed internal guidance to be taken into account when considering changes to a Director's commitments, or when appointing a new Director, as well as formalising the Board approval process for such matters.

Once notified to the company, any potential conflicts and commitments are considered for authorisation by the Board at its next scheduled meeting or, where necessary in the interests of timeliness, by a Committee comprising the Chair, Senior Independent Director and Company Secretary. In particular, the Board or Committee considers the type of role, expected time commitment and any impact which this may have on the Director's duties to Pearson, as well as any relationships between Pearson and the external organisation. The interested Director is not permitted to vote, or be counted in the quorum, for any resolution relating to his/her commitments, conflict or potential conflict. The Board reviews any authorisations granted on an annual basis.

As noted in our 2019 annual report and following the significant vote against the re-election resolution at our 2020 AGM, Mr Lynton and the Chair agreed to review Mr Lynton's situation over the course of 2020 in relation to his other, external, commitments. Mr Lynton has since been additionally appointed to the board of The Boston Beer Company, Inc. Mindful of Pearson's own internal guidance and shareholder sentiment regarding Directors' commitments, it was agreed that Mr Lynton would not seek re-election at the 2021 AGM, as confirmed to the market on 4 February 2021. On this basis, the Board accepted Mr Lynton's additional appointment to the Boston Beer Company board, given that there is only a short period until he steps down at the 2021 AGM. To date there has been no impact on Mr Lynton's ability to commit to the Pearson Board, and he has demonstrated a full attendance record at Pearson since his appointment in 2018. There were no other new commitments of Directors during 2020 which the Board considered to be significant in nature.

The role and business of the Board

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

The key responsibilities of the Board include:

› overall leadership of the company and setting the company's values and standards, including monitoring culture and DE&I initiatives

› determining the company's strategy, including in relation to ESG matters, in consultation with management, reviewing performance against it and overseeing management's execution of it

› major changes to the company's corporate, capital, management and control structures

› approval of all transactions or financial commitments in excess of the authority limits delegated to the Chief Executive and other Executive management

› assessment of management performance, Board and Executive succession planning and talent pipeline

A schedule of formal matters reserved for the Board's decision and approval is reviewed annually and is available on our website at plc.pearson.com/en-GB/company/business-operations.

Strategic planning and decision-making

The Board spends considerable time in assessing whether any proposed action aligns with the strategy and future direction of the business. In addition, regular strategy sessions enhance the Board's decision-making in shaping the company's strategic and financial plans, Sustainability is inherent in the Board's strategic planning and decision-making.

The Board and Committees receive timely, regular and necessary financial, management and other information to fulfil their duties. Comprehensive meeting papers are circulated to the Board and Committee members at least one week in advance of each meeting and the Board receives a regular performance dashboard and key milestones report and regular updates from the Chief Executive and Chief Financial Officer. In addition to meeting papers, a library of current and historical corporate information is made available to Directors electronically to support the Board's decision-making process. The Directors can obtain independent professional advice, at the company's expense, in the performance of their duties. All Directors have access to the advice and services of the Company Secretary, whose appointment and removal is a matter reserved for the full Board.

The Directors recognise their duties towards the shareholders and other stakeholders of the company as set out in Section 172 of the Act, and a continued understanding of the key issues affecting stakeholders is an integral part of the Board's decision-making process. You can read more on p80 about the Board's engagement with stakeholders and an illustrative example of how it takes stakeholder views, and in particular employee feedback, into account in its decision-making.

Board meetings

The Board held seven scheduled meetings in 2020, with discussions and debates focused on the key strategic issues facing the company. Major items covered by the Board in 2020 are shown in the table below. In addition to its scheduled meetings, the Board convenes as necessary to consider matters of a time-sensitive nature. In 2020 the Board convened on three occasions to consider matters relating to COVID-19 and Chief Executive succession. Despite the additional oversight requirement that the company's response to COVID-19 has placed on the Board, the Board is satisfied that each Director contributed to Board discussions and demonstrated sufficient commitment to be able to meet their responsibilities. As shown in the table to the right, each of the Non-Executive Directors attended all meetings during 2020. In addition, the Nomination & Governance Committee confirmed in its annual confirmation that each Director demonstrates the requisite level of commitment and contribution in accordance with Principle H and Provision 18 of the Code. Furthermore, the Board has adapted well in this new, virtual, way of working which has allowed for greater participation from employees. The Board is capable of keeping in touch with the company and employees globally, and will continue to do so for the duration of the global pandemic and into the future.

Board attendance

Directors are expected to attend all Board and Committee meetings, but in certain exceptional circumstances, such as due to pre-existing business or personal commitments, it is recognised that Directors may be unable to attend. In these circumstances, the Directors receive relevant papers and, where possible, will communicate any comments and observations in advance of the meeting for raising as appropriate during the meeting. They are updated on any developments after the meeting by the Chair of the Board or Committee, as appropriate.

Individuals' attendance at Board and Committee meetings is considered, as necessary, as part of the formal review of their performance. There was a high level of attendance by the Directors at Board and Committee meetings in 2020 as shown in the table below and in the Committee reports that follow:

	Board meetings attended
Chair	
Sidney Taurel	**10/10**
Executive Directors	
Andy Bird[1]	**5/6**
John Fallon[2]	**7/9**
Sally Johnson[3]	**4/6**
Coram Williams[4]	**4/4**
Non-Executive Directors	
Elizabeth Corley	**10/10**
Sherry Coutu	**10/10**
Vivienne Cox	**10/10**
Josh Lewis[5]	**4/4**
Linda Lorimer	**10/10**
Michael Lynton	**10/10**
Graeme Pitkethly	**10/10**
Tim Score	**10/10**
Lincoln Wallen	**10/10**

1 Mr Bird joined the Board on 1 May 2020. Mr Bird did not attend any meetings on the topic of Chief Executive succession when he was a candidate.
2 Mr Fallon retired from the Board on 18 October 2020. Mr Fallon did not attend certain meetings on the topic of Chief Executive succession.
3 Ms Johnson joined the Board on 24 April 2020. Ms Johnson did not attend any meetings on the topic of Chief Executive succession.
4 Mr Williams resigned from the Board on 24 April 2020.
5 Mr Lewis retired from the Board on 24 April 2020.

Board meeting focus during 2020

Strategy

- US Higher Education Courseware
- Global Online Learning
- Direct to consumer
- Impact of COVID-19
- Oversight of 2020 operating plan and goals, and preparation for 2021
- Portfolio review
- Capital allocation

Performance

- 2019 preliminary results and annual report and accounts
- 2020 interim results and trading updates
- Regular dashboard and milestone reports
- Operating and strategic plan discussions
- Final and interim dividend proposals
- Continuing review of forecasts
- Impact of COVID-19, including liquidity assessment

Leadership & people

- Chief Executive succession planning
- DE&I updates
- Talent review and pipeline development
- Senior Leadership succession planning
- Impact of COVID-19 on organisational health, including company culture and values
- Employee Engagement Network feedback
- Employee Survey assessments
- Workforce Learning & Development

Read more on employee engagement on p81

Governance & risk

- Legal and regulatory compliance including UK Corporate Governance Code, Companies Act and listed company obligations
- Brexit updates
- Board and Committees evaluation
- Approval of division of responsibilities between Chair and Chief Executive
- Annual review of conflicts of interest
- Approval of Committees' terms of reference
- Data privacy matters
- Social bond

Shareholder engagement

- Ongoing shareholder consultations
- Investor relations strategy and share price performance
- Major shareholders and share register analysis
- Shareholder issues and voting
- Feedback from Chair and Executive Director meetings with shareholders

Corporate governance review

Directors' training and induction

All Directors receive training in the form of presentations about the company's operations and, where possible, through Board meetings held at operational locations and by visiting local facilities and management. Whilst during 2020, and in the immediate future, physical visits remain challenging, the Directors are supported virtually and are offered the same level of interaction where possible, albeit through digital means. When permitted, Directors will be encouraged to visit facilities and management, even if they are travelling to a country or region on non-Pearson business. The Company Secretary and General Counsel, in conjunction with Pearson's advisers, monitor legal and governance developments and update the Board on such matters as agreed with the Chair. Our Directors can also make use of external courses.

The Directors receive a significant bespoke induction programme and a range of information about Pearson when they join the Board. This includes background information on Pearson and details of Board procedures, Directors' responsibilities and various governance-related issues, including procedures for dealing in Pearson shares and their legal obligations as Directors. The induction also typically includes a series of meetings with members of the Board, external legal advisers and brokers, the Pearson Executive Management team and other senior management, presentations regarding the business from senior executives, and a briefing on Pearson's investor relations programme. The induction framework is reviewed by the Nomination & Governance Committee in advance of any Director onboarding.

A tailored and bespoke induction programme which aligned with the Board's focus areas was designed for Andy Bird, who was initially appointed as a Non-Executive Director in May 2020. The induction included business area familiarisation, participation in sessions that related to areas of interest, and topics that were pertinent to the Committees he joined. The Company Secretary sought Mr Bird's feedback following completion of his induction programme, and Mr Bird was positive about the benefits of the programme.

Succession planning and talent

The Board considers oversight of succession planning as one of its prime responsibilities, assisted by the Nomination & Governance Committee. The company has formal contingency plans in place for the temporary absence of the Chief Executive for health or other reasons. The matter of Chief Executive succession is a regular item for discussion and reviewed by the Chair and the Board on an annual basis.

Succession planning for the Board as a whole and for the role of Chair is also considered annually by the full Board and on an ongoing basis by the Nomination & Governance Committee, with the Chair and Senior Independent Director also discussing Committee Chair succession planning on a regular basis. See our Nomination & Governance Committee Report (p84) for further details on succession planning. Also, see our Board 'Skills and Experience' matrix on p73 which outlines competencies the Directors currently possess, as well as particular areas of focus that are helping to inform succession planning, and take into account upcoming retirements.

There is also regular discussion and oversight by the Board of succession planning for key positions at Executive management level. The Executive team has a key role to play in both our strategic planning process and in succession planning and fostering the culture of DE&I required to continue to deliver on our strategy.

As well as Board and Executive management succession, the Board also oversees our leadership pipeline. In December, the Board held a discussion on talent and culture, including a succession planning session focused on the executive pipeline from which the future leaders of Pearson were likely to emerge, both at Pearson Executive Management level and for other key roles. A diverse pipeline of 'ready now' and 'ready later' emerging talent has been identified, and plans put in place to accelerate their development and path to succession where possible, including through measures such as participating in Board and Committee meetings, mentoring by Non-Executive Directors, and by encouraging and enabling individuals to take on external non-executive roles in order to increase their exposure to new areas of business. The company also has targeted development programmes for high-potential talent and mentorship programmes for senior women leaders, as well as a Manager Fundamentals programme for middle management.

Succession planning for Executive Directors

The Chair, Sidney Taurel, keeps the matter of Chief Executive succession under regular consideration and, following the announcement in late 2019 of John Fallon's intention to retire, accelerated the search process. The Board had a clear sense of the attributes it was looking for in the new Chief Executive – which included, but were not limited to, having demonstrable experience in corporate transformation, digital experience, a global view, and an ability to nurture a strong and healthy organisational culture. The Board recognised the challenge in securing all of these attributes in one individual but is pleased with the appointment of Andy Bird. The Board believes that Mr Bird satisfies and exceeds the initial search criteria.

In early 2020, the Chief Financial Officer, Coram Williams, announced his intention to step down from the Board. Accordingly, the Board activated its executive succession plans which had identified Sally Johnson, who was the Deputy CFO, as a 'ready now' candidate to succeed Mr Williams as Chief Financial Officer. Mr Taurel and Ms Cox, Senior Independent Director and Chair of the Nomination & Governance Committee, led discussions on behalf of the Board which resulted in the recommendation of Ms Johnson as CFO-elect, a matter which the Board approved in principle in January 2020. Pearson announced that Ms Johnson would join the Board and assume the position of Chief Financial Officer at the conclusion of the 2020 AGM, with Mr Williams stepping down from the Board at that time.

The Board continues to monitor 'ready now' and 'ready later' candidates, ensuring that Pearson has a diverse pipeline and succession plan.

DIVISION OF RESPONSIBILITIES

There is a defined split of responsibilities between the Chair and the executive leadership of Pearson. The roles and responsibilities of the Chair, Chief Executive and the Senior Independent Director are clearly defined, set out in writing and reviewed and agreed by the Board on an annual basis. These can be found on the company website at plc.pearson.com/en-GB/company/business-operations.

The Chair is primarily responsible for the leadership of the Board and ensuring its effectiveness. He ensures that the Board upholds and promotes the highest standards of corporate governance, setting the Board's agenda and encouraging open, constructive debate of all agenda items for effective decision-making. He regularly meets the Chief Executive to stay informed and provide advice. He also ensures that shareholders' views are communicated to the Board.

Chair's significant commitments There were no changes to the Chair's significant commitments during 2020. Mr Taurel will be stepping down as a Non-Executive Director of IBM Corporation with effect from the date of their 2021 annual meeting of shareholders.

Independence of Chair In accordance with the Code, Sidney Taurel was considered to be independent upon his appointment as Chair on 1 January 2016.

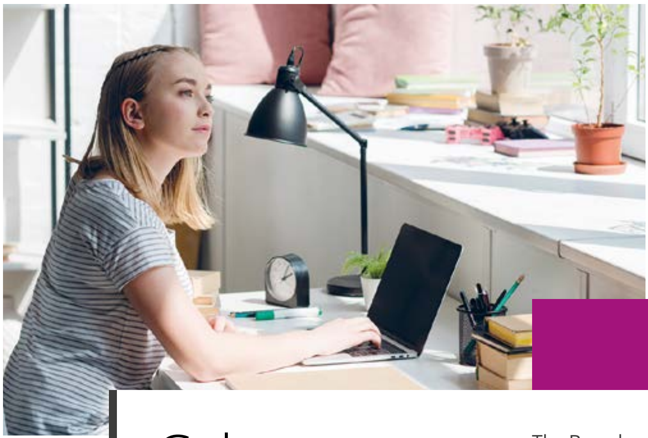
The Chief Executive is responsible for the operational management of the business and for the development and implementation of the company's strategy as agreed by the Board and management. He is responsible for developing operational proposals and policies for approval by the Board, he promotes Pearson's culture and standards, and is one of the key representatives of the company to its external stakeholders.

The Senior Independent Director's role includes meeting regularly with the Chair and Chief Executive to discuss specific issues, as well as being available to shareholders generally should they have concerns that have not been addressed through the normal channels. She also leads the evaluation of the Chair on behalf of the other Directors.

Chair – Sidney Taurel

Chief Executive – Andy Bird

Senior Independent Director – Vivienne Cox



Culture, purpose and values

Pearson's core values – to be brave, imaginative, decent and accountable – go to the heart of our purpose: to help everyone achieve their potential through learning, and the Board and employees are committed to demonstrating these characteristics throughout their work and discussions.

The Board endorses Pearson's culture of innovation, fostering talent and inclusivity at all levels, and demonstrated this during the year by engaging with employees from across Pearson through a variety of events.

The Board monitors the culture and organisational health of the company with the assistance of its Committees, including through regular updates from the Chief Human Resources Officer on talent, DE&I and Pearson's values as well as considering Group-wide programmes such as the Code of Conduct, compliance, Health & Safety, and learning initiatives.

During 2020, and with the help of the Chief Human Resources Officer, we introduced a dashboard drawing together key cultural indicators from across the Group. The dashboard provides the Nomination & Governance Committee with a quantitative framework which the Board utilises alongside other inputs of a more qualitative nature, enabling the Directors to evaluate Pearson's organisational health to monitor and assess company culture.

During 2021, the Board will continue to pay attention to Pearson's culture as the company's vision, mission and values evolve in support of our strategy.

Learn more:

For examples of Board decision-making, see our COVID-19 case study on p79 and our employee engagement case study on p81.

Corporate governance review

GOVERNANCE RESPONSE TO COVID-19

This timeline illustrates a number of key events and initiatives which took place throughout the year at Pearson and provides a high-level indication of the impacts of COVID-19 upon the work of the Board, its committees and broader corporate governance framework in the business.

Preparation

March

Market Disclosure Committee (MDC)

Introduction of more regular MDC meetings to consider COVID-19 impact on trading, culminating in an additional trading update on 23 March 2020 including the decision to pause the share buyback programme

March

Board and all committees

As lockdown and travel restrictions were introduced, the Board and committees moved to fully online meetings

April

Board

An extra Board meeting was called at short notice to consider the financial and workforce implications of COVID-19.

See opposite

April

Audit Committee

The Audit Committee's regular business resilience deep dive considered the early stage response to COVID-19 in impacted regions from an operations, continuity and technology perspective

Response and adjustment

April

Board and Company

AGM arrangements changed as UK entered lockdown. The 2020 AGM was held on 24 April 2020 in a COVID-secure manner and shareholders were encouraged to submit proxy votes in advance and raise questions by email or post

April

Board and all committees

The Board considered input from the Executive team on how Pearson was responding to changing customer needs. All committees considered COVID-19 impacts on their areas of focus. All Directors joined all meetings for awareness of impacts and response

June

Board

The Board's strategy sessions included consideration of impacts of COVID-19 on Pearson's focus areas of investment which informed their discussions as to investment priorities

Recovery and forward looking

Mid-year onwards

Board and Company

Increased Board focus on people to address Pulse survey feedback and increased risk of burnout, introduction of personal development opportunities and wellbeing initiatives e.g. Learning at Work Week and Pearson WELL

July

Remuneration Committee

Decision taken to reset the incentive plan opportunity for employees below Board level to incentivise employees for the second half of 2020 on a proportionate basis

July

Audit Committee

Half-year accounting considerations relating to COVID-19 including going concern assessment, cash flow assumptions, working capital, real estate matters, and risk factors

July, October and December

Reputation & Responsibility Committee

Updates at each meeting on stakeholder groups affected by COVID-19, including customers and employees, with a focus on impacts, stakeholder engagement and the company's response

October and December

Board

Strategy, three-year plan and 2021 operating plan discussed with consideration of COVID-19-related adjustments to plans

December

Remuneration Committee

Consideration of remuneration trends in response to the pandemic

Board response to COVID-19

This case study provides an illustrative example of how the Board has regard to relevant stakeholders and their interests in its decision-making processes, as required by S172 of the Companies Act 2006.

As the COVID-19 pandemic took hold in early 2020, it became clear that its impacts would be felt throughout society.

In the early weeks of the pandemic and having monitored attentively the emerging effects of COVID-19 for the business and its prospects, including through frequent meetings of our Market Disclosure Committee, the Board took the decision to update the market by way of an additional trading statement highlighting the impacts of COVID-19 on the business, setting out a framework for assessing the potential impact of the pandemic on future trading and confirming our decision to pause the £350m share buyback programme as a way of preserving liquidity at a time of uncertainty.

As a Board, we were of the view that Pearson should offer support to as broad a range of stakeholders as possible during this challenging period, and were conscious of the need to balance internal and external demands and to prioritise use of resources. Accordingly, the Chair called an additional meeting of the Board in mid-April 2020 to consider financial scenario planning and the company's broader response to the pandemic. Our key areas for discussion at this meeting were:

- whether to continue to recommend payment of the final dividend for 2019, as announced at our preliminary results in February 2020
- following government announcements disclosing details of the support schemes available for businesses, whether or not to furlough staff and access these funding schemes

In considering these key issues, the Board had regard to a set of financial priorities and guidelines which had been proposed by the Executive team in order to manage the COVID-19 response consistently across the business. These were framed around projected timelines for a global lockdown period and were matched to financial scenario-planning which had been introduced in the early stages of the pandemic across three different scenarios. The priorities and guidelines included measures which struck a balance between the need to protect the company's liquidity and profitability during that exceptional period, the impacts on our employees, the interests of our shareholders and learners, broader reputational considerations, and ensuring that we maintained a healthy and sustainable business that would be able to seize the opportunities we envisaged in the medium- and longer-term as a result of the accelerated shift to online learning and new ways of working.

The Board also had regard to the views of, and potential impact on, stakeholder groups including through:

- input from brokers and advisers who conveyed the views and interests of the shareholder base
- close discussion with the HR function and senior management in respect of workforce considerations, including the possibility of furlough or redeployment as well as concerns such as the impact of new working conditions for the workforce and how best to provide support to employees

As part of the decision process, the Board considered:

- the strength of Pearson's balance sheet and existing levels of access to liquidity
- the extent to which the scenario-planning and input from brokers and advisers had taken into account the possibility of a second wave of the pandemic later in the year or other worst-case scenarios
- moral and reputational considerations associated with the issues of dividend payment and staff furlough, with recognition of the support provided to the company by shareholders and employees through recent transformation activity and noting the importance of that continued support to Pearson's post-pandemic success

Through its oversight of Pearson's response to the pandemic, the Board demonstrated its regard for multiple stakeholders in its decision-making and balanced their interests in order to best promote the success of the company.

Summary of key Board decisions

Shareholders
We continued to pay dividends and paused the share buyback programme

Liquidity
We were able to leverage our strong balance sheet to avoid the need to access government funding

Employees
We did not furlough any staff, instead redeploying where necessary to support greatest areas of need

Customers
We made available free resources to aid online learning. See p13 and p29

Society and broader stakeholders
All Directors made voluntary donations to charities supporting COVID-19 response efforts. See p116

Corporate governance review

Engagement with stakeholders

A strong understanding of our stakeholders and their views is integral to Pearson's strategic planning process, and the Board's strategy sessions are informed by the views and needs of a wide range of stakeholders including customers (such as learners and educational institutions), technology companies, authors, shareholders, members of our Digital Advisory Network, Pearson management and the wider workforce.

As required by the Code, the Board ensures that Pearson engages effectively with, and encourages participation from, its key stakeholders. The Board maintains its oversight through a variety of direct and indirect mechanisms, where possible, and the Reputation & Responsibility Committee monitors the Group's stakeholder engagement framework.

More information on Pearson's key stakeholders, including their areas of concern and our response, is set out in the Strategic report on pp28–29. Further information on how the Directors discharge their duties under S172 of the Act is available on p30

Engagement during 2020

Whilst direct engagement with stakeholders has been challenging for the Board to undertake during a period of prolonged lockdown and travel restrictions, the views of stakeholders have been a key consideration in papers presented to the Board and its Committees and during Boardroom discussions, thus influencing strategic planning and decision-making. This ensured that, whilst physical engagement was not possible for most of the year, the Board made sure that stakeholders still had a voice within the Boardroom. Board members are of the opinion that, despite the difficulties presented by the pandemic, they were able to virtually engage with the company's stakeholders. Some examples of the key activities undertaken by the Board or by individual Directors in relation to stakeholder matters are set out below. For a more detailed look into how the Board has been able to focus on employee engagement, see the following page.

ENGAGEMENT WITH STAKEHOLDERS EXAMPLES

General approach

The Board considered the needs of various stakeholders as a result of the pandemic. This is demonstrated by the company's provision of free services to learners (e.g. UK Learns, on which the Board received presentations, product demonstrations and provided feedback). Through discussions the Board was also able to consider the acceleration of the company's strategy and online presence, as well as future opportunities with employers and new partners, all whilst providing an immediate benefit to the consumer, employers and the community as a whole, and ensuring that the actions taken were financially viable and therefore continuing to support internal stakeholders and our shareholders.

Learners

Consideration was given to the views of consumers, educators and educational institutions on teaching and learning during the pandemic, including their usage and perceptions of Pearson products.

Product demonstrations and communication meant there was a continual feedback mechanism between the company and external stakeholders, which was fed back to the Board.

Examinations

Due to the disruption in exams in the UK (and internationally), there was frequent engagement with government and regulators, educators, institutions and learners by Pearson (including senior management), with the Board providing guidance and listening to the views of these diverse stakeholder groups. This also enabled the Board to consider future strategy and difficulties that may persist if the COVID-19 pandemic continues.

Diversity

The Board recognises the importance of diversity and encourages the company's approaches in addressing this subject matter. As such, the Board has been supportive of the strategies suggested by the DE&I task force, the formation of which was led by the Chief Executive at the time, John Fallon.

The priorities of the DE&I task force are to address issues of importance to stakeholders, including making Pearson products and services anti-racist, collaborating to reform the education systems and ensuring that representation at management levels reflect the racial and ethnic diversity of the geographies in which we operate. Ms Cox also met with members of the task force to discuss how the Board considers its own diversity, and to learn more about the work of the task force first hand. Board diversity was an area of attention for the task force and the Nomination & Governance Committee agreed to increase its target for Directors of colour. During 2020 the Board received regular updates in the form of presentations and Board papers, enabling the Directors to participate in the implementation of strategic initiatives, asking key questions and offering opinions as needed.

Topics discussed during the year included the adoption of a new Code of Conduct and revising talent and recruitment policies, both of which relate to our employees.

In addition, the Board has endorsed a review into the company product and services portfolio to eliminate and prohibit bias, and to better represent our customers and business partners.

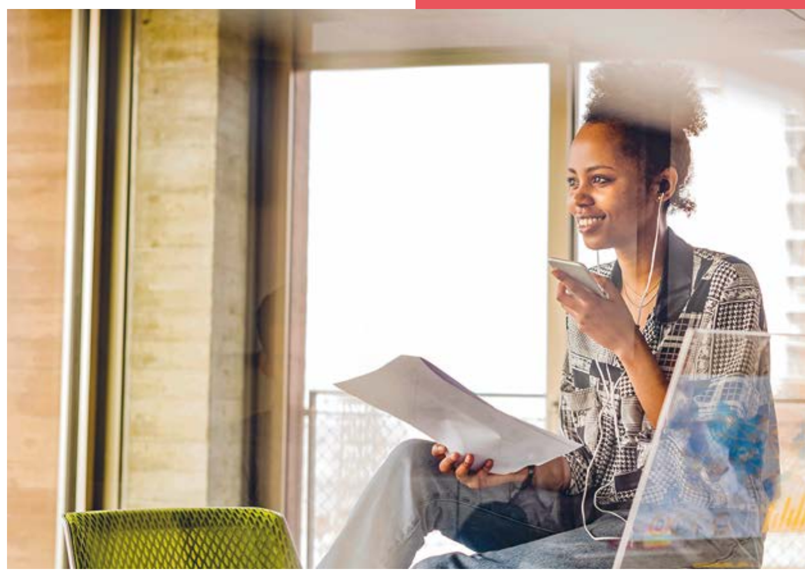
As a result of this, the Reputation & Responsibility Committee has committed to developing a pipeline of more diverse authors. See more on pp88–89

Shareholders

Shareholders are, and will remain, a key consideration in Board decision-making. Although, unfortunately, the Board was unable to engage in person with shareholders at the 2020 AGM and later General Meeting, shareholders were invited to ask any questions of the Board by submitting questions in advance of the meetings. The Board has been able to continue its dialogue throughout the year with our largest shareholders, including extensively in relation to the appointment of our new Chief Executive. This is in addition to the in-person lunch and product demonstrations held in February 2020 with the five largest shareholders. Furthermore, as the pandemic persists, the Board is committed to offering shareholders additional methods of communication. This is demonstrated by the online shareholder event to be held prior to the 2021 AGM.

Employee engagement

This case study provides an illustrative example of how the Board has had regard to employees and their interests in its decision-making processes.



Whilst the Board took stakeholders views into account when making decisions during 2020, it is recognised that engagement was impacted due to COVID-19. For more information on the Board's decision making with regards to COVID-19, see p79. Despite physical interactions being limited, the Directors established a number of methods to engage with employees throughout the year. The Board recognises that Pearson employees are integral to the business and therefore made sure that, in a year of upheaval, employees were listened to, appreciated, supported and rewarded.

At the beginning of 2020 there was little comprehension of the year to come. The Employee Engagement Network (EEN) had established a feedback mechanism between the Board and the workforce, which enabled the Board to hear directly from employees, as well as creating an opportunity to gain additional insight on how to enhance employee satisfaction and work effectiveness, and help engage and retain high performers. This feedback is primarily by a designated Non-Executive Director, Vivienne Cox, engaging with a panel of employee representatives who reflect geographical, generational, operational and cultural diversity as well as length of service. Following each EEN meeting, Ms Cox updates the Board on matters discussed. As part of a review of the EEN's effectiveness, feedback was sought from employee representatives. Areas that members were invited to comment on included accountability, the feedback mechanism and the Network's ability to engage with the rest of the workforce. As a result, EEN members are now encouraged to seek feedback and perspectives on issues from colleagues to ensure that the Board receives a broader range of responses, thereby allowing Directors to be aware of, and understand, broader employee sentiments and make decisions accordingly. These quarterly meetings have also been periodically attended by the Chief Executive and Chief Human Resources Officer. Key topics highlighted in 2020 included working from home, returning to the office, learning and development, wellbeing, diversity and inclusion and the culture of the business. This proved insightful, given the remote nature of working during 2020.

Following Andy Bird being announced as Chief Executive, as he was unable to visit the various company locations, operational sites or meet face-to-face with senior management and employees, Mr Bird led global town halls, participated in functional team meetings and also put in place a series of monthly videos, where he would discuss anything of importance to the company, employees, the wider society, or him personally. The 'Ask Andy' forum was also established, which was set up so employees could share comments, feedback and questions with Mr Bird, to which he personally responds. This enabled Mr Bird to get to know employees both formally and informally.

The Board also receives the results of the quarterly employee surveys, which the entire workforce is encouraged to participate in, and which provide an oversight into employee health and wellbeing, as well as employees' opinions on DE&I initiatives and the company's management. The survey also gives employees an opportunity to provide written feedback, which is summarised and, if there are underlying trends or common themes, presented to the Board.

The Reputation & Responsibility Committee also had sessions on employee health and wellbeing during the pandemic. As a result of this, the Committee decided to explore additional options to support those on the front line.

Key outcomes for 2020

Despite the difficulties 2020 presented, the Directors have been provided with insights into how employees feel about the culture and diversity of Pearson, as well as gauging employee satisfaction more generally. Specific examples include the Directors identifying areas where employees needed additional support, and acting accordingly. As a result, five actions were announced to help support employees, including a paid shutdown in response to health and wellbeing concerns. The Pearson WELL programme was also announced, which will be rolled out globally in 2021. This is a research-based approach to improving employee wellbeing and productivity as a consequence of feedback from both the survey and the EEN and has been endorsed by Directors.

> "It gives me access to engage with Executive management and the Board and contribute in conversations that shape our organisation for the better.
>
> **John Mahlangu** Employee Engagement Network member

Corporate governance review

Board evaluation

The Board operates a three-yearly evaluation cycle which employs a variety of methodologies to ensure the most effective results.

Three-yearly evaluation cycle

Year	Methodology	Last undertaken
1	Questionnaire, tailored to specific needs of the business	2018
2	Internally facilitated interviews, to be led by the Chair, Senior Independent Director and/or Company Secretary as appropriate	2019
3	In-depth evaluation, externally facilitated	2020

Approach and methodology

This Review of the Board's effectiveness was carried out by an external facilitator, Jan Hall Consulting Limited (trading as 'No. 4'), which operates as an independent advisory firm. This Review was conducted as a facilitated self-evaluation.

No. 4 was selected following a review by the Nomination & Governance Committee of various providers and consideration of the potential scope of the evaluation. In addition to facilitating the Board evaluation, No. 4 was also engaged by Pearson in relation to Senior Executive search activity during the year, but otherwise has no other connections to the company or individual Directors.

EVALUATION PROCESS

No. 4 interviewed each of the Board Directors, and also the Executive team members and others closely involved with the Board, all on a confidential and unattributable basis.

The No. 4 Review sought the views of Directors on the effectiveness of the organisation and dynamics of the Board and the Committees, the papers and topics covered at Board and Committee meetings, the purpose and culture of the business, stakeholder engagement, the relationships between the NEDs and management, and the composition and leadership of the Board.

The lead Partners from the external Audit and Remuneration advisory firms were also interviewed.

The output of the evaluation was captured in a report to the Board in December 2020 to enable the Directors to discuss the points raised by the Review.

Discussion areas covered during the individual interviews included matters that are important to Pearson in particular, as well as those items laid down in the Code and associated guidance, including:

- the effectiveness of the organisation and dynamics of the Board and Committees, including composition, competencies, diversity, leadership, agendas, quality of the information provided, governance and decision-making
- relationships between the Board and senior leaders, and between members of the Board itself, including the remits of and interaction among the respective Committees and with the Board
- succession planning for Executive Directors and other senior leaders
- the company's purpose and the Board's monitoring of organisational culture and behaviours
- stakeholder engagement
- understanding of risks facing the company, including probability and mitigation
- concerns and areas for improvement

The Nomination & Governance Committee reviewed the findings from the Board evaluation with the full Board and the evaluator at its meeting in December 2020. To ensure that the process was robust, following the December Committee meeting, No. 4 and the Senior Independent Director held a discussion to confirm that all the information provided in the report was a fair reflection of the range of views provided by each of those interviewed and that the conclusions in the report were not influenced inappropriately by anyone. The Committee will develop an action plan to address areas for improvement and will monitor progress during the year.

In reporting back to the Board, the evaluator reported that conversations with Board members were positive, with unanimous agreement that the Board operates effectively.

Key findings included:

- a high overall level of satisfaction with the functioning of the Board, the competence and capabilities of the Directors, and the quality of relationships between Chair, Non-Executive Directors and the Executive
- a high level of commitment within the Board to Pearson's purpose and a recognition of the significant work done by management to set Pearson up for success in its mission
- positive views in relation to the performance of the Committees including the volume and importance of the work that they undertake on behalf of the Board
- the composition and size of the Board was considered to be appropriate, with a good balance of skills and capabilities, although it was acknowledged that the Board was approaching a number of retirements and the refreshment of its skills and capabilities was a priority, with succession plans in flight
- an acknowledgement that the restrictions on travel and physical meetings afforded by the global pandemic in 2020 had provided challenges for some aspects of interaction between Board members and with management

There was unanimous agreement that the Chair leads the Board in an effective manner, fulfilling Principle F of the Code. The Directors agreed that he demonstrates objective judgement, promotes a culture of openness and debate, and facilitates constructive board relations and the effective contribution of all Non-Executive Directors. This in turn supports Non-Executive Directors in fulfilling the requirements of Principle H of the Code in providing constructive challenge, strategic guidance, offering specialist advice and holding management to account.

The main areas identified by the Board for particular focus during 2021 were:

- supporting the new Chief Executive in delivering on his new vision and strategy for the company, including evolving and monitoring company culture and refreshing risk analysis
- ongoing attention to the balance between strategic considerations and performance monitoring, including in respect of the type and level of information received at Board level, the balance of opportunities for debate and specific decision-making, the assessment of appropriately revised KPI reporting and consideration of market insights
- further supporting Pearson's ESG sustainability agendas, including DE&I
- supporting the company in its ongoing digital transition, including ensuring it can continue to operate successfully in both digital and non-digital worlds where relevant
- ensuring that, despite ongoing pandemic restrictions, the Board, Committees and executive management continue to enhance their virtual interactions, including one-to-one discussions of the evaluation's findings and seeking opportunities for more virtual engagement with the wider workforce as well as other stakeholders where appropriate

In addition, a number of actions were taken during the year in response to findings arising from the 2019 Board evaluation process facilitated by the Senior Independent Director. You can read more about progress on these in the table below.

The Board has confirmed that these items were addressed to its satisfaction, with recommendations having been put into practice or a clear action plan identified for each.

Further, the Chair meets regularly with the Non-Executive Directors as a whole and these sessions include reciprocal feedback on the functioning of the Board to augment the formal Board evaluation process.

Individual evaluation

In addition to the evaluation of the Board as a whole, Executive Directors are evaluated each year on their overall performance against goals agreed by the Board, and in respect of personal objectives under the company's annual incentive plan. These goals and objectives are linked to the key metrics for the company, including both financial and strategic objectives as well as goals linked to culture, talent and brand. Progress against each of these metrics is reviewed by the Board on a regular basis, as part of a dashboard of KPIs.

The Chair leads a formal individual evaluation of each Non-Executive Director every other year and encourages open channels of communication between Directors and the Chair on an ongoing basis. In the Board's opinion, these ongoing lines of communication, combined with a Group-wide culture which allows and encourages feedback at any time, provide the most effective means for evaluation. In assessing the contribution of each Non-Executive Director, the Chair has confirmed that each continues to make a significant contribution to the business and deliberations of the Board. The Non-Executive Directors, led by the Senior Independent Director, also conduct an annual review of the Chair's performance, with the Senior Independent Director providing feedback from this review to the Chair.

Committee evaluation

All Committees undertake an annual evaluation process to review their performance and effectiveness. For 2020, the Committee evaluation process formed part of the wider Board evaluation led by the external evaluator. The findings from this were initially considered by the Board as a whole in December 2020 and are being assessed in more detail at Committee level in 2021. More on this can be read in the Committee reports on the pages that follow.

Progress on findings of 2019 evaluation

Finding	Response/action taken
Refinement of the strategy, in particular continuing to develop the framework supporting lifelong learning and employability and ensuring clear articulation of the strategy	The Board acknowledges the significant progress that has been made on development of the strategy, particularly in respect of the articulation of the five-year strategic vision. Support for Andy Bird as he articulates his new vision and strategy for the company will be a key focus throughout 2021 and the Board is mindful of the need to balance the long-term considerations with execution of short-term goals in a challenging environment for certain parts of the business.
Monitoring and challenge of the digital transformation, including scrutiny of progression metrics and oversight of the continued roll-out of digital products	During 2020, the Board closely monitored progress on the digital transformation through the regular dashboard and deep dives on US Higher Education Courseware, the Pearson Learning Platform (PLP) and Global Online Learning.
Monitoring the risk of transformation fatigue within the organisation	Throughout 2020, the Board monitored both the impact of ongoing transformation pressures on the workforce, and also the impact of the global pandemic, through regular reporting of employee surveys and meetings with the Employee Engagement Network.
An ongoing focus on customers, including appropriate market and behavioural insights to facilitate the right level of scrutiny and challenge by the Board	During the year, the Board received updates on the competitive landscape and discussed customer trends during its regular sessions on the US Higher Education Courseware business. Additionally, the Board's milestones dashboard contains metrics regarding Pearson's performance in the markets in which the company operates, and the competitive landscape is a factor considered in any proposals relating to acquisitions or disposals.

Nomination & Governance Committee report

Committee Chair
Vivienne Cox

Members
Elizabeth Corley, Sherry Coutu, Vivienne Cox, Tim Score and Sidney Taurel

Committee responsibilities include:

→ Appointments

Identifying and nominating candidates for Board vacancies.

→ Balance

Ensuring that the Board and its Committees have the appropriate balance of skills, experience, independence, diversity and knowledge to operate effectively.

→ Succession

Reviewing the company's leadership needs with a view to ensuring the continued ability of the organisation to compete in the marketplace.

→ Governance

Reviewing and overseeing Pearson's corporate governance framework, including culture and employee engagement, Board evaluation and training plans, and Board Diversity Policy.

Terms of reference

The Committee has written terms of reference which clearly set out its authority and duties. These are reviewed annually and can be found on the company website at plc.pearson.com/en-GB/company/business-operations.

Committee attendance

Attendance by Directors at Nomination & Governance Committee meetings throughout 2020:

	Meetings attended
Elizabeth Corley	7/7
Sherry Coutu	7/7
Vivienne Cox	7/7
Josh Lewis[1]	2/2
Tim Score	7/7
Sidney Taurel	7/7

1 Mr Lewis retired from the Pearson Board and the Committee on 24 April 2020.

Role and business of the Committee

The Committee monitors the composition and balance of the Board and of its Committees, identifying and recommending to the Board the appointment of new Directors and/or Committee members. The Committee has oversight of the company's compliance with, and approach to, all applicable regulation and guidance related to corporate governance matters. The Committee also oversees talent and succession plans for senior roles.

Following the retirement of Josh Lewis from the Board in April 2020, the Committee comprises four independent Non-Executive Directors and the Chair of the Board. The Chief Executive and other senior management, including the Chief Human Resources Officer, attend Committee meetings by invitation. All Committee members demonstrated a strong attendance record during the year (see left). In addition to the scheduled meetings held during 2020, the Committee also met as required to consider the Chief Executive succession process.

As Committee Chair, I was pleased to be able to meet some of our larger shareholders at an event in early 2020 and I remain available to engage with any shareholders who have questions or comments about the work of the Committee.

Areas of governance focus during 2020

Throughout 2020, a key area of focus for the Committee was the continued consideration of the revised UK Corporate Governance Code, which came into effect in 2019, in particular to ensure that the agreed revisions to Pearson's governance framework were working effectively following implementation. As part of this, the Committee received a status tracker at each meeting to enable it to consider the appropriateness and maturity of various elements of the framework. Notable items which the Committee discussed as part of its governance oversight role included:

› a review of the effectiveness of the Employee Engagement Network and broader range of workforce engagement mechanisms (see p81)

› development of a culture dashboard to aid the Committee and Board's oversight of Pearson's culture, reflecting cultural priorities, experiential indicators and external benchmarking data (see p77)

› monitoring progress against the agreed areas of focus from the 2019 Board evaluation process (see p83)

Other areas of focus for the Committee during the year included: oversight of investor governance and voting policies and broader governance thought leadership, particularly investor sentiment in response to COVID-19; an annual review of the Board Diversity Policy and adoption of revised accompanying objectives; and preparation for and oversight of the externally facilitated Board evaluation process for 2020. The Committee also received periodic updates from the Chief Human Resources Officer and members of the HR team in respect of diversity and talent initiatives across the business – see p87 for further detail.

Board search and appointments

A key element of the Committee's remit is to lead the process for Board appointments in line with appropriate succession plans. The Committee has defined a set of specific criteria for potential new Non-Executive Directors, in particular giving consideration to the skills, experience and knowledge required in any candidates. Pearson expects all Non-Executive Directors to demonstrate the highest level of integrity and credibility, independence of judgement, maturity, collegiality and the commitment to devote the necessary time.

As part of its regular succession planning activity, and with regard to the upcoming retirements of Ms Cox and Mr Lynton from the Board at the 2021 AGM, the Committee launched a Non-Executive Director search process in the second half of 2020. In preparing for this search, the Chair of the Board and all existing Non-Executive Directors were asked to complete a self-assessment of the skills and experience which they believe they each bring to the Board. The results of this assessment were mapped against Pearson's areas of strategic focus and the anticipated Non-Executive Director retirement timelines in order to identify the key characteristics desired in any potential new Board members and the order of priority for hiring. The Committee agreed that it was particularly interested to identify candidates who would bring a combination of skills and expertise in the following areas:

- global or multinational executive experience, particularly relating to leading complex companies through digital transformations
- UK listed company governance
- digital and/or data analytics
- direct to consumer experience

Taking into account the agreed person specification, the Committee has engaged Russell Reynolds Associates to undertake a search process for new Non-Executive Directors. In line with the objectives of the Board's Diversity Policy, the Committee has asked Russell Reynolds Associates to ensure that the list of candidates reflects diversity of gender and ethnicity as well as diversity in its broadest sense.

At the end of 2019, following the announcement by John Fallon of his intention to retire from the Pearson Board, the Committee commenced a search process for a new Chief Executive, accelerating the ongoing succession planning processes which are regularly reviewed by the Board. The Chief Executive search process was led by the Chair of the Board, Sidney Taurel, and the Committee, led by Ms Cox, was engaged in the management of the process which was reviewed several times by the full Board. The search process resulted in the appointment of Andy Bird who became Pearson's Chief Executive on 19 October 2020.

Andy Bird was initially identified as a potential future Chief Executive candidate in 2019 as part of ongoing succession planning processes conducted by the Board. Although Mr Bird was not in a position to pursue the opportunity to become Chief Executive once Mr Fallon had announced his intention to retire, Mr Taurel recognised that Mr Bird's skills and wealth of experience would nevertheless be invaluable to Pearson, leading to the Board's decision to appoint him as a Non-Executive Director with effect from 1 May 2020. Upon joining the Board, Mr Bird quickly realised the full potential of Pearson and became receptive to taking on the Chief Executive role.

The search process, which included internal and external candidates, was based upon selection criteria including traits such as:

- Highly successful experience in leading a large, international business
- Experience in digital transformation and disruption
- Track record of shareholder value creation
- Experience in brand building
- Cultural fit with Pearson values combined with the ability to effect and accelerate change
- An interest in education
- Strong reputation, integrity, independent thinker

Nomination & Governance Committee meeting focus during 2020

→ Appointments and succession

- Executive and Non-Executive Director succession planning and search activity, including appointment of Andy Bird
- Review of Directors' commitments guidance framework
- Induction outline for new Directors including feedback from recent appointees

→ Balance

- Membership of Board Committees
- DE&I initiatives at Pearson
- Review and approval of Board Diversity Policy and revision of accompanying objectives

→ Governance

- Board evaluation preparation and findings
- Compliance with UK Corporate Governance Code
- Review of effectiveness of the Employee Engagement Network
- Oversight of development of culture dashboard
- Review of Committee terms of reference
- Review of Chair, Chief Executive and SID responsibilities

The thorough and rigorous search process, in which around 100 individuals were considered, yielded several highly qualified candidates. The Board was satisfied that Mr Bird met and exceeded the selection criteria and was the standout candidate and accordingly approved the prospective appointment of Mr Bird as Chief Executive. Mr Bird was not a member of the Nomination & Governance Committee and furthermore was excluded from any Board discussions or decisions relating to Chief Executive succession when he himself was a candidate. The prospective appointment of Mr Bird as Chief Executive announced in August 2020 was subject only to shareholder approval of certain elements of his remuneration package. Read more in the Directors' Remuneration Report on p100

Pearson was assisted in the search process by Russell Reynolds Associates (search activity) and Jan Hall Consulting Limited (trading as 'No. 4') (advisory activity). In addition to the Non-Executive Director and Chief Executive search processes, Russell Reynolds Associates undertakes broader executive search activity for the Group and is a signatory to the Voluntary Code of Conduct for Executive Search Firms. During 2020, in addition to advisory activity relating to the Chief Executive search, No. 4 was engaged to facilitate the annual Board evaluation process.

Nomination & Governance Committee report

Committee evaluation

In 2020 the Committee evaluation formed part of the wider Board evaluation process facilitated by No. 4. The process sought views through a series of one-to-one interviews from all members of the Board, the Pearson Executive Management team, the Company Secretary and his deputy, and areas covered included the effectiveness and dynamics of the Committee, the quality of papers and meeting discussions and the relationships between the Committee and management.

The Committee was considered to have operated effectively throughout 2020 with a clear agenda, focused on the issues of greatest importance, and was led effectively by its Chair. Following the appointment of a new Chief Executive, it is recognised that the Committee will now pivot its attentions to supporting the Board in respect of broader executive succession planning and the development of the talent pipeline.

Committee aims for 2021

In 2021, the Committee will continue to pay attention to the principles and provisions of the Code, giving consideration to areas in which there may be scope to go above and beyond Pearson's current governance arrangements in continuing to ensure a world-class corporate governance framework. We will continue to monitor Pearson's culture in support of the Board's broader oversight of culture and organisational health. We will also hold updates on DE&I and talent and succession, ensuring that the overall frameworks through which the Board oversees these matters are thorough and robust. Additionally, the Committee will oversee the Board evaluation process and monitor progress against the findings from the most recent cycle, and will continue to lead Non-Executive Director search activity, as required, in accordance with Pearson's well-established succession plans.

Vivienne Cox
Chair of Nomination & Governance Committee

Diversity across Pearson

One of the legacies of 2020 is the elevated awareness and conversations around racial justice and inclusive leadership. The Board has taken a close interest in the company response and in October approved a detailed action plan setting out a series of goals and 50 key initiatives for implementation over the next 12 to 18 months. The Board intends to continue to pay attention to how the plan is progressing and the impact it has on increasing diverse representation and in tackling systemic racism at Pearson.

Our Code of Conduct sets out our global standards and responsibilities with regard to DE&I at all employee levels, including the Pearson Executive Management team, and covers many aspects, including gender, age, ethnicity, disability and sexual orientation. This is underpinned by a global statement on DE&I along with country- and business-specific policies. The Global DE&I Council chaired by Chief Executive, Andy Bird, oversees progress on the company DE&I strategy at Pearson. This comprises around 30 members representing employee resource groups, business leaders as well as allies and advocates. For more information on the company's approach to DE&I, see p50 in the Sustainability section.

Board diversity

The commercial benefits of having a diverse Board are well established. At Pearson, we believe that diversity of all types on the Board makes us a better business by enabling enhanced commercial results, and also that inclusive leadership for the company leads to better decision-making. It also reflects an overt commitment to finding and retaining the best, most diverse talent.

The Board embraces the Code's underlying principles with regard to Board balance and diversity, including in respect of ethnicity, gender and age. The objectives set out in the Board's Diversity Policy and our progress towards these objectives are shown in the table opposite. The Committee ensures that the Directors of Pearson demonstrate a broad balance of skills, background and experience, to support Pearson's strategic development and reflect the global nature of our business.

The Committee also ensures that appointments are made on merit and relevant experience, while taking into account the broadest definition of diversity. In the current Non-Executive Director search process, the Committee has encouraged the retained search firm to place an emphasis on putting forward candidates who will enhance the overall diversity of the Board.

The gender diversity of the Board was 45% female representation as at 31 December 2020 (2019: 33%), exceeding the recommendations suggested by the Hampton-Alexander Review aimed at having at least 33% female representation on the Board by 2020. Pearson also satisfies the recommendation in the Parker Review that at least one Director should be from an ethnic minority background ahead of the 2021 target date.

The Board evaluation process conducted in 2020 found that, although Directors believe that the Board's diversity in terms of gender is good, more should be done in respect of other types of diversity, particularly racial and ethnic diversity. Additionally, the Board will pay particular attention to cognitive diversity in its succession planning and talent activity, ensuring that Pearson can benefit from the different viewpoints and ways of thinking and working demonstrated by a cognitively diverse group.

In light of the global events of 2020 and reflecting Pearson's commitments to create a more equitable and inclusive company, we are determined that, as a Board, we must also be representative of our employee base and wider society, including the countries in which we operate. We have therefore adopted revised targets in support of our Board Diversity policy, namely that we will strive to achieve and maintain a Board composition of:

› at least 40% female Directors (previous target: 33%)

› at least two Directors of colour (previous target: one)

In addition to consideration of the Board Diversity Policy, the Nomination & Governance Committee continued its wider oversight of DE&I. This year, the Committee considered inclusion in the context of a wider proposal on culture as well as a detailed report on disability inclusion as part of the company commitment to Valuable 500. For more information on Valuable 500, see p45 in the Sustainability section.

Diversity and talent in Executive pipeline

On our Executive team, there are currently three women out of 10 members (30%) – this excludes the Chief Executive and Chief Financial Officer who are counted in the Board's metric (2019: 22%). Including the Chief Executive and Chief Financial Officer, this rises to 33% women (four women out of 12 members) (2019: 18%). As of 31 December 2020, the number of women forming part of the senior management team, i.e. the Pearson Executive Management team and their direct reports, including the Company Secretary, as required by the Code, is 35 women, representing 36% of that group (2019: 34%).

We have a multi-pronged plan in place to build our pipeline of women in leadership and senior management positions, and the Board and Committee will carefully monitor their development, and the development of all key talent. The Committee also received an update on an internal mentoring scheme whereby each Director is paired with a high-potential female leader at Pearson. This launched at the end of 2018 and, following a successful first cohort in 2019, the Committee agreed during the year that the programme should continue in 2021 with a further cohort of participants. As part of its review of the mentoring scheme in 2020, the Committee also discussed learnings from the first year of the programme and agreed with HR certain additional measures to augment the support provided to both mentors and mentees for future cohorts.

Pearson operates a portfolio of accelerated learning and career development experiences targeted at the Executive pipeline. In 2020, the Global DE&I Council launched a pilot sponsorship programme for diverse talent, focusing particularly on ethnicity and gender. The pilot is designed to assess how sponsorship and senior-level advocacy in the workplace can produce career dividends for protégés and for their sponsors. The model has subsequently been adopted across the company.

Board diversity objectives

During the year, the Committee received a detailed progress update on the company's DE&I strategic approach, framework, governance and measurement models and priority areas. As part of this deep dive, the Committee reviewed and updated the objectives which underpin the Board Diversity Policy. The current objectives, and Pearson's performance against them, are set out below:

Objectives	Progress
We will strive to achieve and maintain a Board composition of: △ › at least 40% female Directors △ › at least two Directors of colour.	✓ The Board includes 45% female Directors at 31 December 2020. ✕ The Board includes one Director who identifies as Mixed – White & Black Caribbean. Diversity, including of race and ethnic background, is a priority area of focus in our ongoing Non-Executive Director search process.
All Board appointments will be made on merit, in the context of the skills and relevant experience that are needed for the Board to oversee Pearson's strategic development and that reflect the global nature of our business.	✓ The Chief Executive search process in 2020 considered a wide range of candidates, including from diverse backgrounds, all of whom were evaluated on the basis of merit. The process resulted in the appointment of Andy Bird whom the Board believes possesses the requisite skills and experience for the role.
The Board will continue to incorporate a focus on a diverse pipeline in its succession and appointment planning including to prioritise the use of search firms which adhere to the Voluntary Code of Conduct for Executive Search Firms (the Voluntary Code) when seeking to make Board-level appointments.	✓ Russell Reynolds Associates assisted Pearson with search activity during 2020, including the external element of the Chief Executive search, and have been appointed in respect of current Non-Executive Director search process. Russell Reynolds Associates are a signatory to the Voluntary Code.
The Board will continue to adopt best practice, as appropriate, in response to the Hampton-Alexander Review and the Parker Review.	✓ The recommendations of the Hampton-Alexander Review and Parker Review in respect of gender and ethnic diversity have been noted by the Board, and were considered as part of the Committee's diversity deep dive in 2020.
The Board will consider its composition and diversity as part of its consideration of effectiveness in the Board evaluation review process.	✓ These matters were considered in the 2020 evaluation process. Read more on p82
Where appropriate, we will assist with the development and support of initiatives that promote all forms of DE&I in the Board, Pearson Executive Management team and other senior management.	✓ Board mentoring scheme of senior leadership talent ran throughout 2019. Following its success, the Nomination & Governance Committee has approved a further round of the programme which will commence in 2021.
We will review and report on our progress in line with the policy and our objectives in the annual report, including providing details of initiatives to promote DE&I in the Board, Pearson Executive Management team and other senior management.	✓ The Nomination & Governance Committee reviewed the Board's Diversity Policy and accompanying objectives during the year, as well as developments on DE&I in the external landscape.
We will continue to make key DE&I information, about the Board, senior management and our wider employee population, available in the annual report, and aim for ongoing transparency in this area in line with best practice.	✓ This information is included in the annual report. Read more about DE&I matters in the wider employee population on p50

✓ Target achieved △ Changed target ✕ Target not met

Reputation & Responsibility Committee report

Committee Chair
Linda Lorimer

Members
Andy Bird, Vivienne Cox, Linda Lorimer, Michael Lynton, Graeme Pitkethly and Lincoln Wallen

Committee responsibilities include:

→ Reputation & stakeholders

Pearson's reputation among major stakeholders, including governments, investors, employees, customers, learners and the education community.

→ Risk

Oversight of Pearson's approach to reputational risk, and ensuring that clear roles have been assigned for the management of the reputation dimension of risks identified.

→ Sustainability & ethics

Oversight of Sustainable Business Plan 2030 and performance against sustainability goals and commitments. Ethical business standards, including Pearson's approach to issues relevant to its reputation as a responsible corporate citizen.

→ Brand & culture

Management of the Pearson brand to ensure that its value and reputation are maintained and enhanced. Pearson's approach to monitoring and supporting the values and desired behaviours that form our corporate culture.

→ Strategy

Strategies, policies and communication plans related to reputation and responsibility issues and the people and processes that are in place to anticipate and manage them.

Terms of reference

The Committee has written terms of reference that clearly set out its authority and duties. These are reviewed annually and can be found on the company website at plc.pearson.com/en-GB/company/business-operations.

Committee attendance

Attendance by Directors at Reputation & Responsibility Committee meetings throughout 2020:

	Meetings attended
Andy Bird[1]	3/3
Vivienne Cox	4/4
Linda Lorimer	4/4
Michael Lynton	4/4
Graeme Pitkethly	4/4
Lincoln Wallen	4/4

1 Mr Bird was appointed to the Committee on 1 May 2020.

Reputation & Responsibility Committee role

The Committee works to assess and advance Pearson's reputation across the range of its stakeholders and to maximise the company's impact on society and the communities in which we work and serve.

The Committee reviews matters that are material to Pearson's stakeholders and the company's long-term sustainability. It regularly receives reports about issues and incidents that could adversely affect the company's reputation, including issues raised by regulators. We promote Pearson's sustainability plan and assess the progress in advancing its tenets as well as monitor the Pearson brand. The Committee works in alignment with the company's Responsible Business Leadership Council, which comprises senior leaders from across the company. As Committee Chair, I am available to engage with any shareholders who have questions or comments about the work of the Committee.

Committee composition

Following his appointment to the Board in 2020, Andy Bird was welcomed as a member of the Committee and, as the new Chief Executive, will continue on the Committee. We benefit from the regular attendance of those senior executives whose work is central to the remit of the Committee; these include the Chief Marketing Officer and Co-President of Direct to Consumer, the Chief Legal Officer, the Chief Strategy Officer, and Senior Vice President – Government Relations & Sustainability.

Areas of focus during 2020

At each meeting, the Committee has a report on recent incidents and issues that could have an impact on the company's reputation.

Throughout the year, the Committee paid particular attention to the impacts of COVID-19 on our stakeholder groups, and considered Pearson's response across a number of different areas. In particular:

› we discussed the digital learning resources that had been made available free of charge to support teachers and learners during the early months of the pandemic. Later in the year, we revisited this topic with leaders of the efficacy and research team to gain insights into the views of teachers and learners after a number of months of using the products, and considered how their feedback could be taken into account in future product development cycles

› in conducting deep dives into health and safety and safeguarding, both principal risks for Pearson, we discussed the increasing prevalence of wellbeing issues in young people resulting from COVID-19. We also considered management's approach to safeguarding in online schooling, a matter of considerable importance, particularly given the substantial increase in students learning online in 2020

› following the cancellation of UK exams in summer 2020, we considered with senior leaders from the UK business the impacts on schools and students and reviewed our engagement with the UK Government and exams regulator. We also discussed the lessons that could be learned from COVID-19 to help to shape the future of school assessment

- we focused on the impacts of COVID-19 on employees with particular attention on wellbeing and working practices. We considered the steps being taken to protect those employees working in public-facing roles and evaluated the framework developed to govern decisions around returning to the office for employees who had shifted to remote working, The Committee began to discuss how Pearson's real estate needs might change post-pandemic with more remote or hybrid work arrangements likely to develop

Another key area of focus for the Committee is oversight of matters relating to sustainability and climate change. Sustainability is at the heart of many issues that are central to Pearson's future and is a strong area of interest for our core customers as well as many of our investors. We considered the three main pillars for our Sustainable Business Plan 2030 and, building on our conversations in 2019, we discussed the detailed goals, milestones and timeline underpinning the plan. We monitored developments to strengthen our commitments to a sustainable supply chain, hearing about the implementation of a new sustainable supplier risk management model. Additionally, following discussions with sustainability colleagues on Pearson's approach to climate change reporting, we recommended that Pearson become a supporter of the Task Force on Climate-related Financial Disclosures (TCFD); thereafter, the company publicly declared its commitment to the TCFD and its recommendations. You can read more about Sustainability on pp40–55

Social justice was an important matter throughout the company in 2020, as described on p27. The Committee focused on the work of the internal DE&I task force as it pertained to our customers. One initiative has been to strengthen Pearson's editorial policy to ensure our products and services demonstrate diverse, equitable and inclusive language and content. An additional set of guidelines were published in February 2021 and will be used in creating new educational content as well as in reviewing existing content. The Committee also suggested ways to broaden the diversity of Pearson's pool of authors, collaborators and peer reviewers so more people of colour are included.

Committee evaluation

In 2020, the evaluation of the Committee was included as part of the wider Board evaluation process led by an external facilitator, Jan Hall of No. 4 Consulting. She conducted one-on-one interviews with each Director, the Pearson Executive Management team, and the Company Secretary and his deputy to secure views about each Committee as well as the company generally. The evaluation found that all members felt positive about the work of the Committee, found its discussions thoughtful and the papers for review comprehensive.

Progress on findings of 2019 evaluation

The 2019 evaluation, where the Senior Independent Director interviewed each Board member, highlighted the increasing importance of the Committee's work and the growing roster of matters within its remit. As a result of this feedback, the Committee committed to scheduling four meetings each year and will endeavour to schedule them when either the Board Chair or Chief Executive or both can attend. During 2020, both the Board Chair and Chief Executive attended all of the Committee's meetings.

Committee aims for 2021

Over the next year, the Committee's work will be especially attentive to our growing emphasis on direct to consumer products and services and to overseeing the risks and opportunities associated with our growing consumer relationships. We will continue to explore Pearson's material sustainability issues as part of our oversight of the Sustainable Business Plan 2030 and monitor progress towards meeting the TCFD recommendations. There will be continuing attention to data privacy and the ethical use of data, which are increasingly important matters as the company becomes more digital. The Committee will also oversee Pearson's framework of engagement with all stakeholder groups and consider the broader workplace culture, as we all continue to evolve our ways of working and learning as a result of COVID-19.

Linda Koch Lorimer

Linda Lorimer
Chair of Reputation & Responsibility Committee

Reputation & Responsibility Committee focus during 2020

→ Reputation & stakeholders

- Issues and incidents reports
- UK school exams – COVID-19 impact and response
- Reporting and transparency – investor feedback and insights
- International reputation management
- Global government relations
- Learners and institutions – supporting remote learning
- Global learner survey
- Stakeholder engagement framework

→ Risk

- Safeguarding
- Health & Safety
- Supply chain and partnership risk

→ Sustainability & ethics

- Sustainable Business Plan 2030 – strategy, pillars and commitments
- Sustainable supply chain
- Climate change and TCFD
- Modern Slavery Act statement
- Access to education for underserved groups

→ Brand & culture

- Brand update
- COVID-19 – supporting our employees
- Future workplace and return to office

→ Strategy

- DE&I in our products and content
- Annual communications plan

Audit Committee report

Committee Chair
Tim Score

Members
Elizabeth Corley, Vivienne Cox, Linda Lorimer, Michael Lynton, Graeme Pitkethly, Tim Score and Lincoln Wallen

Committee responsibilities include:

→ Financial reporting

The quality and integrity of financial reporting and statements and related disclosure, including significant reporting judgements.

→ Policy

Group policies, including accounting policies and practices.

→ External audit

External audit, including the appointment, qualification, independence and effectiveness of the external auditor.

→ Internal audit, risk & internal control

Risk management systems and the internal control environment including oversight of the work and effectiveness of the internal audit function.

→ Compliance & governance

Legal and regulatory requirements in relation to financial reporting and accounting matters and oversight of compliance programmes and investigations.

Terms of reference

The Committee has written terms of reference which clearly set out its authority and duties. These are reviewed annually and can be found on the company website at plc.pearson.com/en-GB/company/business-operations.

Committee attendance

Attendance by Directors at Audit Committee meetings throughout 2020:

	Meetings attended
Elizabeth Corley	4/4
Vivienne Cox	4/4
Linda Lorimer	4/4
Michael Lynton	4/4
Graeme Pitkethly	4/4
Tim Score	4/4
Lincoln Wallen	4/4

Audit Committee role

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

Pearson's Vice President – Internal Audit has a dual reporting line to the Chief Financial Officer and to me, and external auditors have direct access to the Committee to raise any matters of concern and to report on the results of work directed by the Committee. As Audit Committee Chair, I report to the full Board at every Board meeting that follows a Committee meeting. I also work closely with the CFO and senior financial, risk, legal and internal audit personnel outside the formal meeting schedule to ensure robust oversight and challenge in relation to financial control, compliance and risk management. As Committee Chair, I was pleased to be able to meet some of our larger shareholders at an event in early 2020 and I remain available to engage with any shareholders who have questions or comments about the work of the Committee.

Audit Committee meetings and activities

Areas of focus during 2020

In an unprecedented year, the implications of COVID-19 were a consistent theme of focus for the Committee throughout 2020. In April, we considered Pearson's response to, and early impacts from, COVID-19 in respect of areas that fall within the Committee's remit, including:

- crisis management and business continuity planning – we discussed with risk and technology personnel the support being provided to employees and customers to enable them to continue to work safely and effectively in the developing pandemic
- financial reporting and liquidity considerations with particular reference to the escalation of the pandemic during March, in response to which Pearson issued an additional trading update to the market on 23 March and provided enhanced and updated disclosures in its external reporting to reflect COVID-19 impacts
- the decision to pause the tender process for Pearson's external audit, which was made in order to ensure a fair tender process and to take into account additional demands on internal teams and audit firms in the immediate phase of response and adjustment to the pandemic

At every meeting, the Committee considered reports on the activities of the internal audit and compliance functions, including the results of internal audits, project assurance reviews and fraud and whistleblowing reports. The Committee also monitored the company's financial reporting procedures, discussed the finance and IT controls environment, reviewed the services provided by PwC and considered any significant legal claims and regulatory issues in the context of their impact on financial reporting, each on a regular basis.

A further key role of the Committee is to provide oversight and assurance to the Board with regard to the integrity of the company's procedures for the identification, assessment, management and reporting of risk. During 2020, we conducted a number of deep dives into selected principal risks, and the key risks on which the Committee focused throughout the year are set out on p60

View the key activities of the Audit Committee below.

Additional meeting attendees

The Chief Financial Officer, other executives and senior managers from across the business also attended meetings during the year, either as regular invitees of the Committee or to discuss particular items of business. This direct contact with key leadership augments the Committee's understanding of the issues facing the business as well as helping to develop Pearson's talent pipeline through facilitation of board-level engagement opportunities for those leaders and managers. The Chair and Chief Executive each attend Committee meetings regularly at my invitation, with the Chief Executive particularly attending for discussion of matters with an operational and customer focus. The Committee also meets regularly in private with the external auditors and with the Vice President – Internal Audit, and as required with the Chief Legal Officer and Vice President – Global Compliance.

Audit Committee training and knowledge sharing

The Committee receives technical updates at each meeting, including on matters such as accounting standards and the audit and governance landscape, and members are able to request specific or personal training as appropriate. In particular, we have kept abreast of developments relating to audits at a legislative and regulatory level, including the FRC's principles for operational separation for audit firms.

Committee members also meet with local management on a periodic basis, such as when travelling for overseas Board meetings, in order to gain a better understanding of how Pearson's policies are embedded in operations. We hope to resume our programme of meeting in person with local management teams as soon as travel restrictions permit, and in the meantime the Committee continues to engage with a wide range of senior management and technical specialists through virtual methods in order to inform our discussions.

Audit Committee meeting focus during 2020

→ Financial reporting

- Accounting and technical updates
- Impact of legal claims and regulatory issues on financial reporting
- Fair, balanced and understandable reporting, going concern and viability statements including supporting analysis
- 2019 annual report and accounts: preliminary announcement, financial statements and income statement
- Review of interim results and trading updates
- Form 20-F and related disclosures, including annual Sarbanes-Oxley Act section 404 attestation of financial reporting internal controls
- Significant issues reporting

→ Policy

- Accounting matters and Group accounting policies
- Annual review and approval of external auditors' policy
- Treasury policy and reporting
- Tax strategy, including an update on EU state aid and impact of global tax reforms

→ External audit

- Provision of non-audit services by PwC
- Receipt of external auditors' report on Form 20-F and year-end audit
- Report on half-year procedures
- Reappointment of external auditors
- Confirmation of auditor independence
- 2020 external audit plan
- Remuneration and engagement letter of external auditors
- Review opinion on interim results
- Review of the effectiveness of external auditors

→ Internal audit, risk & internal control

- Internal audit activity reports and review of key findings
- Organisational risk management
- 2021 internal audit plan
- Assessment of the effectiveness of internal audit function, internal control environment and risk management systems
- Oversight of The Enabling Programme
- Risk deep dives: information security; data privacy; treasury and insurance; anti-bribery and corruption (ABC); tax; business resilience
- Controls Centre of Excellence updates, see more on p98
- Appointment of new Vice President – Internal Audit

→ Compliance & governance

- Fraud, whistleblowing reports and compliance investigations
- Compliance with accounting and audit-related aspects of the UK Corporate Governance Code
- Audit Committee, Verification Committee and internal audit function terms of reference
- Schedule of authorities

Audit Committee report

Committee focus areas for 2021

The Committee's focus areas for 2021 will include:

- Oversight of Pearson's risk landscape, the approach to which will be refreshed reflecting: external trends; learnings from the pandemic response; and strategic areas of focus
- The tender process for Pearson's external audit. See p94 for further information
- Oversight of the shift to five new reporting segments, reflective of our five new business divisions.

Committee evaluation

Building upon the positive findings of the previous year's evaluation process, in 2020 the Committee evaluation formed part of the wider Board evaluation process facilitated by Jan Hall Consulting Limited (trading as 'No. 4'). The process sought views through a series of one-to-one interviews from all members of the Board, the Pearson Executive Management team, the Company Secretary and his deputy, the Vice President – Internal Audit and the lead external audit partner, and areas covered included the effectiveness and dynamics of the Committee, the quality of papers and meeting discussions and the relationships between the Committee and management.

The evaluation found that the Committee is seen by all Board members to function well with appropriate agendas, papers produced to a good standard and high-quality discussions. The deep dives are perceived to be on the right topics and given the proper time and attention, and the Chair was recognised as having a constructive relationship with management. Risk management was a particular theme discussed in the evaluation process, from both a Committee and full Board perspective, and there was general agreement that risk is managed well at Pearson. One specific recommendation related to increasing the Committee's focus on mapping the key risks to the sources of assurance, although this was not thought to be a major gap. This will be taken into account in the refresh of Pearson's approach to its risk landscape during the coming year.

Fair, balanced and understandable reporting

We are mindful of the Code's Principle N relating to fair, balanced and understandable reporting and we build sufficient time into our annual report timetable to ensure that the full Board receives sufficient opportunity to review, consider and comment on the report as it progresses. Learn more about fair, balanced and understandable reporting on p125

Financial reporting and policies

In February 2021, the Committee considered the 2020 annual report and accounts, including the preliminary results announcement, financial statements, strategic report and Directors' report. The significant issues considered by the Committee relating to the 2020 financial statements are set out on p96.

Financial Reporting Council (FRC)

In September 2020, the Group received correspondence from the FRC's Corporate Reporting Review Team who had reviewed the 2019 annual report and accounts. The FRC's role is to consider compliance with reporting requirements and is based solely on the Group's published 2019 annual report and accounts. Their review does not provide assurance that the 2019 annual report and accounts is correct in all material respects. The FRC raised two enquiries, on which the Group was required to respond to help the FRC Corporate Reporting Review Team understand how the Group had satisfied the relevant reporting requirements. The queries related to:

- impairment review and goodwill allocation
- supplier financing arrangements

In addition, the Group was encouraged to make improvements in relation to a number of observations made by the FRC on the 2019 annual report and accounts, if material and relevant.

In October 2020, the FRC Corporate Reporting Review Team confirmed that they had closed all of their enquiries. The suggested improvements have been incorporated into the 2020 annual report and accounts where material and relevant.

Risk assessment, assurance and integrity

As a Committee, we reviewed our organisational risk management processes and discussed risk status reports at our meetings in July and December. In particular, we considered three themes which run throughout Pearson's principal risks – people, process and technology. As part of this biannual review, we consider any significant changes to the Group's risk profile or new issues arising, and discuss Pearson's risk map including: our appetite for key risks; the probability of these arising and impact if they do; and any mitigating arrangements in place. During 2020, we also conducted a number of deep dives into selected principal risks including data privacy, information security, tax, anti-bribery and corruption, and business resilience. You can read more about Pearson's principal risks and uncertainties on p60

At our meeting in December 2020, and again in February 2021, we considered the plans to evolve Pearson's organisational risk management approach through an increased use of deep dives. These will allow our internal risk team to immerse themselves in particular areas of the business, including consideration of Pearson's culture, and to understand associated existing and horizon risks in a holistic manner. As a Committee, we are supportive of this review of our risk environment in the context of Pearson's new strategy and will receive updates on the outputs of this work at each Committee meeting moving forward. Read more about the Board's responsibility for risk on p98

Members

As at the date of this report, the Committee comprises seven independent Non-Executive Directors, all of whom have financial and/or related business experience due to the senior positions they hold or have held in other listed or publicly traded companies and/or similar large organisations. The Committee possesses a good balance of skills and knowledge with competence and experience covering all aspects of the sectors in which Pearson operates – education, digital and services – and the company's key geographic markets.

Tim Score, Chair of the Committee since April 2015, is the company's designated financial expert, having recent and relevant financial experience, and is an Associate Chartered Accountant. He has also previously served as Audit Committee Chair for The British Land Company plc and National Express Group plc. The qualifications and relevant experience of the other Committee members are detailed on pp69–70

Internal audit

The internal audit function is responsible for providing independent assurance to management and the Audit Committee on the design and effectiveness of internal controls, to mitigate strategic, financial, operational and compliance risks. The Vice President – Internal Audit reports formally to the Chair of the Audit Committee and the CFO and is responsible for the day-to-day operations of internal audit and execution of the annual audit plan. The Committee Chair worked closely with senior management on the process for appointing a new Vice President – Internal Audit, whose formal appointment was a matter for the full Committee's approval in early 2020.

The internal audit mandate is approved annually by the Audit Committee. The audit plan and any changes thereto are also reviewed and approved by the Audit Committee throughout the year. The internal audit plan is aligned to our greatest areas of risk, as identified by the organisational risk management process, and the Audit Committee considers issues and risks arising from internal audits. Management action plans to improve internal controls and to mitigate risks, or both, are agreed with the business area after each audit. Formal management self-assessments allow internal audit to monitor progress in implementing action plans, agreed as part of audits, to resolve any control deficiencies identified. Internal audit will request and assess evidence of action plan implementation and may re-test controls if necessary. Progress of management action plans is reported to the Audit Committee at each meeting. Internal audit has a formal collaboration process in place with the external auditors to ensure efficient coverage of internal controls. Regular reports on the findings and emerging themes identified through internal audits are provided to Executive management and, via the Audit Committee, to the Board.

In 2020, internal audit carried out engagements across Pearson's business units and enabling functions covering the majority of the principal risks. The audit plan is dynamic and additional work was done to assess the company's response to COVID-19, with particular focus on third-party risks.

Internal audit evaluation

At its December meeting, the Committee considered the findings of the review of the performance and effectiveness of Pearson's internal audit function, a process which is undertaken annually. The 2020 review was conducted by distributing a questionnaire to the key stakeholders of the internal audit function – including Committee members, the lead external audit partner, members of the Pearson Executive Management team, and senior financial, legal and operational management.

Based on the findings of the Committee's assessment of the effectiveness of the internal audit function, the Committee is of the opinion that the quality, experience and expertise of the function is appropriate for the business. A specific area identified during the internal audit evaluation was to ensure that the way the function is staffed continues to reflect Pearson's strategy, including through ensuring appropriate skills in the internal audit team in the areas of data analytics, programme assurance and auditing digital transformation.

In 2019, the Internal Audit function underwent its first independent external assessment, in line with the requirements of the International Standards for the Professional Practice of Internal Auditing, which was facilitated by Protiviti. The findings indicated an effective internal audit function that conforms to the Institute of Internal Auditors' International Standards. Opportunities for improvement noted as part of the 2019 assessment largely related to the quality of supporting documentation. In 2020, progress has been made in this respect with greater rigour in the documentation and review of audit engagements.

Compliance, fraud and whistleblowing

The Vice President – Global Compliance oversees compliance with our Code of Conduct and works with senior legal and HR personnel to investigate any reported incidents, including ethical, corruption and fraud allegations. The Audit Committee receives an update at each meeting on all significant investigations as well as data regarding matters raised through our whistleblowing reporting system, with any findings of the external auditors with respect to a particular matter considered as appropriate as part of these discussions. On behalf of the Board, the Committee also considers an annual review of the effectiveness of the whistleblowing system including through benchmarking against peers and monitoring progress against previous years' findings. The Committee Chair's regular reports to the Board include a review of whistleblowing matters of note and all Board members participated in a session with the Vice President – Global Compliance to review compliance investigations and reports for 2020.

The Pearson anti-bribery and corruption (ABC) programme provides the framework to support our compliance with various ABC regulations such as the UK Bribery Act 2010 and the US Foreign Corrupt Practices Act, and the Committee conducts a deep dive into the ABC programme on an annual basis.

In 2020, the Committee heard about enhancements to the investigations policy, playbook and Compliance Council. The Council is designed to reinforce good governance around disciplinary and other remedial measures necessary in response to any large investigative findings. In addition, both COVID-19 and the social justice movement of 2020 impacted the investigations programme. COVID-19 led to challenges in conducting investigations remotely and we saw an increase in reports to HR in respect of COVID-19-related matters. In response to the social justice movement, the Global Compliance Office enhanced SpeakUp efforts with employee resource groups, strengthened our anti-racism stance in our Code of Conduct, and included an 'acts of racism' category in our PearsonEthics.com platform.

External audit

Oversight of external auditors

The Committee reviews and makes recommendations to the Board in respect of the appointment and compensation of the external auditors. These recommendations are made by the Committee after considering the external auditors' performance during the year, reviewing external auditor fees, conducting an effectiveness review, and confirming the independence, objectivity, qualifications and experience of the external auditors.

In conducting its review of the effectiveness of external auditors and making its recommendation to re-appoint PwC for 2021, the Committee had regard to certain factors set out in the FRC's Audit Quality Practice Aid for Audit Committees. In particular, the Committee considered its own observations and interactions with the external auditors, the annual transparency report published by PwC, including in relation to their internal quality control procedures, and the programme of work conducted by the auditors and their reports on that work.

The external auditors' effectiveness review was conducted by distributing a questionnaire to key audit stakeholders, including members of the Audit Committee and key management who interact with the external auditors on a regular basis, including: Chief Financial Officer; Deputy CFO; Vice President – Internal Audit; Vice President – Organisational Risk and Resilience; Vice President – Global Compliance; Senior Vice President – Finance for each business area; and other heads

Audit Committee report

of corporate functions. The process sought views on many aspects of PwC's work and interactions with the company, including the degree to which they demonstrate professional scepticism, integrity and judgement in their work, and their mindset, skills and knowledge. Having reviewed the effectiveness and independence of the external auditors during 2020, as it does every year, the Committee is satisfied that the auditors provide effective independent challenge to management.

The findings of the evaluation, as discussed by the Committee, management and external auditors at the Committee's December 2020 meeting, included:

- overall, responses to the questionnaire were positive, indicating a good-quality, effective and independent external audit process
- the main area identified as presenting an opportunity for possible improvement related to the use of technology in audits. In response to this recommendation, PwC will provide the Committee and management with greater insights into the tools and automation solutions available, although it is recognised by all parties that the feasibility of adopting such solutions has been limited by Pearson's enabling functions transformation programme (known as The Enabling Programme (TEP) G). These insights will be beneficial as the Committee considers the technology capabilities of the participating firms during the tender process in the coming year
- a small number of other minor comments were raised during the review, primarily relating to communication of expectations between the external audit and Pearson teams. PwC and management have committed to work together to follow up on these areas and will report back to the Committee in the first half of 2021

The Committee will continue to review the performance of the external auditors on an annual basis and will consider their independence and objectivity and the quality of the external audit, taking account of all appropriate guidelines.

There are no contractual obligations restricting the Committee's choice of external auditors. The external auditors are required to rotate the audit partner responsible for the Pearson audit every five years and the current lead audit partner, Giles Hannam, rotated onto the Pearson audit at the beginning of 2018.

Audit tendering and rotation

Pearson's last audit tender was in respect of the 1996 year end and resulted in the appointment of Price Waterhouse as auditors. Developments at an EU level regarding mandatory audit rotation for listed companies changed the UK landscape on audit tendering and rotation. EU regulations, which have now been incorporated into UK law, and the 2014 Order by the UK Competition and Markets Authority (CMA) impose mandatory tendering and rotation requirements, with Pearson required to appoint a new auditor no later than for the 2024 financial year end.

In last year's annual report, having taken account of the status of internal business and finance transformation programmes, the Committee announced its intention to proceed with an audit tender during 2020, with a view to changing audit firm for the financial year ending 31 December 2021. However, shortly after the Committee's approval to proceed, the impact of the COVID-19 pandemic and associated guidance from the FRC led the Committee Chair and management to recommend that the tender process be put on hold, a recommendation which the Committee approved.

While the pandemic and associated shifts in ways of working have persisted into 2021, the immediate resulting pressures that were evident in the first half of 2020 have eased and Pearson teams and external audit firms are now accustomed to operating in virtual and remote capacities. At its meeting in February 2021, the Committee therefore revisited the matter of audit tendering and agreed that it was appropriate to recommence the audit tender process by issuing a Request for Proposal (RFP) in March 2021, with a view to changing audit firm for the financial year ending 31 December 2022. The Committee is confident that the process will be run in a fair, open and transparent manner, notwithstanding that it will be wholly or primarily conducted through virtual and remote means.

In making this decision, the Committee recalled its rationale from the previous year, noting that finance and management teams believe they have the capacity to support a tender and change in auditor, leveraging changes from the finance transformation programme. Although elements of the finance transformation are yet to be implemented in certain international markets, the majority of Group audit scope sits within North America and the UK and it is felt manageable by the Committee, management and the finance function to onboard a new auditor at a time of change in those smaller International markets.

In considering the relaunch of the tender process, the Committee noted that the Committee Chair had liaised with the internal working group during 2020 and early 2021 to keep abreast of matters pertaining to the paused tender process. In making its decision, the Committee has had regard to the detailed timeline, governance framework (including confirmation of the working group that will lead the process), independence considerations, scoring and selection criteria and the degree of involvement by all Committee members in the various stages of the process. The Committee has determined, with the agreement of management, that the proposed new timeline achieves an appropriate balance between business priorities and internal capacity while also allowing a rigorous and comprehensive audit tender process.

Following the upcoming audit tender, Pearson will adopt a policy of putting the audit contract out to tender at least every 10 years, as required. The Committee will continue to pay close attention to developments in the audit landscape, including the BEIS consultation on reforms to the audit sector, and will take these into account as and when appropriate.

Compliance with the CMA Order

Pearson confirms that it was in compliance with the provisions of The Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014 during the financial year ended 31 December 2020.

Review of the external audit

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

At its July 2020 meeting, the Committee discussed and approved the external audit plan and reviewed the key risks of misstatement of Pearson's financial statements. The external auditors provided an update at the December 2020 Committee meeting, having concluded that their analysis of significant and elevated risks remained the same.

The table on p96 sets out the significant issues considered by the Committee together with details of how these items have been addressed. The Committee discussed these issues with the auditors at the time of their review of the half-year interim financial statements in July 2020 and again at the conclusion of their audit of the financial statements for the full year in February 2021.

All the significant issues were also areas of focus for the auditors. Learn more in the Independent auditor's report on p128

In December 2020, the Committee discussed with the auditors the status of their work, focusing in particular on internal controls and Sarbanes-Oxley testing.

As the auditors concluded their audit, they explained to the Committee:

- The work they had conducted over revenue, including over contracts in certain of the Group's businesses in the US and UK that span year-end, where revenue is recognised using estimated percentage of completion based on costs and judgements in relation to provisions for returns
- Their work in evaluating management's goodwill impairment exercise, on a value-in-use basis, including assessing assumptions around cash-generating unit (CGU) identification, operating cash flow forecasts, perpetuity growth rates and discount rates
- The impact of COVID-19 on the key accounting judgements and the measures which they had taken to complete their audit remotely in light of pandemic-related restrictions
- The work performed over the nature and presentation of non-trading items, focusing on subjective judgements and the transparency with which related adjusted measures are presented
- The work they had done to audit the provisioning levels in respect of potential tax exposures and uncertain tax positions and related disclosures and the work performed over deferred tax asset recoverability
- Their evaluation of the recoverability of investments in digital platforms and pre-publication assets
- The results of their controls testing for Sarbanes-Oxley Act section 404 reporting purposes and in support of their financial statements audit
- The results of their work over the company's going concern and viability statement reports
- Their work in relation to other matters which are not classified as key audit matters, but may give rise to additional disclosure requirements e.g. pensions
- The work performed over the carrying value of investments in subsidiaries for the Pearson plc parent company

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

Auditors' independence

In line with best practice, our relationship with PwC is governed by our policy on external auditors, which is reviewed and approved at least annually by the Audit Committee. The policy establishes procedures to ensure that the auditors' independence is not compromised, as well as defining those non-audit services that PwC may or may not provide to Pearson. Any allowable services are in accordance with relevant UK and US legislation and auditor standards. The policy takes into account certain voluntary commitments by PwC regarding independence and applies to all Pearson businesses globally, including associate companies.

The Audit Committee approves all audit and non-audit services provided by PwC. Our policy on the use of the external auditors for non-audit services reflects the restriction on the use of pre-approval in the 2016 FRC Guidance on Audit Committees and, accordingly, all non-audit services, irrespective of value, are required to be approved by the Audit Committee. In particular, we expressly prohibit the provision of certain tax, HR and other services by the external auditor. We review non-audit services on a case-by-case basis, including reviewing the ongoing effectiveness and appropriateness of our policy. In 2020, our policy was further updated to comply with the FRC's Revised Ethical Standard published in December 2019. The standard applies restrictions on certain non-audit services and applies a cap on the level of permitted non-audit services fees which can be billed in any year.

The Audit Committee receives regular reports summarising the amount of fees paid to the auditors. During 2020, Pearson spent £0.2m more on non-audit fees with PwC compared with 2019, due to an increase in fees associated with the audit of efficacy reporting. For 2020, non-audit fees represented 8% of external audit fees (6% in 2019).

For all non-audit work in 2020, PwC was selected only after consideration that it was best able to provide the services we required at a reasonable fee and within the terms of our policy on external auditors. Where PwC is selected to provide audit-related services, we take into account its existing knowledge and experience of Pearson. Where appropriate, services were tendered prior to a decision being made as to whether to award work to the auditors.

Significant non-audit work performed by PwC during 2020 included:

- audit of Pearson's efficacy programme
- provision of comfort letters for potential bond issues and certain US regulatory filings
- half-year review of interim financial statements

A full statement of the fees for audit and non-audit services is provided in note 4 to the financial statements on p158

Tim Score
Chair of Audit Committee

Audit Committee report

Significant issues considered by the Audit Committee

Issue	Action taken by Audit Committee	Outcome
→ Impairment reviews		
Pearson carries significant goodwill and other intangible asset balances. There are significant estimates and assumptions used in the impairment review. COVID-19 has impacted key assumptions in the impairment review. Pearson has made significant impairments to goodwill across a variety of its businesses in recent years.	The Committee monitored the Group's plans and forecasts during the year to determine if there were impairment triggers. The Committee considered the results of the Group's goodwill impairment reviews which were undertaken in June and December. Key assumptions – including cash flows derived from strategic and operating plans, long-term growth rates and the weighted average cost of capital – were reviewed and challenged, particularly in light of the impact of COVID-19. The Committee considered the sensitivities to changes in assumptions and the adequacy of disclosures required by IAS 36 'Impairment of Assets' in relation to the Group's CGUs, noting that certain CGUs still remain sensitive to assumption changes after a number of impairments in recent years.	Annual impairment review finalised with confirmation of sufficient headroom in each of the CGUs.
→ Sales returns		
The determination of appropriate provisions for sales returns requires a significant amount of judgement and, in the light of recent volatility in returns in the US Higher Education Courseware business, the Committee continued to review returns data and our policy on providing for returns.	The Committee considered returns provisioning for the US Higher Education Courseware business and reviewed the methodology for establishing provisions. The Committee were particularly interested to understand the impact of the new digital-first strategy in North America on estimates associated with returns and stock obsolescence.	Assumptions underlying the returns reserve methodology were reviewed and challenged. The Committee was satisfied that the level of provisions held for sales returns is adequate.
→ Going concern and viability		
The assessment of the Group's viability and the appropriateness of the going concern assumption.	The Committee reviewed future budgets and cash flow forecasts to understand the Group's available liquidity and ability to continue as a going concern. The Committee reviewed and challenged the risks identified to the forecasts. The Committee reviewed the outcome of the severe but plausible scenario modelling and stress testing. The Committee specifically considered the impact of COVID-19 on the budgets, cash flow forecasts and risks. The Committee reviewed actions to protect the Group's liquidity position, including the pausing of the share buyback programme and the issuance of a bond.	The Committee reviewed and challenged future forecasts and the risks to those forecasts. The Committee was satisfied with the stress testing performed and the severe but plausible scenario modelling. The Committee noted that in all scenarios the Group had a high level of liquidity headroom and sufficient headroom against covenant requirements. The Committee was satisfied with the actions the Group has taken to protect liquidity. The Committee is satisfied with the assessment of the Group's viability and is satisfied that the Group is a going concern. The Committee is satisfied with the disclosures related to going concern and viability.

Issue	Action taken by Audit Committee	Outcome
→ Impact of COVID-19		
COVID-19 has impacted the operations and trading performance of the Group. The Group assessed the impact of COVID-19 on specific areas of the balance sheet including: › Working capital and pre-publication assets › Property and leases › Acquisition intangibles › Pension assets The Group assessed the impact of COVID-19 on liquidity and the going concern assessment.	The Committee considered the impact of COVID-19 on key areas of judgement in the balance sheet. In particular the Committee were interested in the impact of COVID-19 on the assessment of accounting estimates related to expected credit losses, inventory obsolescence, sales returns and the recoverability of pre-publication assets. The Committee reviewed future budgets and cash flow forecasts to understand the impact of COVID-19 on the Group's available liquidity and ability to continue as a going concern. The Committee reviewed actions to protect the Group's liquidity position including the pausing of the share buyback programme and the issuance of a bond. The Committee considered the adequacy of disclosures related to COVID-19. The Committee also considered the impact of COVID-19 on ways of working, including the ability of employees to operate key financial controls and timelines related to external financial reporting.	The Committee was satisfied that the impact of COVID-19 has been appropriately reflected on the balance sheet. They noted that the impact of COVID-19 has not been significant in the majority of areas. The Committee was satisfied with the actions the Group has taken to protect liquidity. The Committee is satisfied that the impacts of COVID-19 have been adequately disclosed and that any difficulties related to new ways of working have been adequately addressed. The Committee approved an extension to the year end external reporting timetable in light of the impacts of COVID-19 on ways of working.
→ Tax		
The impact of tax legislation changes including US tax reform, EU state aid, proposed digital services tax, the trend for increased tax transparency, and provision levels.	The Committee considered various developments during the year, including Pearson's ongoing response to the European Commission's decision that the UK's Finance Company Partial Exemption rules constituted state aid, OECD developments in proposals to tackle the challenges arising from the digitalised economy, an internal refinancing of the Group's US operations and updates on global tax authority audit activity including Brazil. The Committee considered an update on Pearson's tax reporting agenda, including ongoing involvement endorsing the B-Team Responsible Tax Principles and the publication of Pearson's fourth Annual Tax Report.	The Committee was satisfied with Pearson's approach to managing the impact of tax legislation changes and agreed with the views of management regarding tax provisioning levels.

Risk governance and control

Control environment

The Board has overall responsibility for Pearson's systems of internal control and risk management, which are designed to manage, and where possible mitigate, the risks facing Pearson, safeguard assets and provide reasonable, but not absolute, assurance against material financial misstatement or loss. The Board agrees risk management requirements and, in assessing the effectiveness of the risk management effort, reviews a range of inputs as described elsewhere in this report. The Board can and does challenge the reporting it receives and will request further information as needed to make its assessment.

The Board confirms that it has conducted and continues throughout the year to review the effectiveness of Pearson's systems of risk management and internal control in accordance with provision 29 of the Code and the FRC Guidance on Risk Management, Internal Control and Related Financial and Business Reporting (FRC Guidance). The Board confirms these systems operated satisfactorily throughout the year and to the date of this report, and no significant failings or weaknesses were identified in the review process.

The Board has delegated responsibility for monitoring the effectiveness of the company's risk management and internal control systems to the Audit Committee. The Audit Committee oversees a risk-based internal audit programme, including periodic audits of the risk processes across the organisation. It provides assurance on the management of risk (including risk deep dives, as described on p92), and receives reports on the efficiency and effectiveness of internal controls. You can read more about Pearson's internal audit function on p93. Each business area maintains internal controls and procedures appropriate to its structure, business environment and risk assessment, while complying with company-wide policies, standards and guidelines. These controls and procedures are monitored and certified through the Group-wide Controls Centre of Excellence.

Internal control and risk management

Our internal controls and risk oversight are monitored and continually improved to ensure their compliance with FRC Guidance.

The Board is ultimately accountable for effective risk management in Pearson and determines our strategic approach to risk. It confirms our organisational risk management framework as well as our risk appetite targets. Twice yearly it receives and reviews reports on the status of the top Group-wide risks. It is supported in the following ways:

› the Audit Committee is responsible for overseeing internal controls within Pearson which includes determining the risk appetite (recommended by Pearson Executive Management team), reviewing and commenting upon key risks, and ensuring that risk management is effective

› Pearson's Executive and leadership teams are responsible for identifying and mitigating principal risks

› leaders and managers at all levels in Pearson are responsible for managing risk in their area of responsibility, including the identification, assessment and treatment of risk

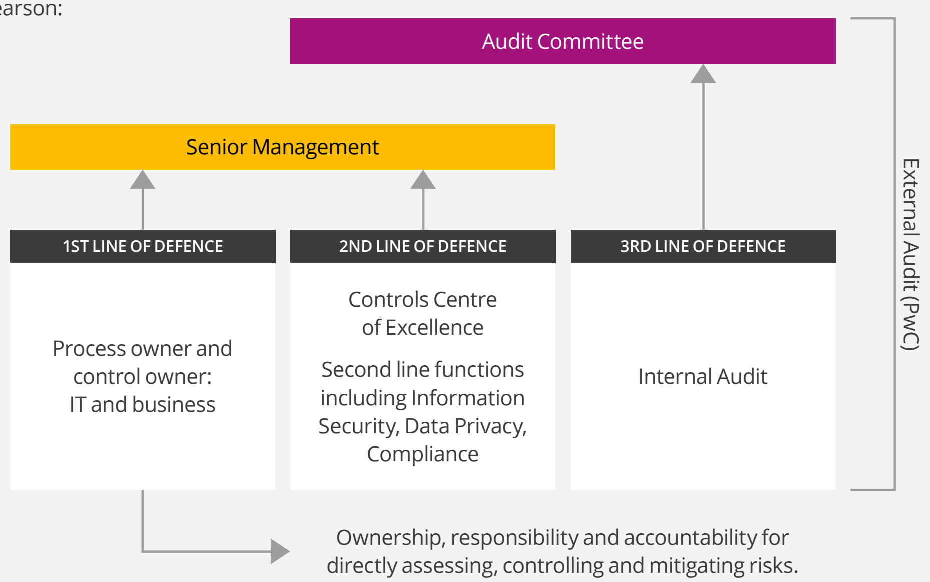
› the Organisational Risk and Resilience team owns the overall risk management framework for the company and facilitates consolidated reporting on risk

› the internal audit team provides independent assurance on the adequacy of the risk management arrangements in place. The internal audit plan is aligned to identified Pearson-wide risks and it presents issues and risks arising from internal audits at each Audit Committee meeting

The involvement of the Board and Audit Committee in the design, implementation, identification, monitoring and review of risks (including setting risk appetite and reviewing how risk is being embedded in our culture) is outlined in more detail in the organisational risk management section on p56

LINES OF DEFENCE

The below diagram shows the lines of defence within Pearson:



Financial management and reporting

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

There is an ongoing process to monitor the risks and effectiveness of controls in relation to the financial reporting and consolidation process, including the related information systems. This includes up-to-date Pearson financial policies, formal requirements for finance to certify that they have been in compliance with policies and that the control environment has been maintained throughout the year, consolidation reviews and analysis of material variances, finance technical reviews, and review and sign-off by senior finance managers. The Group finance function also monitors and assesses these processes and controls through finance and technology compliance functions and a Controls Steering Committee comprising cross-functional experts.

These controls include those over external financial reporting which are documented and tested in accordance with the applicable regulatory requirements, including section 404 of the Sarbanes-Oxley Act, which is relevant to our US listing. One key control in this area is the Verification Committee, which submits reports to the Audit Committee. This Committee is chaired by the Company Secretary, and members include the Chief Financial Officer and her deputy, the Deputy Chief Legal Officer, Vice President – Internal Audit and Senior Vice President – Investor Relations as well as senior members of financial management. The primary responsibility of this Committee is to review Pearson's public reporting and disclosures to ensure that information provided to shareholders is complete, accurate and compliant with all applicable legislation and listing regulations. In addition, our separate Market Disclosure Committee is responsible for considering potential inside information and its treatment in accordance with the Market Abuse Regulation.

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

Treasury management

The treasury department operates within policies approved by the Audit Committee on behalf of the Board, and treasury transactions and procedures are subject to regular internal audit. Major transactions are authorised outside the department at the requisite level, and there is an appropriate segregation of duties. Frequent reports are made to the Deputy Chief Financial Officer and Chief Financial Officer. Regular reports are prepared for the Audit Committee and an annual risk review meeting takes place between the Treasurer and Audit Committee. The Treasury Policy is described in more detail in note 19 to the financial statements on p176

Insurance

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

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

Tax

The Board has delegated responsibility for the integrity of financial reporting and risk management to the Audit Committee. This includes setting tax strategy and monitoring tax risk. The Tax Department reports at least annually to the Audit Committee. Regular updates are provided to the Deputy CFO and the CFO throughout the year.

Directors' remuneration report

Committee Chair
Elizabeth Corley

Members as at 31 December 2020
Elizabeth Corley, Sherry Coutu, Tim Score and Sidney Taurel

Key messages from the Remuneration Committee

- Despite financial performance in line with revised expectations, the 2020 incentive outcomes for Executive Directors reflect the unforeseen impact of COVID-19 on the business.
- To secure the appointment of our new Chief Executive, Andy Bird, the Committee developed a remuneration package taking into account the global market in which Pearson competes for talent.
- The Committee reviewed incentive arrangements for our senior management below Board level, with the aim of strengthening support for the delivery of our strategic objectives, while promoting pay for performance and aligning incentives across the organisation.
- There will be a 1.5% salary increase for the Chief Financial Officer in 2021, in line with the wider UK workforce. The salary for the Chief Executive is fixed until 2023.
- The Committee remains focused on ensuring the remuneration arrangements in place for the broader employee population are consistent with the need to attract and retain the right talent for a digital future.

Terms of reference

The Committee's terms of reference are in line with the 2018 UK Corporate Governance Code and are available on the Governance page of the company's website at plc.pearson.com/en-GB/company/business-operations. (A summary of the Committee's responsibilities is shown on p120)

Board Committee attendance

The following table shows attendance by Directors at Committee meetings throughout 2020:

	Remuneration Committee Attendance
Elizabeth Corley	7/7
Sherry Coutu	7/7
Josh Lewis[1]	3/3
Tim Score	7/7
Sidney Taurel	7/7
Andy Bird[2]	1/3

1 Josh Lewis retired from the Pearson Board on 24 April 2020.
2 Andy Bird joined the Committee on 1 May 2020. He stepped down from this role on 18 October 2020 following his appointment as Chief Executive Officer. Andy Bird was not present at any Remuneration Committee meeting where his remuneration was discussed.

Dear shareholders

The last year has been one of substantial change. As for many companies, the global COVID-19 pandemic presented new and unprecedented challenges for Pearson. Additionally, Pearson has seen change to our Executive Directors including, after an extensive global search in a highly competitive marketplace, the appointment our new Chief Executive, Andy Bird, in October 2020.

In what has been a particularly challenging year from an operational and financial perspective, Pearson delivered sales and adjusted operating profit performance in line with revised expectations, with continued growth in online learning.

During 2020, despite the impact of COVID-19, Pearson maintained its dividend and did not access government funding or take advantage of the furloughing programme.

In line with Pearson's values, Pearson's response to COVID-19 focused on supporting our employees, customers, partners and broader stakeholders during the pandemic. In particular, with regard to our employees, protecting their health, safety and wellbeing was a key priority. Accelerated by the pandemic, Pearson reviewed and updated a number of our workforce policies, to ensure these best support our operational needs whilst promoting a healthy work-life balance for our employees, including but not limited to flexible working policies and extending the global reach of our Employee Assistance Programme.

Recognising the impact of the pandemic on the broader communities which we not only work, but also live and learn in, the Chair of the Board, the Non-Executive Directors and Executive Directors voluntarily took a temporary three-month reduction in salary/fees, which was donated to charities to help support these local communities.

In addition, the Committee exercised its discretion when granting the 2020 Long-Term Incentive Plan (LTIP) award to Executive Directors, recognising the recent share price volatility. As a result, a reduced number of shares were granted to the Chief Financial Officer, Sally Johnson, helping to protect against any windfall gains on vesting. No other Executive Director was eligible to participate in the 2020 LTIP.

Appointment of new Chief Executive

On 24 August 2020, Pearson announced that Andy Bird would be appointed as its new Chief Executive and Executive Director from 19 October 2020. Andy has a rare track record as a proven leader of a large, complex and diverse business, and a wealth of experience driving digital change in a disrupted consumer content business, while creating shareholder value. This positions him very well to build on the foundations that have been laid over the last few years and lead Pearson as it becomes a digital-first consumer-focused lifelong learning company. The Committee looks forward to working with Andy Bird in driving the business forward to enhance value for all stakeholders.

In order to secure such an exceptional candidate, the Committee developed a one-off bespoke remuneration package for recommendation to the Board. In doing so we sought to maintain our existing shareholder approved Directors' Remuneration Policy for future years while finding a means to bridge the considerable gap in compensation practice between the UK and the US, Andy's home market, where both amounts and structures are quite different. The Committee developed a one-off arrangement, the co-investment award, to help bridge this gap. This solution was enabled by Andy Bird's decision to invest personally and substantially in Pearson shares. The Committee recognises that such a one-off arrangement is not typical in the UK market, but believe it was the optimal structure to secure Andy Bird's recruitment whilst incentivising the creation of long-term shareholder value and keeping our forward-looking policy unchanged.

All other elements of Andy Bird's remuneration package are in line with our approved Directors' Remuneration Policy, which is aligned with UK market practice and key governance principles.

Whilst within policy, the Committee recognises that this package represents an uplift over his predecessor. When setting the package, the Committee considered, as is typical practice, Andy Bird's proven skills and experience, the remuneration he received in his prior role and compensation levels for Chief Executive roles at comparable companies (including both FTSE-listed companies and global sector comparators). After careful evaluation, the Committee determined that such a package was appropriate, balancing these various reference points. While the Committee was mindful of internal relativities, it believed that securing such an exceptional candidate as Andy Bird was fundamental to Pearson's future success.

- Andy Bird will receive a salary of $1,250,000 per annum, which is fixed until at least 2023
- His pension contribution is set at 16% of base salary, our new hire rate for Executive Directors as set out in our approved policy, and is aligned with the pension provision that UK employees of a similar age are eligible to receive
- He will be eligible to participate in both the Annual Incentive Plan (AIP) and LTIP from 2021. The maximum AIP opportunity will be 200% of base salary and the LTIP award will have a maximum face value of 300% of base salary
- Pearson will also provide a contribution towards accommodation costs in New York so that Andy has a base close to Pearson's operations on the East Coast

Further information on these arrangements can be found on p110

Participation in the co-investment arrangement required Andy Bird to purchase and hold Pearson shares at an aggregate cost to him of 300% of base salary ($3.75 million), demonstrating his commitment to his role, creating immediate alignment with shareholders and fulfilling from the outset our shareholding guideline.

In consideration for this investment, Andy was granted a co-investment award equal to 750% of base salary, which will vest in three equal tranches as soon as practicable following 31 December 2021, 31 December 2022 and 31 December 2023. Vesting is subject to performance underpins, to ensure the Committee can reduce vesting if in its opinion performance of the business or the individual does not support this, and continued employment. Shares that vest will be subject to a holding period until 31 December 2023. Further information on the co-investment award, can be found on p111

Shareholder engagement

The co-investment award was not envisaged within our approved Directors' Remuneration Policy, and therefore, prior to Andy's appointment, we sought shareholder approval. In advance of this, and in developing the remuneration package, the Committee engaged extensively with shareholders. The Board very much appreciated the support received by the majority of shareholders for the resolution at our General Meeting in September 2020, although we noted that a significant minority voted against the proposals.

In light of this outcome, given the Committee's commitment to an ongoing and transparent dialogue with our shareholders, we undertook an engagement exercise in early 2021 in order to listen and further understand the views and perspectives of our shareholders.

Shareholders remained supportive of Andy Bird's appointment, recognising the one-off nature of the co-investment award as a bridge between UK and US practice, appreciated our determination to keep our approved Directors' Remuneration Policy otherwise unchanged, and noted that there had been no buy-out of remuneration forgone at a previous employer.

The two main areas of concern raised by investors related to the time horizon over which the co-investment award is required to be held, specifically that this is a shorter time horizon than the five years specified in the UK Corporate Governance Code; and the performance underpins.

In terms of the time horizon, the co-investment arrangement is structured to incentivise the transformation of the business and growth in the near-term. The Committee therefore considered it appropriate that the phased vesting schedule and holding period to three years reflect the period over which we expect Andy Bird to deliver, as well as the fact that he has invested a significant amount of his own funds into Pearson shares. Further, under our Directors' Remuneration Policy, he is required to build a shareholding equal to the value of 300% of salary. This must be maintained for a period of two years post-employment. This ensures continued alignment to shareholder interests and incentivises the delivery of long-term sustainable value.

On the performance underpins, during the second half of 2020, the Committee spent time considering how these will be assessed. In addition to consideration of the specific underpins, it is the Committee's intention that, prior to the vesting of each tranche of the co-investment award, a holistic review of performance is undertaken, including consideration of the experience of all stakeholders, such as learners, employees, customers and shareholders, as well as the effectiveness of risk management and internal controls. Further details on this assessment process can be found on p112

I would personally like to thank all those who engaged with us during this process. The support of our shareholders enabled Pearson to appoint a new Chief Executive who we believe will unlock new growth potential for the company and ultimately return value to all our stakeholders.

Summary of other leadership changes

John Fallon stepped down from the role of Chief Executive on 18 October 2020. He remained employed by Pearson until 31 December 2020, acting as an adviser and facilitating a smooth transition. There was no payment for loss of office and, in respect of his outstanding AIP and LTIP awards, the Committee determined that John would be treated as a 'good leaver'. Further details of remuneration arrangements in respect of John's retirement can be found on p116

During the year, Pearson also saw a change in its Chief Financial Officer. On 24 April 2020, Sally Johnson was appointed to the role of Chief Financial Officer and Executive Director, replacing Coram Williams.

Directors' remuneration report

Sally's remuneration arrangements, which are in line with our Directors' Remuneration Policy, were disclosed in last year's Directors' Remuneration Report and further details are provided on p113. Coram Williams received no payment for loss of office. He was not eligible for an AIP or LTIP in respect of 2020 and he forfeited any unvested LTIP awards on departure.

In line with its Terms of Reference, the Committee has also approved remuneration arrangements for a number of new appointments to the Pearson Executive team.

Executive remuneration framework and alignment to strategy

The Committee was pleased to receive the support of 95% of our shareholders for our Directors' Remuneration Policy at the 2020 AGM. Our Directors' Remuneration Policy is intended to support Pearson in achieving its purpose while driving long-term sustainable value for shareholders. It also reflects the provisions of the UK Corporate Governance Code and evolving market practice.

Following his appointment, Andy has reviewed and revised our forward-looking strategy. While the Committee continues to believe the current Directors' Remuneration Policy and its implementation appropriately incentivises the delivery of the new strategy, it will keep this under review over the coming year, engaging with shareholders on key areas of focus.

Pearson has a clear purpose – to help people make progress in their lives through learning. Our strategy and priorities are anchored around this purpose, which is embedded in the actions and behaviours of our leaders. In that context, a focus on building an inclusive culture, increasing diverse representation within our workforce, accelerating our sustainability strategy and investing in our own people's learning are all key strategic priorities. Therefore, for 2021, we have incorporated clear metrics in relation to these priorities within our AIP framework, further strengthening the relationship between our purpose and our executive remuneration arrangements. The Committee will keep this approach, including the weighting of these metrics, under review.

Incentive outcomes for 2020

As noted, sales and adjusted operating profit performance were in line with revised expectations but performance during 2020 was significantly affected by the COVID-19 pandemic. This is reflected in incentive outcomes for Executive Directors, targets for which were set at the start of the financial year.

Only John Fallon and Sally Johnson were eligible to participate in the AIP in respect of financial year 2020. Despite the strategic progress made during the year, Pearson did not meet the financial targets, which were set prior to the onset of COVID-19. As a result, there will be no payment under the AIP to Executive Directors.

Annual incentive awards will however be made to the wider employee population recognising their contribution during the year.

The LTIP award granted in 2018 is due to vest this year based on performance to 31 December 2020 against stretching earnings per share (EPS), return on invested capital (ROIC) and relative total shareholder returns (TSR) targets. Performance targets were not met in respect of this award and therefore this award will lapse in full.

The Remuneration Committee did not exercise any discretion in respect of these outcomes.

Looking forward to 2021 – senior management

Following Andy's appointment, the Committee reviewed the structure of incentives for 2021 for senior management below Board level, including the broader Pearson Executive team, with the aim of creating incentives that better support the delivery of Pearson's corporate objectives while strengthening the link between pay and performance. As a result, the previous single incentive plan operated for this population will be replaced with a more typical annual bonus plus long-term incentive structure. The long-term incentive will comprise both performance shares and restricted shares, recognising the markets in which we compete for talent. Overall, the Committee considers that this change in incentive structure promotes and encourages pay for performance whilst providing greater alignment with our approach to pay across Pearson.

Looking forward to 2021 – Executive Directors

The Committee reviewed the salary of Sally Johnson and approved an increase of 1.5% for 2021. This is in line with the salary increase awarded to the wider workforce in the UK. Andy Bird's salary remains fixed until 2023.

The AIP for 2021 will continue to be based on a balanced mix of financial and strategic measures, in line with prior years. For the 2021 LTIP, at the time of writing, the Committee had not yet finalised setting performance targets but these will be provided on our website prior to the AGM. When setting targets, the Committee follows a robust process, taking into account Pearson's strategic plan, as well as external expectations. Targets set will be stretching in this context.

The Committee continues to engage in conversations with shareholders. The conversations that we have had over the last year have been invaluable and we thank shareholders for the time they have spent with us. We look forward to receiving your support at the AGM in relation to our remuneration report.

Elizabeth Corley
Chair of Remuneration Committee

15 March 2021

Executive remuneration framework and implementation for 2021

Pearson has a set of remuneration principles that govern pay for the whole organisation. Remuneration arrangements for our Executive Directors have been developed with these principles in mind.

Remuneration principles that apply across the whole organisation

1 Aligned to longer-term strategy	2 Pay for performance	3 Market competitive	4 Targeted differentiation	5 Tailored	6 One part of the employee value proposition
Reward will be linked to achieving Pearson's longer-term strategy, growth and sustainability	Remuneration framework and outcomes are aligned with performance	Pay levels will be market competitive, based on role, grade and contribution to ensure individuals are fairly rewarded in line with the market	There will be targeted differentiation of reward across our employees linked to talent and performance management	The approach to reward may be tailored in certain circumstances to address a specific market/business need but will be designed in a way that is consistent with our underlying reward philosophy	Remuneration is one part of our broader employee value proposition and not the only reason to work for Pearson

Our Directors' Remuneration Policy and its implementation supports our purpose of helping people make progress in their lives through learning, our strategy and ultimately the delivery of long-term sustainable value for all stakeholders, including our shareholders.

In developing the forward-looking Directors' Remuneration Policy, the Committee had due regard to the UK Corporate Governance Code, wider workforce remuneration and emerging best practice in relation to Executive Director remuneration.

- Pearson's remuneration principles, as set out above, were developed to ensure **alignment to company culture** and position Pearson as an employer of choice, with an ability to attract and retain the right talent to support the company's digital future, whilst recognising that remuneration is one part of the broader employee value proposition at Pearson.
- Our ongoing executive remuneration framework is designed to be **simple**, with total remuneration made up of fixed and performance- linked elements supporting different strategic objectives
- Our remuneration framework and outcomes are designed to be **aligned with performance** achieved:
  - Performance measures selected for the AIP and LTIP are key to achieving strategic objectives. The Committee reviews performance measures on an annual basis to ensure they continue to incentivise the right management behaviours and goals
  - We carry out a robust target-setting process each year, taking into account Pearson's strategic plan, as well as analyst consensus to reflect market expectations, resulting in stretching yet achievable targets for the AIP and LTIP
  - Maximum awards under the AIP and LTIP are capped and clearly disclosed in our Policy
  - When determining payouts, the Committee discusses if the outcome is reflective of overall company performance and the experience of stakeholders, including shareholders and employees, over the period and, if not, has discretion to adjust outcomes.
- The Committee is **mindful of reputational and other risks** when implementing the forward-looking Directors' Remuneration Policy and determining outcomes for Executive Directors and senior management. The company also has safeguards in place, such as malus and clawback provisions and a two-year holding period on the LTIP, as well as robust shareholding guidelines which extend post-employment and were further strengthened last year
- Before signing off the annual remuneration report, the Committee reviews drafts and provides input to **clarify** our disclosures. Where material changes are proposed to the operation of our Directors' Remuneration Policy, we would normally consult with key shareholders to ensure the rationale for such changes is fully understood and provide the opportunity for shareholders to feed into the decision-making process and inform our final conclusions

Executive remuneration framework and implementation for 2021

Summary of our forward-looking Directors' Remuneration Policy

The table below provides a summary of our forward-looking Directors' Remuneration Policy and its implementation for 2021. This does not include the co-investment award granted to Andy Bird on his appointment as this was a one-off arrangement and does not form part of our forward-looking executive remuneration framework. The full Directors' Remuneration Policy is available on the Governance page of the company's website at plc.pearson.com/en-GB/company/business-operations.

B Base salary

Key features

› Base salaries are set to provide the appropriate rate of remuneration for the job, taking into account relevant recruitment markets, business sectors and geographic regions

› Base salaries are normally reviewed annually, with any increases normally in line with typical increases awarded to other employees in the Group

› Salary reviews take into account: general economic and market conditions; the level of increases made across the company as a whole; particular circumstances such as changes in role, responsibilities or organisation; the remuneration and level of increases for executives in similar positions in comparable companies in both the UK, US and internationally; and individual performance

2021 implementation

› Andy Bird – $1,250,000 (no change)

› Sally Johnson – £522,725 (1.5% increase)

Andy Bird's first salary review will occur in 2023.

When reviewing Sally Johnson's base salary, the Committee took into account the level of increases made across the company as a whole, business and individual performance, and general economic and market conditions. The increase awarded to Ms Johnson is in line with the general increase across the UK.

A&B Allowances and benefits

Key features

› Allowances and benefits which reflect the local competitive market and may include travel-related benefits, health-related benefits, risk benefits and any other benefits provided to the majority of employees. The Committee may introduce other benefits if it is considered appropriate to do so

› The cost of the provision of allowances and benefits varies from year to year depending on cost to Pearson

2021 implementation

No changes for 2021. Executive Directors will continue to receive travel, health and risk-related benefits. Andy Bird will also receive a contribution towards accommodation costs.

R Retirement benefits

Key features

› Employees in the UK, including Executive Directors, are eligible to join the Money Purchase 2003 section of the Pearson Pension Plan. Executive Directors are eligible to join this plan or receive a cash allowance of equivalent value

› The Committee has discretion to put in place retirement benefit arrangements in line with local market practice. The Committee may also honour all pre-existing retirement benefit obligations, commitments or other entitlements that were entered into by a member of the Pearson Group before that person became a Director, such as participation in the Final Pay section of the Pearson Pension Plan

› Executive Directors, who opt out of the pension, can receive a cash allowance of up to 16% of base salary, in line with the maximum company contribution as a percentage of salary that UK employees of a similar age are eligible to receive

2021 implementation

Sally Johnson is an existing member of the Final Pay section of the Pearson Pension Plan. Her pension accrual rate is 1/60th of pensionable salary per annum, restricted to the Plan earnings cap.

Andy Bird is not a member of a pension scheme operated by Pearson. Instead, he receives a payment of 16% of base salary in lieu of pension. This is in line our new hire rate for Executive Directors, as set out in our approved policy, and is aligned with the pension provision that UK employees of a similar age are eligible to receive.

AIP Annual incentive plan

Key features

- Motivates towards the achievement of annual business goals and strategic objectives and provides a focus on key financial and non-financial metrics, with financial metrics accounting for at least 75% of the total annual opportunity
- The Committee sets performance measures and their relative weightings annually to ensure continuing alignment with strategy and that targets are sufficiently stretching
- The Committee has discretion to adjust payments if it believes that the formulaic outcome does not reflect underlying financial or non-financial performance or if such other exceptional factors warrant doing so
- Malus and clawback provisions apply

2021 implementation

Maximum opportunity for 2021:

- 200% of base salary for the Chief Executive
- 170% of base salary for the Chief Financial Officer

50% of the maximum opportunity payable for on-target levels of performance.

For 2021, the following balanced mix of financial and strategic measures will be used, which is unchanged from the previous year:

Adjusted operating profit	Sales	Operating cash flow	Strategic measures
30%	30%	20%	20%

Strategic measures for 2021 will focus on:

- Making Pearson fit for the future and investing in our talent
- Digital growth, consumer engagement and product effectiveness
- Building an inclusive culture, increasing diverse representation and accelerating our sustainability strategy

As in previous years, a financial underpin will apply in respect of the strategic measures. Targets will be disclosed in full retrospectively following the end of the performance period.

LTIP Long-Term Incentive Plan

Key Features

- Drive long-term profitability, share price growth and value creation whilst aligning the interests of Executives and shareholders
- Awards are made annually, and vest on a sliding scale based on performance against stretching corporate performance targets measured at the end of the three-year performance period
- Awards are subject to a post-vesting holding period of two years following the end of the performance period
- The Committee is guided by the principle of aligning shareholder and management interests and therefore reserves the right to adjust pay-outs before they are released if it believes that the vesting outcome does not reflect underlying performance or if other exceptional factors warrant doing so
- Malus and clawback provisions apply

2021 implementation

Maximum opportunity for 2021:

- 300% of base salary for the Chief Executive
- 245% of base salary for the Chief Financial Officer

Performance will be measured over three years, with any shares vesting subject to an additional two-year holding period.

Given the recent announcement of the company's refreshed strategy, at the time of writing, the Committee had not yet finalised performance targets for the 2021 LTIP grant. The targets will be made available on the website before the AGM and will be disclosed in the Regulatory News Service (RNS) announcement at the time of grant, which is expected to be in May as normal. The Committee remains committed to timely disclosure of targets once they have been confirmed.

SG Shareholding guidelines

Key Features

- Align the interests of Executives and shareholders and encourage long-term shareholding and commitment to the company
- Executive Directors are expected to build up a substantial shareholding in the company within five years from their date of appointment to the Board. The current requirement is 300% of salary for the Chief Executive and 200% of salary for other Executive Directors
- Executive Directors are expected to retain their shareholding guideline (or actual holding if lower) for two years following stepping down as an Executive Director

2021 implementation

No changes for 2021.

Executive remuneration framework and implementation for 2021

CNF Chair and NED Fees

Key Features

- To attract and retain high-calibre individuals, with appropriate or industry-relevant skills, by offering market competitive fee levels
- The Chair is paid a single fee for all responsibilities
- The Non-Executive Directors are paid a basic fee, with Committee Chairs, members of the main Board Committees and the Senior Independent Director paid an additional fee to reflect their extra responsibilities
- The Chair and Non-Executive Directors receive no other pay or benefits, except for reimbursement of expenses, and do not participate in incentive plans
- A minimum of 25% of the Chair's and Non-Executive Directors' basic fee are paid in shares

2021 implementation

No changes for 2021.

Role	Fees for 2021
Chair of the Board	£500,000
Base fee for Non-Executive Directors	£70,000
Senior Independent Director fee	£22,000

Role	Chair	Member
Audit Committee	£27,500	£15,000
Remuneration Committee	£22,000	£10,000
Nomination & Governance Committee	£15,000	£8,000
Reputation & Responsibility Committee	£15,000	£8,000

Workforce remuneration at Pearson

The Committee takes its responsibilities concerning the oversight of remuneration, policies and practice for the wider organisation seriously. Our remuneration principles are consistent across the employee population but how they are applied varies by business need, level and geography as required. The key difference in executive remuneration compared to the approach to remuneration across the workforce is that remuneration for our Executive Directors is more heavily weighted towards variable pay and linked to the delivery of our strategic objectives.

Our approach to remuneration across the wider organisation is as follows:

- **Base salary** – Set taking into account economic factors, competitive market rates, roles, skills, experience and individual performance
- **Allowances and benefits** – Reflect the local labour market in which they are based. All eligible employees (including Executive Directors) are also eligible to participate in savings-related share acquisition programmes in the UK, US and the rest of the world, which are not subject to any performance conditions
- **Retirement benefits** – Reflect local market practice. Pearson employees in the UK may participate in the same underlying pension arrangements as the Executive Directors, subject to certain age bands and legacy arrangements
- **Annual incentives** – Around 11,000 employees participate in an Annual Incentive Plan, which is funded based on similar performance measures as those used for the Executive Directors. A number of other employees participate in alternative forms of cash-based annual bonus such as sales incentive and commission plans based on performance targets and profit-shares where required for legislative reasons
- **Long-term incentives** – From 2021, senior management will participate in a new long-term incentive arrangement, which comprises both performance shares and restricted shares, recognising the markets in which Pearson competes for talent. This replaces the single incentive plan previously operated for this population. Below this senior management level, approximately 6% of employees – selected on the basis of their role, performance and potential – participate in share incentive schemes

During the year, the Committee received reports from the Chief Executive and Chief Human Resources Officer on pay and conditions across the company as a whole, and on the recruitment and retention experience. This includes any relevant feedback or insights received from employees through the Employee Engagement Network, which was established in 2019 and is attended periodically by the Chief Executive and Chief Human Resources Officer. In addition, any feedback received from employees through the employee engagement survey, which captures views on pay and benefits, helps inform Committee decisions. The Committee continues to develop the ways in which it engages with the wider organisation on executive remuneration.

The Committee also considers the company's gender pay gap for Great Britain. This year, the Committee was pleased to see that further progress was made on narrowing the gender pay gap, although noted that there was still more work to be done. In this regard, Pearson has a robust action plan and continues to drive investment towards the hiring, retention and development of women, as well as other diverse talent groups. Further details, including on the actions being taken to address the gap across our organisation, can be found within our gender pay gap report. Pearson is committed to promoting diversity, equity and inclusion globally, and during 2021 plans to extend our gender pay gap reporting to other countries in which we operate.

Remuneration report for 2020

Certain parts of this report have been audited as required by the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 as amended. Those tables which have been subject to audit are marked with an asterisk.

Single total figure of remuneration and prior year comparison*

Total aggregate emoluments for Executive and Non-Executive Directors were £3,215m in 2020. These emoluments are included within the total employee benefit expense in note 5 to the financial statements (p159)

Executive Directors

The remuneration received by Executive Directors in respect of the financial years ended 31 December 2020 and 31 December 2019 is set out below.

Andy Bird was appointed as Chief Executive and an Executive Director on 19 October 2020. The table below reflects remuneration received by Andy Bird in respect of his role as Executive Director. Remuneration received by him in respect of his Non-Executive Director role prior to his appointment as Chief Executive is included in the table on p116

John Fallon stepped down as Chief Executive and as a Board Director on 18 October 2020.

Sally Johnson was appointed Chief Financial Officer and Executive Director on 24 April 2020.

Coram Williams stepped down as Chief Financial Officer and as a Board Director on 24 April 2020.

In respect of each of these individuals, the table below reflects remuneration received while an Executive Director of the company.

Executive Director 'single figure' remuneration

	Andy Bird $000s		John Fallon £000s		Sally Johnson £000s		Coram Williams £000s	
Element of remuneration 000s	**2020**	**2019**	**2020**	**2019**	**2020**	**2019**	**2020**	**2019**
B Base salary	**260**	–	**653**	813	**353**	–	**172**	537
A&B Allowances and benefits	**125**	–	**24**	30	**9**	–	**12**	8
R Retirement benefits	**42**	–	**178**	211	**45**	–	**1**	62
Total fixed pay	**427**	–	**855**	1,054	**407**	–	**185**	607
AIP Annual incentives	**–**	–	**–**	–	**–**	–	**–**	–
LTIP Long-term incentives	**–**	–	**–**	562	**–**	–	**–**	–
Total variable pay	**–**	–	**–**	562	**–**	–	**–**	–
Total remuneration	**427**	–	**855**	1,616	**407**	–	**185**	607

Notes to single figure table*

B Base salary

The base salary shown in the single figure table reflects salary paid in the financial year while an Executive Director of the company. Andy Bird is paid in US dollars, while other Executive Directors are paid in pound sterling.

In response to the COVID-19 pandemic, John Fallon and Sally Johnson voluntarily took a temporary salary reduction of 25% and 20%, respectively, for the three-month period May to July. This was donated to charities engaged in COVID-19-related activities. The single figure table includes their salaries before this charitable donation.

A&B Allowances and benefits

The breakdown of benefits is as follows for 2020:

	Andy Bird $000	John Fallon £000	Sally Johnson £000	Coram Williams £000
Travel	–	16	9	–
Health	4	2	–	1
Accommodation	60	–	–	–
Other	61	6	–	11

Travel benefits comprise car allowance, shared use of a company car and driver for business purposes (for John Fallon only), and reimbursements of a taxable nature resulting from business travel and engagements. Health benefits comprise healthcare, health assessment and gym subsidy. Accommodation benefits for Andy Bird relate to the contribution towards the rental costs of an apartment in New York to be used for business purposes. Other benefits received relate to fees for professional services and subscriptions. For Andy Bird these are in connection with his appointment as Chief Executive.

In addition to the allowances and benefits set out, Executive Directors may also participate in company benefit or policy arrangements that have no taxable value and/or are available to all other employees in the same location.

Remuneration report for 2020

R Retirement benefits

Further detail on retirement benefits is set out later in this report on p113

AIP Annual incentives

The 2020 AIP for the Executive Directors was based on a mix of financial (80% weighting) and strategic measures (20% weighting). The 2020 AIP resulted in a nil payout for both John Fallon and Sally Johnson. For more detail on performance metrics and performance against targets in 2020, see below.

Andy Bird and Coram Williams were not eligible to participate in the 2020 AIP.

LTIP Long-term incentives

The 2018 LTIP award was subject to performance conditions assessed to 31 December 2020. Performance targets were not met and therefore the award will lapse in full. For further details see p110

The single figure of remuneration for 2019 includes the vesting of the 2017 LTIP award. The value of the award has been updated to reflect the dividends accrued and the share price on the date of vesting (1 May 2020) of 455.5p.

The value of the 2017 award previously disclosed in the 2019 Remuneration Report was estimated to be £803,000 for John Fallon based on a three-month average share price of 671.0p and did not reflect any dividends accrued on those shares.

The 2017 LTIP award which vested on 1 May 2020 was granted on 11 September 2017 when the share price was 586.0p. Between the date of grant and the vesting date, the share price had decreased to 455.5p. No element of the 2017 LTIP value disclosed in the single figure is therefore attributable to share price growth. The Remuneration Committee did not exercise discretion in respect of this share price movement.

AIP Executive Directors' annual incentive payments for 2020*

John Fallon and Sally Johnson were eligible to participate in the 2020 AIP. The following table summarises the performance targets and performance against these targets for the 2020 award which resulted in a nil payout.

Overall outcome

		Performance range				Payout
Performance measure	**% of total**	**Threshold**	**Target**	**Max**	**Actual results**	**% of max bonus opportunity**
Adjusted operating profit	30%	£445m	£482m	£539m	£313m	0%
Sales	30%	£3,734m	£3,785m	£3,851m	£3,397m	0%
Operating cash flow	20%	£398m	£429m	£492m	£315m	0%
Strategic measures	20%		See opposite			0%
	100%					0%

Note 1: The outcomes under all measures have been reviewed by internal audit.

Performance against strategic measures

The targets (and outcomes) for performance against each of the strategic measures are shown in the table below.

Whilst material progress was made against all strategic goals in the year despite the impact of COVID-19, the financial underpin, which was set in line with the operating profit threshold for 2020, was not met. Therefore, there is no payout under the strategic measures for 2020.

Strategic priority	Measure	% of total funding	Threshold	Target	Max.	Outcome
Accelerate the digital transformation of the company	Growth in digital and digitally- enabled sales	5%	+1% on prior year	+3% on prior year	+5% on prior year	› Whilst the company benefitted from a material shift to fully digital services with sales up 10%, this was also offset by the impact of COVID-19 on digitally-enabled businesses, such as VUE test centres, which declined 16% resulting in a net reduction of 2% for the year.
	Digital platforms – delivery of three 2020 milestones on digital roadmap	5%	Delivery of one milestone	Delivery of two milestones	Delivery of all three milestones	› The second phase of Revel was successfully launched in October 2020 with good progress also made against a number of other milestones including in relation to Employability pilot (UK Learns) › The digital roadmap is on track with the launch of additional Revel titles and c.250 new eText titles on the PLP.
Make the most of Pearson's world of talent	Implement a learning culture to support upskilling of workforce	5%	Conduct Learning Survey across the company and build out learning strategy	Further refinement of learning strategy, including implementation of learning culture initiatives for 2020	Pilot of learning strategy in one part of the business	› Specific learning questions were integrated into all employee pulse surveys alongside the creation of five-year vision and strategy for learning. This culminated in the delivery of the first 'Global Learning at Work' week and progress on new initiatives to support a learning culture and employee learning. One of these was the development of a 'Pearson Capabilities Framework', linked to skills, which was piloted as part of talent review process.
Create a simpler organisation	Continue roll-out of The Enabling Programme and implement Business Value Realisation plan	5%	Development of roadmap for Rest of World (RoW) and completed Business Value Realisation plan	One RoW territory tested and ready to implement plus completed plan for optimisation	TEP implemented within at least one RoW territory and demonstrable cost savings from optimisation	› TEP successfully went live in Asia in November 2020 › The Business Value Realisation programme is now closed and optimisation activity is fully underway despite disruption due to COVID-19.

Note: If an element of judgement was required to assess achievements that were not completely quantifiable, Internal Audit provided an independent assessment to the Committee.

Remuneration report for 2020

LTIP Executive Directors' Long-Term Incentive Plan award vesting for 2020*

In May 2018, John Fallon and Coram Williams were made awards under the 2018 LTIP. These awards were based on performance the business delivered over the three-year period from 2018 to 2020. On leaving the Company, Coram Williams forfeited all unvested LTIP awards, including this award.

The LTIP award made to John Fallon would have vested on the normal vesting date, pro-rated for time to reflect John's departure prior to the normal vesting date, but the applicable performance targets have not been not met and therefore his award, together with awards for other participants, will lapse in full.

The targets and performance against these targets are as follows:

		Performance range							Vesting	
Performance measure	% of total	Threshold	Target	Maximum	Payout at threshold	Payout at target	Payout at maximum	Actual	% achievement	% of total award
Adjusted EPS	A third	65p	68p	80p	15%	65%	100%	28.7p	0%	0%
ROIC	A third	5.0%	6.0%	8.0%	15%	65%	100%	2.9%	0%	0%
Relative TSR	A third	Median	N/A	Upper Quartile	25%	N/A	100%	Below median (Ranked 51 out of 94)	0%	0%
	100%								**Total**	**0%**

Relative TSR was measured against the constituents of the FTSE 100 at the start of the performance period. Overall, the Committee considers that the Remuneration Policy has operated as it intended during 2020.

Appointment of Chief Executive Officer

In October 2020, Andy Bird was appointed as Chief Executive after a very thorough recruitment process. In order to secure Andy Bird's appointment, the Committee developed a remuneration package mindful of practice in Andy Bird's home market – the US – where pay rates are substantially higher than in the UK and the way pay is structured is often very different. The Committee believe that such a package was an essential bridge between practices in order to secure an exceptional candidate who will lead Pearson through the next phase of its strategic development.

Going forward remuneration arrangements

With the exception of the co-investment award, a one-off arrangement to support his recruitment, Andy Bird's remuneration arrangements were set in line with our approved Directors' Remuneration Policy, which is aligned to UK market practice and key governance principles. Whilst within policy, the Committee recognises that this package represents an uplift over his predecessor. When setting the package, the Committee considered, as is typical practice, Andy Bird's proven skills and experience, the remuneration he received in his prior role and compensation levels for Chief Executive roles at comparable companies (including both FTSE-listed companies and global sector comparators). After careful evaluation, the Committee determined that such a package was appropriate, balancing these various reference points. While the Committee was mindful of internal relativities, it believed that securing such an exceptional candidate as Andy Bird was fundamental to Pearson's future success.

Remuneration Element	Amount	Commentary
Base salary	$1,250,000	Andy's first salary review will be in 2023. His base salary will be fixed at $1,250,000 until then.
Retirement benefits	16% of salary	Andy receives an annual cash allowance of 16% of base salary in lieu of pension. This is the cash allowance available to new hire Executive Directors under our shareholder approved Directors' Remuneration Policy and aligns to the maximum company contribution that UK employees of a similar age are eligible to receive.
Annual Incentive Plan Participation	Maximum annual opportunity of 200% base salary	Andy will be eligible to participate in Pearson's Annual Incentive Plan from 1 January 2021. He will have a maximum opportunity of 200% of base salary and a target bonus equal to 50% of the maximum opportunity.
Long-Term Incentive Plan Participation	Maximum annual opportunity of 300% base salary	From 2021, Andy will be eligible to participate in the Pearson Long-Term Incentive Plan with a maximum annual face value of 300% of base salary.
Benefits	In accordance with the Directors' Remuneration Policy	Andy receives benefits in line with our Directors' Remuneration Policy, including travel-related benefits, private healthcare and risk-related benefits. In addition, the Company makes a contribution towards the rental costs of an apartment in New York to be used for business purposes, the cost of which will be capped at of $240,000 per year ($20,000 per month) prior to any taxes which may be due. The Committee considers it critical for Andy to have a base in New York so that he can be close to Pearson operations on the East Coast, while also facilitating easier travel to our London headquarters.
Shareholding requirements	In accordance with the Directors' Remuneration Policy	Andy will be required to hold Pearson shares with a market value of 300% of base salary, this requirement will extend for two years post-employment. As at 31 December 2020, Andy had met his shareholding requirement.

Co-investment award*

As set out in the Chair's letter, in order to secure Andy Bird as our Chief Executive the Committee designed a one-off co-investment award. While recognising that such an award was not typical in the UK market, the Committee believes that this was the optimal structure to secure Andy Bird's recruitment whilst incentivising the creation of long-term shareholder value.

In order to grant the co-investment award, which was not envisaged in the Directors' Remuneration Policy approved by shareholders at the AGM held on 24 April 2020, the Company sought shareholder approval of a resolution to amend the Directors' Remuneration Policy on 18 September 2020. This resolution received support from 67% of shareholders. Given the unusual nature of the co-investment award in the UK market, the Board very much appreciated the support received by the majority of shareholders, although noted that a significant minority voted against the proposals. Pearson engaged extensively with shareholders during Andy's appointment process, and in light of the General Meeting outcome, the Committee undertook a further engagement exercise to listen to and understand the views and perspectives of our shareholders, as described in the Chair's letter.

The key features of the award are detailed below.

Director	Date of award	Vesting date	Number of shares	Face value	Face value (% of base salary)[1]
Andy Bird	9 December 2020	See below	1,208,861	$9,375,000	750%

1 Face value was determined using a share price of 590.2p (five-day average to 24 August 2020) and a USD:GBP exchange rate of 1.314 (five-day average to 24 August 2020).

The grant of the co-investment award was conditional on Andy purchasing Pearson shares equal to 300% of base salary by 31 December 2020 (being a total value of $3.75m), which he must continue to hold throughout the period to 31 December 2023. This personal investment by Andy demonstrates his commitment to the role and creates immediate alignment with shareholders.

The co-investment award will vest in three equal tranches as soon as practicable following 31 December 2021, 31 December 2022 and 31 December 2023 respectively and will be subject to performance underpins and Andy's continued employment as at each vesting date. Shares that vest will be subject to a holding period until 31 December 2023.

The co-investment award was designed taking into account Andy's home market – the US – where the structure of pay is often very different to the UK and aims to incentivise the transformation of the business and growth in the near-term. It was therefore considered appropriate that the phased vesting schedule and holding period to December 2023 reflect the period over which it is expected value will be delivered to our shareholders.

The vesting of the co-investment award is subject to the achievement of performance underpins to ensure the Committee can reduce vesting if in its opinion the performance of the business or the individual does not support this. These underpins are intended to prevent payment for failure.

The vesting of each tranche of the award will be subject to the following performance underpins:

› an appropriate level of progress being made in relation to delivering our strategy including our ongoing transition from print to digital

› no significant ESG issues related to Andy's tenure occurring which result in significant reputational damage

In addition, the vesting of the final tranche of the award will also be subject to the following TSR underpin:

› the company's TSR from the date of the announcement of Andy's appointment to 31 December 2023 is either (1) positive; or (2) is at median or above when compared to the performance of the FTSE 100

If one or more of the underpins are not achieved, then the Committee would consider whether, and to what extent, a discretionary reduction in the number of shares vesting was required.

In considering whether any adjustment was required in relation to the underpins on progress against strategy and ESG issues, the Committee will consider the framework on the following page.

Remuneration report for 2020

Framework for assessment of performance underpins

1 Initial review of underpins

How is delivery of the strategy progressing

Have there been any ESG issues

2 Consideration of broader performance and stakeholder experience

Impact on key performance indicators/measures

How has Pearson performed over the relevant period? Consider both financial and non-financial performance.

- In terms of progress against the strategy, is this reflected in key performance indicators/measures which were identified as part of the development of the strategy (e.g. digital growth)?
- In respect of any ESG issues, has there been any impact on key performance indicators/measures?

Wider stakeholder experience

What has the experience of wider stakeholders been over the relevant period?

Shareholders | Employees | Customers | Suppliers

Risk and controls

Consider progress of strategy and ESG issues in the context of the approved risk appetite and internal control framework.

Culture and conduct

Does decision-making promote a culture in line with approved policies and values? Have there been any conduct issues which the Committee should take into account?

Input from others

Draw on input from other Committees (e.g. Reputation & Responsible Committee) as well as management teams.

3 Determination of the number of shares vesting

Taking all of the above into account, the Committee to consider whether vesting of the relevant tranche of the co-investment award is equitable and reasonable, or whether, and to what extent, a discretionary reduction is required

Appointment of Chief Financial Officer

Sally Johnson was appointed as Chief Financial Officer on 24 April 2020. Sally's remuneration arrangements were disclosed in the 2019 annual report and accounts on p106. On appointment, Sally's base salary was set at £515,000 per annum, in line with the starting salary of Coram Williams in 2015. Her maximum AIP opportunity is 170% of salary and she will be granted an annual LTIP award with a maximum face value of 245% of salary.

Long-term incentives awarded in 2020*

The following LTIP awards were granted during the year:

Director	Date of award	Vesting date	Number of shares	Face value	Face value (% of base salary)	Value for threshold performance (% of maximum)[1]	Performance period
Sally Johnson	1 May 2020	1 May 2023	220,000	£1,262,184	245%	18.3%	1 Jan 20–31 Dec 22

1 Under the adjusted EPS and ROIC elements, 15% vests for threshold performance; under the TSR element, 25% vests for threshold performance. This is the weighted average of vesting for threshold.

Face value was determined using a share price of 573.72p (five-day average to 1 March 2020). The Committee exercised its discretion in determining the appropriate share price to use for this purpose which is normally the closing share price on the trading day prior to the date of grant (which would have been 459.80p). However, mindful of recent share price volatility, the Committee exercised its discretion to use the five-day average share price to 1 March 2020, which was the share price used to determine share awards for the wider employee population and resulted in a lower number of shares being granted.

The Committee reserves the right to adjust payouts up or down before they are released if it believes that the vesting outcome does not reflect underlying financial or non-financial performance or if such other exceptional factors warrant doing so. In making such adjustments, the Committee is guided by the principle of aligning shareholder and management interests.

Any shares vesting based on performance to 31 December 2022 will be subject to an additional two-year holding period to 1 May 2025.

Details of the performance targets for the 2020 long-term incentive awards are set out in the tables below:

Adjusted earnings per share (EPS) (one-third)		Net return on invested capital (ROIC) (one-third)		Relative total shareholder return (TSR) (one-third)	
Vesting schedule (% max)	Adjusted EPS for FY22	Vesting schedule (% max)	Adjusted net ROIC for FY22	Vesting schedule (% max)	Ranked position vs FTSE 100
15%	45.5p	15%	5.2%	25%	Median
65%	52.5p	65%	6.2%	–	–
100%	60p or above	100%	7.5% or above	100%	Upper quartile

Note 1: Straight-line vesting will occur in between the points shown, with no vesting for performance below threshold.
Note 2: Pearson's TSR performance is currently measured relative to the constituents of the FTSE 100 Index over the performance period. The Committee intends to keep this comparator group under review for future LTIP awards.

R Executive Directors' retirement benefits and entitlements*

Details of the Directors' pension entitlements and pension-related benefits during the period each served as an Executive Director in 2020 are as follows:

	Andy Bird $000s	John Fallon £000s	Sally Johnson £000s	Coram Williams £000s
Value of defined benefit	–	20	45	1
Other allowances in lieu of pension	42	158	–	–
Total value in 2020	42	178	45	1
Accrued pension at 31 December 2020	–	109	57	40

Note 1: The accrued pension at 31 December 2020 is the deferred annual pension to which the member would be entitled on ceasing pensionable service on 31 December 2020. It relates to the pension payable from the UK Plan. Normal retirement age is 62.
Note 2: The value of defined benefit reflects the change in value over the period, less inflation.
Note 3: Other allowances in lieu of pension represent the cash allowances paid.
Note 4: Total value is the sum of the previous two rows and is disclosed in the single figure of remuneration table.

Remuneration report for 2020

Pension Plans

Andy Bird – Payment in Lieu of Pension

Andy Bird receives a payment in lieu of pension at 16% of his base salary. This is the new hire Executive Director rate in accordance with our Directors' Remuneration Policy as approved at the 2020 AGM which was set in line with the pension provision for UK employees of a similar age.

John Fallon – The Pearson Pension Plan

John Fallon was a member of the Final Pay Section of the Pearson Pension Plan. Mr Fallon left Pearson on 31 December 2020 at which point his benefit accrual in the Plan ceased. Mr Fallon attained the maximum service accrual for this benefit when he reached 20 years' service in October 2017. With effect from this date, he had accrued a benefit of two-thirds of his final pensionable salary and no further service-related benefits were accrued under the Plan. Based on the 2020/21 earnings cap of £170,400, he will have accrued a pension of £108,680 per annum at this time.

In addition, during 2020 he received a taxable and non-pensionable cash supplement in lieu of the previous FURBS arrangement. This supplement was reduced from 26% to 23% of base salary during 2020 as the first annual step in reducing John Fallon's pension entitlements to align with the UK workforce rate of 16% of base salary under our revised Directors' Remuneration Policy. There are no enhanced early retirement benefits.

Sally Johnson – The Pearson Pension Plan

Sally is an existing member of the Final Pay Section of the Pearson Pension Plan. Her accrual rate is 1/60th of pensionable salary per annum, restricted to the Plan earnings cap (£170,400 per annum in 2020/21). There are no enhanced early retirement benefits.

Coram Williams – The Pearson Pension Plan

Coram Williams was a member of the Final Pay Section of the Pearson Pension Plan. Coram left Pearson on 24 April 2020, at which point his benefit accrual in the Plan ceased. He had an accrual rate of 1/60th of pensionable salary per annum, restricted to the Plan earnings cap (£166,200 per annum in 2019/2020), with continuous service with a service gap. There are no enhanced early retirement benefits.

SG Directors' interests in shares and value of shareholdings*

Shareholding guidelines

Executive Directors are expected to build up a substantial shareholding in the company in line with the policy of encouraging widespread employee share ownership and to align the interests of Executive Directors and shareholders. The current requirement is 300% of base salary for the Chief Executive and 200% of base salary for the Chief Financial Officer. Shares that count towards these guidelines include any shares held unencumbered by an Executive Director, their spouse and/or dependent children plus any shares vested but held pending release under a share plan and any shares unvested but not subject to future performance conditions (on a net of tax basis). Executive Directors have five years from their date of appointment to the Board to reach the guideline. Once the guideline has been met, it is not re-tested, other than when shares are sold.

Executive Directors are expected to retain their current guideline (or actual shareholding if lower) for two years following stepping down as an Executive Director. This guideline does not apply to shares purchased by the Director. On stepping down from the Board, John Fallon was reminded of his obligation with regards to this post- employment shareholding requirement, which the Committee will review on an annual basis.

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

Directors' interests

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

Director	Current shareholding (ordinary shares) at 31 Dec 20	Conditional shares subject to performance at 31 Dec 20	Conditional shares subject to employment only at 31 Dec 20	Total number of ordinary and conditional shares at 31 Dec 20	Guideline (% salary)	Guideline met?
Chair						
Sidney Taurel	223,406	–	–	–	–	–
Executive Directors						
Andy Bird	586,437	1,208,861	–	1,795,298	300%	Yes
John Fallon	450,262	517,000	70,135	1,037,397	300%	Yes (see note 7)
Sally Johnson	11,822	220,000	24,052	255,874	200%	n/a (see note 6)
Coram Williams	56,108	–	–	56,108	200%	n/a (see note 7)
Non-Executive Directors						
Elizabeth Corley	32,795	–	–	–	–	–
Sherry Coutu	5,061	–	–	–	–	–
Vivienne Cox	8,945	–	–	–	–	–
Josh Lewis	14,818	–	–	–	–	–
Linda Lorimer	13,838	–	–	–	–	–
Michael Lynton	18,785	–	–	–	–	–
Graeme Pitkethly	2,276	–	–	–	–	–
Tim Score	48,472	–	–	–	–	–
Lincoln Wallen	11,668	–	–	–	–	–

Note 1: Share interests are shown as at 31 December 2020. For Directors who stepped down from the Board during the year, share interests are shown as at the date of their stepping down.
Note 2: 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 under the Long-Term Incentive Plan and any other share plans they might have participated in.
Note 3: Conditional shares subject to performance means unvested shares which remain subject to performance conditions and/or performance underpins and continuing employment for a pre-defined period. This includes the LTIP awards granted in 2018, 2019 and 2020, and, in respect of Andy Bird, his co-investment award. The LTIP awards granted to John Fallon will be pro-rated for time to reflect his departure prior to the normal vesting date. The performance targets for the 2018 LTIP award were not met and therefore these awards will lapse in full.
Note 4: Conditional shares subject to employment only means unvested shares which are subject to a holding period and continued employment. For Sally Johnson this includes share awards granted before her appointment to the Board in May 2020.
Note 5: Sally Johnson also holds 2,658 options under the Pearson Save For Shares scheme, a savings-related share acquisition programme open to all employees. These are not subject to future performance conditions.
Note 6: Sally Johnson has five years from the date of her appointment as an Executive Director on 24 May 2020 to reach the shareholding guideline.
Note 7: John Fallon met his shareholding guideline. However, as a result of the decrease in share price, the value of his shareholding on departure from the Board was less than 300% of salary. Coram Williams had five years from the date of his appointment as an Executive Director on 1 August 2015 to reach the shareholding guideline. He stepped down from the Board on 24 April 2020.
Note 8: Graeme Pitkethly purchased 6,075 shares on 8 March 2021, taking his total holding to 8,351 shares. There have been no other changes in the interests of any Director between 31 December 2020 and 12 March 2021, being the latest practicable date prior to the publication of this report.

Remuneration report for 2020

CNF Chair and Non-Executive Director remuneration*

The remuneration paid to the Chair and Non-Executive Directors in respect of the financial years ended 31 December 2020 and 31 December 2019 is as set out in the table below. In response to the COVID-19 pandemic, the Chair and Non-Executive Directors voluntarily took a temporary fee reduction of 50% and 25%, respectively, for the three-month period May to July. This was donated to charities engaged in COVID-19-related activities. The figures in the table below are before this charitable donation.

Director £000s	2020 Total fees	2020 Taxable benefits	2020 Total	2019 Total fees	2019 Taxable benefits	2019 Total
Sidney Taurel	500	16	516	**500**	**8**	**508**
Andy Bird	41	–	41	**–**	**–**	**–**
Elizabeth Corley	115	1	116	**115**	**–**	**115**
Sherry Coutu	88	2	90	**56**	**–**	**56**
Vivienne Cox	129	3	132	**128**	**1**	**129**
Josh Lewis	28	7	35	**88**	**2**	**90**
Linda Lorimer	99	8	107	**98**	**4**	**102**
Michael Lynton	92	3	95	**91**	**–**	**91**
Graeme Pitkethly	92	1	93	**57**	**–**	**57**
Tim Score	116	1	117	**116**	**1**	**117**
Lincoln Wallen	92	0	92	**91**	**4**	**95**
Total	1,392	42	1,434	**1,340**	**20**	**1,360**

Note 1: A minimum of 25% of the Chair's and Non-Executive Directors' basic fee is paid in shares.
Note 2: Taxable benefits refer to travel, accommodation and subsistence expenses incurred while attending Board meetings during the period that were paid or reimbursed by the company which are deemed by HMRC to be taxable in the UK. The amounts in the table above include the grossed-up cost of UK tax to be paid by the company on behalf of the Directors.
Note 3: Andy Bird joined the Pearson Board as a Non-Executive Director with effect from 1 May 2020. He was appointed Chief Executive Officer and an Executive Director of Pearson on 19 October 2020. The table above reflects remuneration paid to him in respect of his Non-Executive Director role. Remuneration received in respect of his Executive Director role is set out in the table on p107.
Note 4: Sherry Coutu and Graeme Pitkethly joined the Pearson Board as Non-Executive Directors with effect from 1 May 2019. Josh Lewis retired from the Board at the AGM in May 2020.

Remuneration arrangements in respect of John Fallon's and Coram Williams' departure*

John Fallon

John Fallon stepped down as Chief Executive and as a Director of Pearson plc on 18 October 2020. John remained an employee and adviser until 31 December 2020 to support the transition to Andy Bird as new Chief Executive Officer.

Between 19 October 2020 and 31 December 2020, John was employed on his existing remuneration arrangements, save as described below.

- On ceasing to be employed by Pearson, and in accordance with the terms of his contract of employment, there was no payment for loss of office
- John remained eligible for an award under the AIP for the period 1 January 2020 to 31 December 2020. The award was based on Pearson group performance for 2020. As described on p108, performance for 2020 resulted in a nil payout
- John did not receive any award under the LTIP in respect of 2020
- John was treated as a good leaver in respect of his outstanding awards under the LTIP and treatment of the awards was in accordance with the relevant plan rules. The LTIP awards will vest on their normal vesting dates, subject to the achievement of the applicable performance conditions. They will be pro-rated to reflect John's departure prior to the normal vesting date. As described on p110, the 2018 LTIP will lapse in full
- In accordance with the Directors' Remuneration Policy, John was provided with appropriate support for his transition totalling a value of £60,000. Pearson will continue to support John with tax advice and filings in connection with his employment with Pearson. Pearson has also paid a total of £21,818, including associated taxes, in legal fees in connection with his departure
- In line with the Directors' Remuneration Policy, John is required to retain Pearson shares with a value of 300% of his base salary (or his actual shareholding if lower) for a period of two years from 19 October 2020. This guideline does not apply to shares purchased by John or earned prior to him being appointed as Chief Executive

Coram Williams

Coram Williams stepped down from the role of Chief Financial Officer on 24 April 2020. Coram Williams did not receive any payment in respect of his unserved notice period nor was there any payment for loss of office. Coram was not eligible for any AIP payment in respect of 2020 nor was he granted a 2020 LTIP. He forfeited all unvested LTIP awards on departure.

In accordance with the Directors' Remuneration Policy, Pearson continued to support Coram Williams with tax advice and filings in connection with any obligations resulting from his employment with Pearson.

Payments to former Directors*

There were no payments to former Directors in 2020.

Payments for loss of office*

All payments made to John Fallon and Coram Williams in respect of their stepping down as Executive Directors of Pearson are as set out opposite.

There were no additional payments for loss of office made to or agreed for Directors in 2020.

Service contracts

The terms and conditions of appointment of our current Directors are available for inspection at the company's registered office during normal business hours and at the AGM.

The Executive Directors have notice periods in their service contracts of 12 months from the company and six months from the Executives. Their contracts are dated 23 August 2020 (Andy Bird) and 15 January 2020 (Sally Johnson).

Non-Executive Directors serve Pearson under letters of appointment which are renewed annually and do not have service contracts. The Non-Executive Directors' letters of appointment do not contain provision for notice periods or for compensation if their appointments are terminated. The Chair's appointment may be terminated on 12-months' notice.

Executive Directors' non-executive directorships

Neither of the current Executive Directors, Andy Bird nor Sally Johnson, hold any external appointments.

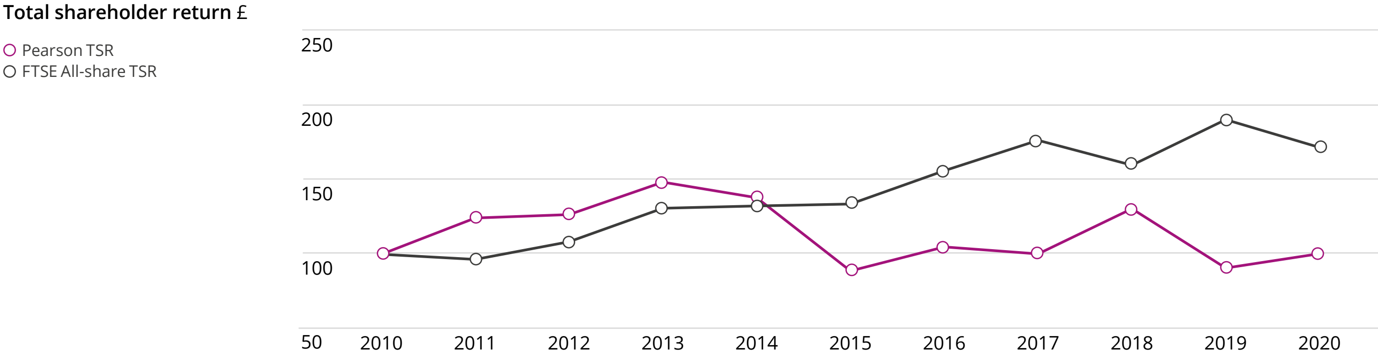
Historical performance and remuneration

Total shareholder return performance

Below we set out Pearson's total shareholder return (TSR) performance relative to the FTSE All-Share index on an annual basis over the 10-year period 1 January 2011 to 31 December 2020. This comparison has been chosen because the FTSE All-Share represents the broad market index within which Pearson shares are traded. TSR is the measure of the returns that a company has provided for its shareholders, reflecting share price movements and assuming reinvestment of dividends (source: Datastream).

In accordance with the reporting regulations, this section also presents Pearson's TSR performance alongside the single figure of total remuneration for the Chief Executive over the last 10 years and a summary of the variable pay outcomes relative to the prevailing maximum at the time.

Total shareholder return £



Source: Thomson Reuters Datastream

	Marjorie Scardino									John Fallon	Andy Bird
Chief Executive remuneration	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2020**
Total remuneration (single figure, £000s)	8,340	5,330	1,727	1,895	1,263	1,518	1,758	3,094	1,616	**855**	**334**
Annual incentive (% of maximum)	76%	24%	34%	51%	Nil	24%	44%	45%	Nil	**Nil**	**N/A**
Long-term incentive (% of maximum)	68%	37%	Nil	Nil	Nil	Nil	Nil	42%	33%	**Nil**	**N/A**

Note 1: Total remuneration is as reflected in the single total figure of remuneration table.
Note 2: Annual incentive is the actual annual incentive received by the incumbent as a percentage of maximum opportunity.
Note 3: Long-term incentive is the payout of performance-related share awards where the year shown is the final year of the performance period for the purposes of calculating the single total figure of remuneration.
Note 4: The single figure remuneration for Andy Bird has been converted using a USD:GBP exchange rate of 1.2772 (average exchange rate for 2020).

Remuneration report for 2020

Comparative information

The following information is intended to provide additional context regarding the total remuneration for Executive Directors.

Relative percentage change in remuneration of Directors and employees

The following table sets out the percentage change in base salary/fees, allowances and benefits and annual incentives between 2019 and 2020 in respect of all Directors of the Company during the year compared to the average percentage change for all employees of Pearson plc. The figures for all Directors are calculated based on remuneration received in the relevant year as set in the tables on p107 and p116. For base salary/fees, part-year figures have been pro-rated for the purposes of this disclosure.

While the Committee reviews base pay for the Executive Directors relative to the broader employee population, benefits are driven by local practices and eligibility is determined by level and individual circumstances which do not lend themselves to comparison.

	Percentage change in pay for Directors compared to the average employee of the company		
	Base salary/fees	Allowances and benefits	Annual Incentives
Average employee	2%	7%	10%
Executive Directors			
Andy Bird	–	–	–
John Fallon	1%	-19%	–
Sally Johnson	–	–	–
Coram Williams	0%	46%	–
Chair and Non-Executive Directors			
Sidney Taurel	0%	95%	–
Andy Bird	–	–	–
Elizabeth Corley	0%	–	–
Sherry Coutu	5%	–	–
Vivienne Cox	1%	159%	–
Josh Lewis	-5%	269%	–
Linda Lorimer	1%	102%	–
Michael Lynton	1%	–	–
Graeme Pitkethly	8%	–	–
Tim Score	0%	-20%	–
Lincoln Wallen	1%	-97%	–

Relative importance of pay spend

The Committee considers Directors' remuneration in the context of the company's allocation and disbursement of resources to different stakeholders. We chose adjusted operating profit because this is a measure of our ability to reinvest in the company. We include dividends because these constitute an important element of our return to shareholders.

			Headline change	
All figures in £ millions	2020	2019	£m	%
Adjusted operating profit	**313**	581	-268	**-46%**
Dividends	**146**	147	-1	**-1%**
Share buybacks	**176**	Nil	–	**–**
Total wages and salaries	**1,152**	1,258	-106	**-8%**

Note 1: Adjusted operating profit is as set out in the financial statements.
Note 2: Wages and salaries include continuing operations only and include Directors. Average employee numbers for continuing operations for 2020 were 21,335 (2019: 22,734). Further details are set out in Note 5 to the financial statements on p159

Chief Executive to employee pay ratio

The table below illustrates the ratio of Chief Executive to employee pay for 2020, using the single total figure of remuneration as disclosed on p107 compared to the full-time equivalent total reward of employees whose pay is ranked at the 25th, 50th and 75th percentiles (as identified by the gender pay gap methodology) in the GB workforce.

		Chief Executive pay ratio		
Year	Method	25th percentile	50th percentile	75th percentile
2020	B: Gender pay gap methodology	42.5	31.9	19.5
2019	B: Gender pay gap methodology	65.9	47.2	36.0

- Gender pay gap data from April 2020 was used to identify the employees at the 25th, 50th and 75th percentiles. Data was analysed for a number of employees around each quartile figure to ensure that there were no anomalies
- Using the gender pay gap data to identify the quartile employees is considered appropriate as this is a good representation of the relevant employee population at the year end, and is the most practicable methodology given the timing of the disclosure and determination of remuneration outcomes for the wider workforce
- Total remuneration for each employee, which was calculated with reference to 31 December 2020, has been compared to the Chief Executive's single figure. For 2020, the Chief Executive's single figure is a combined figure for Andy Bird and John Fallon, recognising the change in leadership during the year. Andy Bird's single figure has been converted using a USD:GBP exchange rate of 1.2772 (the average exchange rate for 2020)

- For the quartile employees, total remuneration has been calculated on a similar basis to the Chief Executive's single figure. Base salary and pension are based on full year figures taken from payroll. Benefits have been taken from the relevant individual's P11D in line with the methodology used for the Executive Directors. Annual bonus figures are based on the relevant manager recommendations and relate to performance in 2020. None of the employees at the 25th, 50th or 75th percentile had share awards vesting in 2020
- Total remuneration figures for the 25th, 50th and 75th percentile employees are as follows: £27,996, £37,275 and £60,970. The respective base salaries are: £27,103, £33,879 and £52,000
- A significant proportion of the Chief Executive's pay is linked to performance and, in respect of the LTIP, share price growth. Therefore, the Chief Executive's pay varies year-on-year based on company performance. In 2020, there was no payout for Executive Directors under either the AIP or the LTIP, reflecting the unforeseen impact of COVID-19 on the business. As such, the Chief Executive's single figure for 2020 comprises only fixed pay. In comparison, John Fallon's single figure for 2019 included the vesting of his 2017 LTIP award. This is the primary reason for the reduction in the Chief Executive pay ratio for 2020
- The company considers the median pay ratio consistent with the company's wider policies on employee pay, reward and progression. The Committee remains focused on ensuring that remuneration arrangements in place for the broader employee population are consistent with the need to attract and retain the right talent for the company's digital future

Dilution and use of equity

Pearson can use existing shares bought in the market, treasury shares or newly issued shares to satisfy awards under the company's various share plans. For restricted stock awards under the LTIP, the company would normally expect to use market purchased shares. There are limits on the amount of new-issue equity we can use. In any rolling 10-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. The headroom available for all Pearson plans, Executive or discretionary, and shares held in trust is as follows:

Headroom	2020
All Pearson plans	**8.1%**
Executive or discretionary plans	**5.0%**
Shares held in trust	**4.9%**

The Remuneration Committee in 2020

Role	Name	Title
Chair	Elizabeth Corley	Independent Non-Executive Directors
	Andy Bird (from 1 May until 18 October 2020)[1]	
	Sherry Coutu	
	Josh Lewis (until 24 April 2020)	
	Tim Score	
	Sidney Taurel[2]	Chair of the Board
Internal attendees	John Fallon	Chief Executive to 18 October 2020
	Andy Bird[1]	Chief Executive from 19 October 2020
	Coram Williams	Chief Financial Officer to 24 April 2020
	Sally Johnson	Chief Financial Officer from 24 April 2020
	Anna Vikström Persson	Chief Human Resources Officer
	Paul Christian	Senior Vice President – Reward
	Stephen Jones	Company Secretary to 30 June 2020
	Graeme Baldwin	Company Secretary from 1 July 2020
External advisers	Deloitte LLP	

1 Andy Bird was not present at any Remuneration Committee meeting where his remuneration was discussed.
2 Sidney Taurel was a member of the Committee throughout 2020 as permitted under the UK Corporate Governance Code.

Remuneration report for 2020

Advisers to the Remuneration Committee

During 2020, the Remuneration Committee received advice from independent Remuneration Committee advisers, Deloitte LLP. Deloitte LLP were appointed by the Committee in July 2017 following a tender process. The Committee also received legal advice from Freshfields Bruckhaus Deringer LLP in the course of the year.

Deloitte LLP supplied the Committee with advice on current market trends and developments, incentive plan design and target setting, investor engagement and other general Executive remuneration matters. In respect of their services to the Committee during 2020, Deloitte LLP were paid fees, which were charged on a time spent basis, of £229,150. During the year, separate teams within Deloitte LLP also provided Pearson plc with certain tax and other advisory and consultancy services.

Deloitte LLP are founding members of the Remuneration Consultants' Group and adhere to its Code of Conduct.

The Committee remains satisfied that the advice provided by Deloitte LLP was objective and independent, and that the provision of other services in no way compromised their independence. It is the view of the Committee that the Deloitte LLP engagement partner and team that provide remuneration advice to the Committee do not have connections with Pearson or its Directors that may impair their independence. The Committee reviewed the potential for conflicts of interest and judged that there were appropriate safeguards against such conflicts.

Terms of reference

The Committee's full charter and terms of reference are available on the Governance page of the company's website. A summary of the Committee's responsibilities is set out below.

The terms of reference reflect the provisions of the 2018 Code.

Committee responsibilities

→ Determine and review policy

Determine and regularly review the remuneration policies for the Executive Directors, the presidents and other members of Pearson's Executive Management (who report directly to the Chief Executive). These policies include base salary, annual and long-term incentives, pension arrangements, any other benefits, and termination of employment. When setting remuneration policy, the Committee also takes into account remuneration practices and related policies for the wider workforce.

→ Shareholder engagement

Ensure the company maintains an appropriate level of engagement with its shareholders and shareholder representative bodies in relation to the remuneration policy and its implementation.

→ Review and approve implementation

Regularly review the implementation and operation of the remuneration policy and approve the individual remuneration and benefits packages of Executive Management.

→ Approve performance-related plans

Approve the design of, and determine targets for, any performance-related pay plans operated by the Group for the Pearson Executive Management team and approve the total payments to be made under such plans.

→ Set termination arrangements

Advise and decide on general and specific remuneration arrangements in connection with the termination of employment of Executive Management.

→ Determine Chair's remuneration

Delegate responsibility for determining the remuneration and benefits package of the Chair of the Board.

→ Appoint remuneration consultants

Appoint and set the terms of engagement for any remuneration consultants who advise the Committee, and monitor the cost of such advice.

→ Talent, retention and gender pay gap

Review updates from management on talent, retention and gender pay gap.

→ Workforce remuneration

Have oversight of workforce remuneration, policies and practice for the wider organisation.

Remuneration Committee meeting focus during 2020

During the year the Committee undertook the following activities:

- Reviewed and approved 2019 annual and long-term performance and payouts to Executive Directors and senior management
- Reviewed and approved incentive arrangements for the company and how this will apply to Executive Directors and senior management for 2020
- Determined remuneration arrangements for the appointment of a new Chief Executive and Chief Financial Officer. This included engaging extensively with shareholders in respect of remuneration arrangements for the new Chief Executive, and continued monitoring of shareholder views following the outcome of the General Meeting in September 2020
- Approved remuneration arrangements for a number of new appointments to the Executive Committee
- Approved remuneration arrangements to apply in respect of John Fallon's retirement
- Reviewed shareholder and shareholder representative body feedback on remuneration, shareholder voting at Pearson's 2020 AGM and considered shareholder engagement strategy. Received input from investor relations on market expectations
- Received updates on the financial performance of the business and progress against strategic measures. Noted and reviewed the status of in-flight incentives
- Received updates on pay and conditions across the company a s a whole and took these into account when determining executive remuneration
- Noted updates on corporate governance, including a review of the 2020 AGM remuneration reporting season
- Reviewed the company's gender pay gap disclosures and noted the actions being taken to address the gap
- Noted the activity of the Standing Committee of the Board in relation to the operation of the company's equity-based reward programmes and noted the company's use of equity for employee share plans

Committee evaluation

Annually, the Committee reviews performance, constitution and charter and terms of reference to ensure it is operating at maximum effectiveness and recommends any changes it considers necessary to the Board for approval. Overall, following its review in 2020, it was considered that the Committee is operating effectively with strong processes in place and a high quality of discussion. The review recognised the Committee's efforts during 2020, in particular its contribution towards the Chief Executive succession process.
Going forward, the Committee will continue to ensure remuneration arrangements for senior management support the attraction of key talent as well as the delivery of the company's strategy. The Committee remains vigilant in assessing the extent to which its activities support and enable progress in the company.

Voting on remuneration resolutions

The following table summarises the details of votes cast in respect of the remuneration resolutions:

	% of votes cast for	% of votes cast against	Votes withheld
Annual remuneration votes (2020 AGM)	99.37%	0.63%	3,310,701
2020 Remuneration Policy vote (2020 AGM)	95.12%	4.88%	219,641
Amendment to Remuneration Policy (2020 EGM)	67.22%	32.78%	370,074

The Directors' remuneration report has been approved by the Board on 15 March 2021 and signed on its behalf by:

Elizabeth Corley
Chair of Remuneration Committee

Additional disclosures

Pages 66–126 of this document comprise the Directors' report for the year ended 31 December 2020.

Set out below is other statutory and regulatory information that Pearson is required to disclose in its Directors' report.

Going concern

The Directors have made an assessment of the Group's ability to continue as a going concern and consider it appropriate to adopt the going concern basis of accounting.

Viability statement

As set out on p63, the Board has also reviewed the prospects of Pearson over the three-year period to December 2023 taking account of the company's three-year plan, a 'severe but plausible' downside case and further stress-testing based on the principal risks set out from p60

Based on the results of these procedures, and considering the company's strong balance sheet, the Directors have a reasonable expectation that Pearson will be able to continue in operation and meet its liabilities as they fall due over the three-year period ending December 2023. Further details of the Group's liquidity are shown in the Financial review on p35

Share capital

Details of share issues and cancellations are given in note 27 to the financial statements on p189. 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 2020, 753,257,638 ordinary shares were in issue. At the AGM held on 24 April 2020, the company was authorised, subject to certain conditions, to acquire up to 76,063,126 ordinary shares by market purchase and to issue up to 507,087,512 ordinary shares. Shareholders will be asked to renew this authority at the AGM on 30 April 2021.

Share buyback

In December, we announced the sale of our 25% stake in Penguin Random House to Bertelsmann, generating total net proceeds of approximately $675m. The partial divestment of our stake in Penguin Random House was in line with our strategy for simplification and allowed us to create significant shareholder value through the synergies from the integration of the two businesses. Our stake in Penguin Random House will have generated c.£1.9bn in net disposal proceeds and dividends.

In line with our capital allocation priorities (to the right), the Board decided that we would use the proceeds from the above transaction to maintain a strong balance sheet and invest in our business in addition to returning £350m of surplus capital to shareholders following the closing of the transaction.

The share buyback programme, announced in December 2019, commenced on 16 January 2020 and was paused until further notice on 23 March 2020 as a prudent measure while the impact of COVID-19 was assessed. The original intention was to buy back approximately £350m of shares and at the date of pausing the programme approximately 30m shares had been bought back and cancelled at a cost of £176m. For further details, see note 27 to the financial statements.

The Board considers that maintaining a very strong balance sheet is appropriate, and as such there are no plans to reinitiate the buyback.

We have set out clear capital allocation priorities as follows:

- Maintaining a strong balance sheet and solid investment-grade credit ratings through an appropriate capital structure
- Investing in the business to drive organic growth
- A focused and disciplined approach to value enhancing acquisitions
- Delivering shareholder returns through a sustainable and progressive dividend policy
- Returning surplus cash to shareholders where appropriate through buybacks or special dividends

Major shareholders

Information provided to the company pursuant to the Financial Conduct Authority's Disclosure Guidance and Transparency Rules (DTR) is published on a Regulatory Information Service and on the company's website.

As at 31 December 2020, the company had been notified under DTR 5 of the following holders of significant voting rights in its shares.

	Number of voting rights	Percentage as at date of notification
Lindsell Train Limited	84,082,002	11.18%
Schroders plc[1]	75,127,663	9.98%
Silchester International Investors LLP	75,051,050	9.97%
BlackRock, Inc.[2]	48,912,172	6.50%
Cevian Capital II GP Limited	40,623,241	5.40%
FIL Limited[3]	39,151,633	5.19%
Ameriprise Financial, Inc. and its group	41,236,375	5.02%
Libyan Investment Authority[4]	24,431,000	3.01%

1 Includes 32,725 (0.004%) qualifying financial instruments to which voting rights are attached.
2 Includes 1,275,234 (0.16%) qualifying financial instruments to which voting rights are attached.
3 Includes 3,208,453 (0.43%) qualifying financial instruments to which voting rights are attached.
4 Based on notification to the company dated 7 June 2010. We have been notified of no change to this holding since that date. Assets belonging to, or owned, held or controlled on 16 September 2011 by the Libyan Investment Authority and located outside Libya on that date, are frozen in accordance with The Libya (Sanctions) (EU Exit) Regulations 2020.

Between 31 December 2020 and 12 March 2021, being the latest practicable date before the publication of this report, the company received further notifications under DTR 5, with the most recent positions being as follows:

	Number of voting rights	Percentage as at date of notification
BlackRock, Inc.[1]	52,806,616	7.00%
FIL Limited[2]	37,330,624	<5%

1 Includes 493,684 (0.06%) qualifying financial instruments to which voting rights are attached.
2 Includes 12,021,420 (1.59%) qualifying financial instruments to which voting rights are attached.

Annual General Meeting

The notice convening the AGM, to be held at 12:00 noon on Friday, 30 April 2021 at 190 High Holborn, London, WC1V 7BH, is contained in a circular to shareholders to be dated 24 March 2021.

Registered auditors

In accordance with section 489 of the Act, a resolution proposing the reappointment of PricewaterhouseCoopers LLP as auditors to the company will be proposed at the AGM, at a level of remuneration to be agreed by the Audit Committee.

Amendment to Articles of Association

Any amendments to the Articles of Association of the company (the Articles) may be made in accordance with the provisions of the Companies Act 2006 (the Act) by way of a special resolution. At the forthcoming AGM, the Board is proposing amendments to the company's current Articles. For additional details, see the Notice of Meeting.

Rights attaching to shares

The rights attaching to the ordinary shares are defined in the Articles. A shareholder whose name appears on the company's register of members can choose whether his/her shares are evidenced by share certificates (i.e. in certificated form) or held electronically (i.e. uncertificated form) in CREST (the electronic settlement system in the UK).

Subject to any restrictions below, shareholders may attend any general meeting of the company and, on a show of hands, every shareholder (or his/her representative) who is present at a general meeting has one vote on each resolution and, on a poll, every shareholder (whether an individual or a corporation) present in person or by proxy shall have one vote for every 25p of nominal share capital held. A resolution put to the vote at a general meeting is decided on a show of hands unless before, or on the declaration of the result of, a vote on a show of hands, a poll is demanded. A poll can be demanded by the Chair of the meeting, or by at least three shareholders (or their representatives) present in person and having the right to vote, or by any shareholders (or their representatives) present in person having at least 10% of the total voting rights of all shareholders, or by any shareholders (or their representatives) present in person holding ordinary shares on which an aggregate sum has been paid up of at least 10% of the total sum paid up on all ordinary shares. At this year's AGM, voting will again be conducted on a poll, consistent with best practice.

Shareholders can declare a final dividend by passing an ordinary resolution but the amount of the dividend cannot exceed the amount recommended by the Board. The Board can pay interim dividends on any class of shares of the amounts and on the dates and for the periods they decide. In all cases, the distributable profits of the company must be sufficient to justify the payment of the relevant dividend.

The Board may, if authorised by an ordinary resolution of the shareholders, offer any shareholder the right to elect to receive new ordinary shares, which will be credited as fully paid, instead of their cash dividend.

Any dividend which has not been claimed for 12 years after it became due for payment will be forfeited and will then belong to the company, unless the Directors decide otherwise.

If the company is wound up, the liquidator can, with the sanction of a special resolution passed by the shareholders, divide among the shareholders all or any part of the assets of the company and he/she can value assets and determine how the division shall be carried out as between the shareholders or different classes of shareholders. The liquidator can also, with the same sanction, transfer the whole or any part of the assets to trustees upon such trusts for the benefit of the shareholders.

Voting at general meetings

Any form of proxy sent by the shareholders to the company in relation to any general meeting must be delivered to the company (via its registrars), whether in written or electronic form, not less than 48 hours before the time appointed for holding the meeting or adjourned meeting at which the person named in the appointment proposes to vote.

The Board may decide that a shareholder is not entitled to attend or vote either personally or by proxy at a general meeting or to exercise any other right conferred by being a shareholder if he/she or any person with an interest in shares has been sent a notice under section 793 of the Act (which confers upon public companies the power to require information with respect to interests in their voting shares) and he/she or any interested person failed to supply the company with the information requested within 14 days after delivery of that notice. The Board may also decide, where the relevant shareholding comprises at least 0.25% of the nominal value of the issued shares of that class, that no dividend is payable in respect of those default shares and that no transfer of any default shares shall be registered.

Pearson operates an employee benefit trust to hold shares, pending employees becoming entitled to them under the company's employee share plans. There were 587,977 shares held as at 31 December 2020. The trust has an independent trustee which has full discretion in relation to the voting of such shares. A dividend waiver operates on the shares held in the trust.

Pearson also operates two nominee shareholding arrangements which hold shares on behalf of employees. There were 2,734,235 shares held in the Sharestore account and 1,129,959 shares held in the Global Nominee account as at 31 December 2020. The beneficial owners of shares held in Sharestore are invited to submit voting instructions online at www.shareview.co.uk. If no instructions are given by the beneficial owner by the date specified, the trustees holding these shares will not exercise the voting rights. The Global Nominees closed on 31 December 2020 following the transfer of administration to Computershare Investor Services plc. Beneficial holders of shares held in the Computershare Share Plan Account (SPA) are invited to submit voting instructions online at www.equateplus.com. If no instructions are given by the beneficial owner by the date specified, the nominee holding these shares will not exercise the voting rights.

Additional disclosures continued

Transfer of shares

The Board may refuse to register a transfer of a certificated share which is not fully paid, provided that the refusal does not prevent dealings in shares in the company from taking place on an open and proper basis. The Board may also refuse to register a transfer of a certificated share unless: (i) the instrument of transfer is lodged, duly stamped (if stampable), at the registered office of the company or any other place decided by the Board, and is accompanied by the certificate for the share to which it relates and such other evidence as the Board may reasonably require to show the right of the transferor to make the transfer; (ii) it is in respect of only one class of shares; and (iii) it is in favour of not more than four transferees.

Transfers of uncertificated shares must be carried out using CREST and the Board can refuse to register a transfer of an uncertificated share in accordance with the regulations governing the operation of CREST.

Variation of rights

If at any time the capital of the company is divided into different classes of shares, the special rights attaching to any class may be varied or revoked either:

(i) with the written consent of the holders of at least 75% in nominal value of the issued shares of the relevant class or

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

Without prejudice to any special rights previously conferred on the holders of any existing shares or class of shares, any share may be issued with such preferred, deferred or other special rights, or such restrictions, whether in regard to dividend, voting, return of capital or otherwise as the company may from time to time by ordinary resolution determine.

Appointment and replacement of Directors

The Articles contain the following provisions in relation to Directors.

Directors shall be no less than two in number. Directors may be appointed by the company by ordinary resolution or by the Board. A Director appointed by the Board shall hold office only until the next AGM and shall then be eligible for reappointment, but shall not be taken into account in determining the Directors or the number of Directors who are to retire by rotation at that meeting. The Board may from time to time appoint one or more Directors to hold Executive office with the company for such period (subject to the provisions of the Act) and upon such terms as the Board may decide and may revoke or terminate any appointment so made.

The Articles provide that, at every AGM of the company, at least one-third of the Directors shall retire by rotation (or, if their number is not a multiple of three, the number nearest to one-third). The first Directors to retire by rotation shall be those who wish to retire and not offer themselves for re-election. Any further Directors so to retire shall be those of the other Directors subject to retirement by rotation who have been longest in office since they were last re-elected but, as between persons who became or were last re-elected on the same day, those to retire shall (unless they otherwise agree among themselves) be determined by lot. In addition, any Director who would not otherwise be required to retire shall retire by rotation at the third AGM after they were last re-elected.

Notwithstanding the provisions of the Articles, the Board has resolved that all Directors should offer themselves for re-election annually, in accordance with the UK Corporate Governance Code (the Code).

The company may by ordinary resolution remove any Director before the expiration of his/her term of office. In addition, the Board may terminate an agreement or arrangement with any Director for the provision of his/her services to the company.

Powers of the Directors

Subject to the 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 authorisation, and any statutory restrictions or restrictions imposed by shareholders in a general meeting).

Directors' indemnities

A qualifying third-party indemnity (QTPI), as permitted by the Articles and sections 232 and 234 of the Act, has been granted by the company to each of its Directors. Under the provisions of the QTPI, the company undertakes to indemnify each Director against liability to third parties (excluding criminal and regulatory penalties) and to pay Directors' costs as incurred, provided that they are reimbursed to the company if the Director is found guilty, the court refuses to grant the relief sought or, in an action brought by the company, judgement is given against the Director. The indemnity has been in force for the financial year ended 31 December 2020 and is currently in force. The company has purchased and maintains Directors' and Officers' insurance cover against certain legal liabilities and costs for claims in connection with any act or omission by such Directors and Officers in the execution of their duties.

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.

At 31 December 2020, the Group's principal bank facility, the $1,190m revolving credit facility agreement, allowed that upon a change of control of the company, any participating bank may require its outstanding advances, together with accrued interest and any other amounts payable in respect of such facility, and its commitments, to be cancelled, each within 60 days of notification to the banks by the agent. The facility was undrawn at year end. The group's outstanding Fixed Rate Notes (See note 18 Borrowings for more information) also contain a provision requiring that, in the event of a change of control which leads to a downgrade in credit rating below Baa3 (Moody's) or BBB- (Standard and Poor's), the company is required to make an offer to investors to repurchase outstanding instruments at par plus accrued interest, which investors are not obliged to accept. For these purposes, a 'change of control' occurs if the company becomes a subsidiary of any other company, or one or more persons acting either individually or in concert obtains control (as defined in section 1124 of the Corporation Tax Act 2010) of the company.

Shares acquired through the company's employee share plans rank *pari passu* with shares in issue and have no special rights. For legal and practical reasons, the rules of these plans set out the consequences of a change of control of the company.

Other statutory information

Other information that is required by the Companies Act 2006 (the Act) and by the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (as amended) to be included in the Directors' report, and which is incorporated by reference, can be located as follows:

Summary disclosures index	**See more**
Dividend recommendation	**p32**
Financial instruments and financial risk management	**p176**
Important events since year end	**p36**
Future development of the business	**p12**
Research and development activities	**p26**
Employment of disabled persons	**p50**
Employee involvement	**p49**
Greenhouse gas emissions and energy consumption data	**p46**
Statement describing employee engagement	**p30**
Statement describing regard to suppliers, customers and other stakeholders' interests	**p30**

With the exception of the dividend waiver described on p123 there is no information to be disclosed in accordance with Listing Rule 9.8.4.

No political donations or contributions were made or expenditure incurred by the company or its subsidiaries during the year.

Fair, balanced and understandable reporting and disclosure of information

As required by the Code, we have established arrangements to ensure that all information we report to investors and regulators is fair, balanced and understandable. A process and timetable for the production and approval of this year's report was agreed by the Board at its meeting in December 2020. The full Board then had the opportunity to review and comment on the report as it progressed.

Representatives from financial reporting, corporate affairs, company secretarial, legal and risk are involved in the preparation and review of the annual report to ensure a cohesive and balanced approach and, as with all of our financial reporting, our Verification Committee conducts a thorough verification of narrative and financial statements. We also have procedures in place to ensure the timely release of inside information, through our Market Disclosure Committee.

The Audit Committee is also available to advise the Board on certain aspects of the report, to enable the Directors to fulfil their responsibility in this regard. The Directors consider that the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the company's position, performance, business model and strategy.

The Directors also confirm that, for each Director in office at the date of this report:

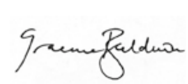
- so far as the Director is aware, there is no relevant audit information of which the Group and company's auditors are unaware
- they have taken all the steps that they ought to have taken as Directors in order to make themselves aware of any relevant audit information and to establish that the Group and the company's auditors are aware of that information.

Directors in office

The following Directors were in office during the year:

A Bird – appointed on 1 May 2020	L K Lorimer
E P L Corley	M M Lynton
S L Coutu	G D Pitkethly
V Cox	T Score
J J Fallon – retired on 18 October 2020	S Taurel
S K M Johnson – appointed on 24 April 2020	L A Wallen
S J Lewis – retired on 24 April 2020	C Williams – resigned 24 April 2020

The Directors' report has been approved by the Board on 15 March 2021 and signed on its behalf by:



Graeme Baldwin
Company Secretary

Statement of Directors' responsibilities

Statement of Directors' responsibilities

The Directors are responsible for preparing the annual report and the financial statements in accordance with applicable law and regulation.

Company law requires the Directors to prepare financial statements for each financial year. Under that law, the Directors have prepared the Group and company financial statements in accordance with International Accounting Standards in conformity with the requirements of the Companies Act 2006. Additionally, the Financial Conduct Authority's Disclosure Guidance and Transparency Rules require the Directors to prepare the Group financial statements in accordance with International Financial Reporting Standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in 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 Group and company and of the profit or loss of the Group for that period. In preparing the financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently
- state whether for the Group and company financial statements, International Accounting Standards in conformity with the requirements of the Companies Act 2006 and, for the Group, International Financial Reporting Standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union have been followed, subject to any material departures disclosed and explained in the financial statements
- make judgements and accounting estimates that are reasonable and prudent
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and company will continue in business

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group and company's transactions and disclose with reasonable accuracy at any time the financial position of the Group and company and enable them to ensure that the financial statements and the Directors' remuneration report comply with the Companies Act 2000.

The Directors are also responsible for safeguarding the assets of the Group and company 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 pp69–70, confirms that, to the best of their knowledge:

- the Group and company financial statements, which have been prepared in accordance with International Accounting Standards in conformity with the requirements of the Companies Act 2006 and, for the Group, International Financial Reporting Standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union, give a true and fair view of the assets, liabilities, financial position and profit of the Group and company
- the Strategic report contained in the annual report includes a fair review of the development and performance of the business and the position of the Group and company, together with a description of the principal risks and uncertainties that they face

This responsibility statement has been approved by the Board on 15 March 2021 and signed on its behalf by:

Sally Johnson
Chief Financial Officer

Financial statements

In this section

Consolidated financial statements

Notes to the consolidated financial statements

Company financial statements

Independent auditors' report to the members of Pearson plc

Report on the audit of the financial statements

Opinion

In our opinion, Pearson plc's consolidated financial statements and company financial statements (the 'financial statements'):

- give a true and fair view of the state of the Group's and of the company's affairs at 31 December 2020 and of the Group's profit and the Group's and company's cash flows for the year then ended;
- have been properly prepared in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements, included within the Annual Report and Accounts (the "Annual Report"), which comprise: the consolidated and company balance sheets at 31 December 2020; the consolidated income statement and consolidated statement of comprehensive income, the consolidated and company cash flow statements and the consolidated and company statements of changes in equity for the year then ended; and the notes to the financial statements, which include a description of the significant accounting policies.

Our opinion is consistent with our reporting to the Audit Committee.

Our audit approach

Overview

Audit scope

- We conducted our Group audit work in three key territories, being the UK, US and Brazil. This included full scope audits at three reporting components and specific audit procedures at a further eight components. The territories where we conducted audit procedures, together with work performed at corporate functions and at the Group level, accounted for approximately: 73% of the Group's revenue; 73% of the Group's statutory profit before tax; and 72% of the Group's adjusted profit before tax.
- For the purposes of the parent company audit, we performed a full scope audit in the UK of all material financial statement line items.

Key audit matters

- Carrying value of goodwill (Group)
- Returns provisioning (Group)
- Recoverability of pre-publication assets (Group)
- Provisions for uncertain tax positions (Group)
- Impact of COVID-19 (Group and company)
- Risk of fraud in revenue recognition (Group)
- Carrying value of investments in subsidiaries (company)

Materiality

- Overall Group materiality: £19 million (2019: £27 million) based on approximately 5% of the three year average of the Group's adjusted profit before tax.
- Overall company materiality: £45 million (2019: £49 million) based on approximately 1% of net assets.
- Performance materiality: £14 million (Group) and £34 million (company).

Separate opinion in relation to international financial reporting standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union

As explained in note 1 to the consolidated financial statements, the Group, in addition to applying international accounting standards in conformity with the requirements of the Companies Act 2006, has also applied international financial reporting standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union.

In our opinion, the consolidated financial statements have been properly prepared in accordance with international financial reporting standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ('ISAs (UK)') and applicable law. Our responsibilities under ISAs (UK) are further described in the auditors' responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We remained independent of the Group in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which include the FRC's Ethical Standard, as applicable to listed public interest entities and we have fulfilled our other ethical responsibilities in accordance with these requirements.

To the best of our knowledge and belief, we declare that non-audit services prohibited by the FRC's Ethical Standard were not provided to the Group.

Other than those disclosed in note 4 to the consolidated financial statements, we have provided no non-audit services to the Group in the period under audit.

The scope of our audit

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements.

Capability of the audit in detecting irregularities, including fraud

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined in the auditors' responsibilities for the audit of the financial statements section, to detect material misstatements in respect of irregularities, including fraud. The extent to which our procedures are capable of detecting irregularities, including fraud, is detailed below.

Based on our understanding of the Group and industry in which it operates, we identified that the principal risks of non-compliance with laws and regulations related to failure to comply with UK and international tax regulations, adherence to data protection requirements in the jurisdictions in which the Group operates and holds data and compliance with anti-bribery and corruption legislation in the jurisdictions in which the Group operates and we considered the extent to which non-compliance might have a material effect on the financial statements. We also considered those laws and regulations that have a direct impact on the preparation of the financial statements such as the Companies Act 2006 and Listing Rules. We evaluated management's incentives and opportunities for fraudulent manipulation of the financial statements (including the risk of override of controls) and we determined that the principal risks related to posting inappropriate journal entries, management bias in accounting for estimates, including estimates relating to revenue recognition, and manipulation of cut-off of shipments at major warehouse locations. The Group engagement team shared this risk assessment with the component auditors so that they could include appropriate audit procedures in response to such risks in their work. Audit procedures performed by the Group engagement team and/or component auditors included:

- Discussions with management, internal audit and the Group's legal advisors, including considerations of known or suspected instances of non-compliance with laws and regulations and fraud;
- Review of correspondence received from regulators and consideration of the impact, if any, on our audit and the disclosures made in the financial statements;
- Evaluation and testing of the effectiveness of management's controls designed to prevent and detect irregularities;
- Assessment of matters reported on the Group's whistleblowing helpline and the results of management's investigation of such matters;
- Identification and testing of significant manual journal entries;
- Testing of cut-off of shipments at major warehouse locations; and
- Testing of assumptions and judgements made by management in making significant accounting estimates.

There are inherent limitations in the audit procedures described above. We are less likely to become aware of instances of non-compliance with laws and regulations that are not closely related to events and transactions reflected in the financial statements. Also, the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations or through collusion.

Key audit matters

Key audit matters are those matters that, in the auditors' professional judgement, were of most significance in the audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by the auditors, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. These matters, and any comments we make on the results of our procedures thereon, were addressed in the context of our audit of the financial statements as a whole and in forming our opinion thereon and we do not provide a separate opinion on these matters.

This is not a complete list of all risks identified by our audit.

The impact of COVID-19 is a new key audit matter this year. Finance transformation, which was a key audit matter last year, is no longer included as the more significant elements of the Group's finance transformation programme were completed prior to 2020 and as the level of change to financial systems, processes and controls in 2020 has been significantly less than in 2019. In addition, we have removed the key audit matter related to disposals as the sale of the Group's US K-12 Courseware business in 2019 involved a number of complex accounting judgements and the application of management estimates whereas the sale of the Group's remaining stake in Penguin Random House in 2020, while material, did not involve complex judgements or estimation. Otherwise, the key audit matters below are consistent with last year.

Key audit matter	How our audit addressed the key audit matter
→ Carrying value of goodwill (Group)	
Refer to note 11 in the consolidated financial statements. The Group recorded goodwill of £2,094m (2019: £2,139m) at 31 December 2020. The carrying values of goodwill and intangible assets are dependent on estimates of future cash flows of the underlying cash generating units (CGUs) and there is a risk that if management does not achieve these cash flow estimates it could give rise to further impairment charges. This risk increases in periods when the Group's trading performance and projections do not meet expectations. The impairment reviews performed by management contain a number of significant judgements and estimates. Changes in these assumptions can result in materially different impairment charges or available headroom. No impairment charge has been recorded in 2020.	We obtained management's value in use impairment model at 31 December 2020 and we tested its mathematical integrity. We validated the carrying amounts of the net assets subject to impairment testing to the underlying accounting records, making sure that there was appropriate consistency between the assets and liabilities that were included in management's assessment and the related cash flows. We agreed the forecast cash flows to board approved budgets and strategic plans and we assessed how these budgets and strategic plans are compiled. We evaluated management's related judgements and estimates, including short-term revenue and operating profit growth rates, cash conversion, corporate cost allocations and restructuring savings. We compared management's forecasts and key assumptions to industry projections and comparable companies where this information was available and we evaluated the historical accuracy of management's budgeting and forecasting. We deployed valuations experts to assess the perpetuity growth rate and discount rate for each CGU by comparison with third party information, past performance and relevant risk factors. We compared management's valuations with third party valuations implied by trading and transaction multiples of the Group's competitors where this information was available for specific CGUs. Our procedures focused on the North American Courseware, OPM, Other International and Brazil CGUs where headroom is lower or more sensitive to changes in key assumptions. We performed our own independent sensitivity analysis to understand the impact of reasonably possible changes to key assumptions. We specifically evaluated the impact of the COVID-19 pandemic on management's future cash flow projections by comparison to external market economic forecasts. We performed independent sensitivity analysis to evaluate the impact of different COVID-19 scenarios on the Group's impairment judgements. We assessed the appropriateness of management's decision to provide additional disclosures about sensitivities in note 11 of the financial statements in relation to the North American Courseware, OPM, Other International and Brazil CGUs. More broadly, we considered whether the disclosures in note 11 complied with IAS 36. Based on the procedures performed, we noted no material issues arising from our work.

Independent auditors’ report to the members of Pearson plc

Key audit matter	How our audit addressed the key audit matter
→ Returns provisioning (Group)	
Refer to notes 3 and 24 in the consolidated financial statements. The Group has provided £86m (2019: £122m) for sales returns at 31 December 2020. The most significant exposure to potential returns within the Group arises in the US Higher Education Courseware business. Trends in the US market, including the growth of textbook rentals and the availability of free online content, continue to affect this business and have the potential to impact returns levels if shipping practices and arrangements with retailers are not managed in response to these trends. Management provides for returns based on past experience by customer and channel.	We assessed management’s evaluation of market trends and the Group’s responses and we considered whether management’s provisioning methodology continues to be appropriate in this context. We tested the returns provision calculations at 31 December 2020 and we agreed inputs including historical sales and actual returns experience to underlying records. We performed detailed testing over shipment and returns levels around the year-end and we evaluated whether these gave rise to an increased risk of future returns. We considered the reduction in the provision for sales returns in 2020 by reference to the related reduction in US Higher Education Courseware sales. We evaluated whether management had adopted methods and reached estimates for future returns that were supportable and appropriate. Based on the procedures performed, we noted no material issues arising from our work.
→ Recoverability of pre-publication assets (Group)	
Refer to note 20 in the consolidated financial statements. The Group holds £905m (2019: £870m) of pre-publication assets at 31 December 2020. Pre-publication assets represent direct costs incurred in the development of education platforms, programmes and titles prior to their public release. Given that these assets are amortised, management is required to undertake impairment trigger assessments at least annually or when triggering events occur. As a result of COVID-19, management has undertaken formal impairment tests of all material pre-publication assets in 2020. Judgement is required to assess the recoverability of the carrying value of these assets. This judgement is further complicated by the transition to digital as the Group invests in new, less proven, inter-linked digital content and platforms.	We assessed the appropriateness of capitalisation and amortisation policies and we considered whether these policies had been consistently applied. We selected a sample of costs to test their magnitude and appropriateness for capitalisation. We evaluated the reasonableness of amortisation periods and profiles compared to sales forecasts and historical sales experience, including considering the impact of the transition towards digital products. We obtained management’s impairment models at 31 December 2020 and we tested their mathematical integrity. We validated the carrying amounts of the pre-publication assets subject to impairment testing to the underlying accounting records. We assessed the reasonableness of discount rates applied by management. We assessed forecast cash flows against historical experience and future expectations. We challenged the carrying value of certain pre-publication assets where products are yet to be launched, are less proven or where sales are lower than originally anticipated. We performed our own independent sensitivity analysis to understand the impact of reasonably possible changes to key assumptions. Based on the procedures performed, we noted no material issues arising from our work.

Key audit matter	How our audit addressed the key audit matter
→ Provisions for uncertain tax positions (Group)	
Refer to notes 7 and 34 in the consolidated financial statements. The Group is subject to several tax regimes due to the geographical diversity of its businesses. At 31 December 2020, the Group held provisions for uncertain tax positions of £104m (2019: £152m). Management is required to exercise significant judgement in determining the appropriate amount to provide in respect of potential tax exposures and uncertain tax positions. The most significant provisions relate to US tax, transfer pricing and tax on prior year disposals. In addition, there are material unprovided tax exposures related to EU state aid and a Brazilian tax authority assessment related to goodwill amortisation deductions. Changes in assumptions about the views that might be taken by tax authorities can materially impact the level of provisions recorded in the consolidated financial statements.	We engaged our tax specialists in the US and UK and we obtained an understanding of the Group's tax strategy and risks. We assessed the tax impact of business developments in 2020, including the disposal of the Group's remaining stake in Penguin Random House and internal refinancing transactions. We recalculated the Group's tax provisions and determined whether the treatments adopted were in line with the Group's tax policies and had been applied consistently. We evaluated the key underlying assumptions, particularly in the US and UK. In making this evaluation, we considered the status of tax authority audits and enquiries. We considered the basis and support in particular for provisions not subject to tax audit in comparison with our experience of similar situations at comparable companies. We evaluated whether any risk of material misstatement existed for uncertain tax positions outside of the US and UK. We evaluated the consistency of management's approach to establishing or changing prior provision estimates and we validated that changes in prior provisions reflected a change in facts and circumstances during 2020. Where provisions have not been established, including for material potential exposures like EU state aid and the assessment from the Brazilian tax authority, we evaluated the basis for management's judgements, including an assessment of the treatment of similar exposures at comparable companies. We evaluated third party advice obtained by the Group as we independently formed our own view about the likelihood of these possible tax risks crystallising in future cash outflows. We noted that the assumptions and judgements required to formulate these provisions mean that the range of possible outcomes is broad. We evaluated the disclosures in notes 7 and 34 in relation to provisions for uncertain tax positions and we considered whether the disclosures were consistent with the underlying positions and with the requirements of IAS 1 and IAS 12. Based on the procedures performed, we noted no material issues arising from our work.

Independent auditors' report to the members of Pearson plc

Key audit matter	How our audit addressed the key audit matter
→ Impact of COVID-19 (Group and company)	
The COVID-19 pandemic has had a significant impact on the operations and recent trading performance of the Group. The extent of the impact of the pandemic on future trading performance is difficult to predict and will vary across the Group's portfolio of businesses. Therefore, there is inherent uncertainty in determining the impact of the pandemic on certain aspects of the consolidated and company financial statements. The financial statement areas that were most significantly impacted by COVID-19 involve those accounting estimates that are reliant on management's future budgets and forecasts, including impairment assessments for goodwill in the consolidated financial statements and for investments in subsidiary undertakings in the company financial statements, which have been addressed in separate key audit matters in this report, and going concern. In addition, management has reassessed a number of other accounting estimates in order to assess the impact of COVID-19, including inventory obsolescence, expected credit losses, sales returns, recoverability of product development and deferred tax assets, pension plan asset valuations and impairment trigger assessments for intangible assets, right-of-use property assets and sub-lease receivables. We focused on the impact of COVID-19 on the preparation of the consolidated and company financial statements as its impact is significant and widespread, both in terms of the impact on a range of the Group's accounting judgements and estimates and in terms of related disclosures in the Annual Report. In addition, management's ways of working, including the operation of key financial controls, have been impacted by COVID-19 as a result of employees working remotely and using technology-enabled working practices. There has also been an impact on our audit working practices as certain audit activities that have historically been undertaken in person, including inventory counts and component auditor oversight procedures, have had to be undertaken remotely.	We revisited our audit risk assessment originally presented to the Group in July 2020 as further information about the impact of COVID-19 on the Group's operations and trading became available. We updated our planned audit responses to a number of key audit matters and areas of focus to address the financial reporting and audit implications of the COVID-19 pandemic. Our conclusions in respect of going concern are set out separately in this report. With respect to management's key accounting estimates, we evaluated and tested management's reassessment of these estimates and the methodologies applied to arrive at these estimates. We performed procedures to assess any control implications arising from the change in management's ways of working and we assessed the effectiveness of management's key control operation compared to prior periods. We assessed our ability to execute the audit when operating under the restrictions of national lockdowns and related international travel restrictions. We implemented alternative communication and review protocols with management and with component auditors. We agreed with the Group an extension to the planned timetable for the sign-off of the Annual Report and audit completion in order to provide adequate time for management to make its assessment of the business and financial reporting impacts of COVID-19 and for our Group and component audit teams to complete the required audit procedures. With respect to inventory counts, we attended certain counts virtually using a live video feed and we were able to obtain the level of evidence and support that we required. We reviewed management's disclosures in relation to the impact of COVID-19 in the Annual Report, considering whether the disclosures were consistent with the Group's scenario planning and with actual trading experience. Based on the procedures performed, we noted no material issues arising from our work.
→ Risk of fraud in revenue recognition (Group)	
Refer to note 3 in the consolidated financial statements. Certain of the Group's businesses in the US and UK enter into contracts that span year-end, where revenue is recognised using estimated percentage of completion based on costs. These include contracts to design, develop and deliver testing and accreditation services. These contracts generate material deferred revenue balances and changes to the underlying assumptions or estimation calculations could have a material effect on the consolidated financial statements.	For a selection of the larger and more judgemental contracts, we read the contracts and we assessed the accounting methodologies applied to calculate the proportion of revenue being recognised in 2020. We considered whether management's revenue recognition practices are in accordance with Group policies and related accounting standards and have been consistently applied. We tested costs incurred to date and management's estimates of forecast costs and revenues by reference to historical experience and current contract status. We recalculated management's percentage of completion estimates and we performed look-back tests to assess management's historical accuracy of forecasting for these types of arrangement. In addition, we tested revenue recognised around year-end to ensure that it was recognised in the proper period, focusing on cut-off of shipments at the Group's major shipping locations, and we performed manual journals testing focusing on unusual or unexpected entries to revenue. Based on the procedures performed, we noted no material issues arising from our work.

Key audit matter	How our audit addressed the key audit matter
→ Carrying value of investments in subsidiaries (company)	
Refer to note 2 in the company financial statements. The company holds investments in subsidiaries amounting to £6,619m (2019: £6,664m) at 31 December 2020. Investments in subsidiaries are accounted for at cost less provision for impairment in the company balance sheet. Investments are tested for impairment if impairment indicators exist. If such indicators exist, the recoverable amounts of investments in subsidiaries are estimated in order to determine the extent of the impairment loss, if any. Any such impairment loss is recognised in the income statement. The impairment assessment was identified as a key audit matter given the size of the underlying investment carrying values and the differential to the Group's market capitalisation. Further impairment indicators were identified in connection with certain of the investments in subsidiaries due to the carrying value of investments exceeding their net assets. The assessment required the application of management judgement, particularly in determining whether any impairment indicators have arisen that trigger the need for an impairment assessment and in assessing whether the carrying value of each investment can be supported by the recoverable amount. Changes to these judgements and estimates could have a material impact on the company financial statements.	We evaluated management's assessment whether any indicators of impairment existed by comparing the carrying values of investments in subsidiaries with their net assets at 31 December 2020. For investments where the net assets were lower than the carrying values, we assessed their recoverable value by reference to the value in use of the investments compared to their carrying values at 31 December 2020. Where applicable, we verified that the recoverable values of investments were consistent with the recoverable values of the related CGUs tested for goodwill impairment purposes, leveraging the audit work undertaken as part of the Group audit. We separately evaluated the difference between the carrying value of the company's investments in subsidiaries and the Group's market capitalisation. Based on the procedures performed, we noted no material issues arising from our work.

How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the structure of the Group and the company, the accounting processes and controls and the industry in which they operate.

The consolidated financial statements are a consolidation of 521 reporting units, each of which is considered to be a component. We identified three components in the UK and US that required a full scope audit due to their size. Audit procedures over specific financial statement line items were performed at a further five components in the UK, US and Brazil to achieve appropriate audit coverage. In addition, we have undertaken certain unpredictable audit procedures on a rotational basis covering components that have not historically been included in Group audit scope.

In establishing the overall approach to the Group audit, we determined the type of work that needed to be performed at the components by us, as the Group engagement team, or by component auditors within PwC UK and from other PwC network firms operating under our instruction. Where the work was performed by component auditors, we determined the level of involvement we needed to have in the audit work at those reporting units to be able to conclude whether sufficient appropriate audit evidence had been obtained as a basis for our opinion on the consolidated financial statements as a whole.

We performed full scope audits in respect of NCS Pearson (encompassing the US businesses which form part of the Global Assessment segment), Pearson Education US (encompassing the US business which forms part of the North American Courseware segment) and Pearson Education UK (forming part of the International segment).

We performed specified procedures at a further five components within the North American Courseware, Global Online Learning and International segments and across the Enabling Functions over financial statement line items including revenue, trade and other receivables, deferred income, cash, intangible assets and amortisation, accruals, provisions for returns, product development and amortisation, fixed assets and depreciation, cost of sales and operating expenses. This ensured that sufficient and appropriate audit procedures were performed to achieve sufficient coverage over these financial statement line items.

In addition to instructing and reviewing the reporting from our component audit teams, we conducted file reviews and participated in key meetings with local management. We also had regular dialogue with component teams throughout the year.

Independent auditors’ report to the members of Pearson plc

The Group consolidation, financial statement disclosures and corporate functions were audited by the Group engagement team. This included our work over taxation, goodwill and acquired intangible assets, post-retirement benefits and major transactions. Taken together, the components and corporate functions where we conducted audit procedures accounted for approximately 73% of the Group’s revenue, 73% of the Group’s statutory profit before tax and 72% of the Group’s adjusted profit before tax. This provided the evidence we needed for our opinion on the consolidated financial statements taken as a whole. This was before considering the contribution to our audit evidence from performing audit work at the Group level, including disaggregated analytical review procedures, which covered certain of the Group’s smaller and lower risk components that were not directly included in our Group audit scope.

Our audit of the company financial statements was undertaken in the UK and included substantive procedures of all material balances and transactions.

Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and in aggregate, on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

	Consolidated financial statements	Company financial statements
Overall materiality	£19m (2019: £27m)	£45m (2019: £49m)
How we determined it	Approximately 5% of the three year average of the Group’s adjusted profit before tax	Approximately 1% of net assets
Rationale for benchmark applied	The Group’s principal measure of performance is adjusted operating profit, which excludes one-off gains and losses, costs of major restructuring and acquired intangible asset amortisation and impairment charges, in order to present results from operating activities on a consistent basis. We have also excluded the results of Penguin Random House from this benchmark for each of the three years following its disposal. We have taken this measure into account in determining our materiality as it is the metric against which the performance of the Group is most commonly assessed by management and reported to shareholders. From adjusted operating profit, we deducted net finance costs. Given the volatility in profitability in 2020 as a result of COVID-19, we based our materiality calculation on a three year average of the Group’s adjusted profit before tax.	Pearson plc is the ultimate parent company which holds the Group’s investments. Therefore, the entity is not in itself profit-oriented. The strength of the balance sheet is the key measure of financial health that is important to shareholders, since the primary concern for the company is the payment of dividends. We therefore consider net assets to be an appropriate benchmark. Certain account balances were included in scope for the audit of the consolidated financial statements and were therefore audited to a materiality level set below overall materiality established for the Group audit. However, we determined that the company did not require a full scope audit of its complete financial information for the purposes of the audit of the consolidated financial statements.

For each component in the scope of our Group audit, we allocated a materiality that is less than our overall Group materiality. The range of materiality allocated across components was approximately £3m to £16m.

We use performance materiality to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds overall materiality. Specifically, we use performance materiality in determining the scope of our audit and the nature and extent of our testing of account balances, classes of transactions and disclosures, for example in determining sample sizes. Our performance materiality was 75% of overall materiality, amounting to £14m for the consolidated financial statements and £34m for the company financial statements.

In determining the performance materiality, we considered a number of factors, including the history of misstatements, risk assessment and aggregation risk and the effectiveness of controls, concluding that an amount at the upper end of our normal range was appropriate.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £2m for the Group and company audits (2019: £2m) as well as misstatements below those amounts that, in our view, warranted reporting for qualitative reasons.

Conclusions relating to going concern

Our evaluation of the Directors' assessment of the Group's and the company's ability to continue to adopt the going concern basis of accounting included:

- Evaluation of management's base case and downside case scenarios, understanding and evaluating the key assumptions, including assumptions related to COVID-19;
- Validation that the cash flow forecasts used to support management's impairment, going concern and viability assessments were consistent;
- Assessment of the historical accuracy and reasonableness of management's forecasting;
- Consideration of the Group's available financing and debt maturity profile;
- Testing of the mathematical integrity of management's liquidity headroom, covenant compliance, sensitivity and stress testing calculations;
- Assessment of the reasonableness of management's planned or potential mitigating actions; and
- Review of the related disclosures in the Annual Report.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the Group's and the company's ability to continue as a going concern for a period of at least twelve months from when the financial statements are authorised for issue.

In auditing the financial statements, we have concluded that the Directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

However, because not all future events or conditions can be predicted, this conclusion is not a guarantee as to the Group's and the company's ability to continue as a going concern.

In relation to the company's reporting on how they have applied the UK Corporate Governance Code, we have nothing material to add or draw attention to in relation to the Directors' statement in the financial statements about whether the Directors considered it appropriate to adopt the going concern basis of accounting.

Our responsibilities and the responsibilities of the Directors with respect to going concern are described in the relevant sections of this report.

Reporting on other information

The other information comprises all of the information in the Annual Report other than the financial statements and our auditors' report thereon. The Directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

With respect to the Strategic Report and Governance Report, we also considered whether the disclosures required by the UK Companies Act 2006 have been included.

Based on our work undertaken in the course of the audit, the Companies Act 2006 requires us also to report certain opinions and matters as described below.

Strategic Report and Governance Report

In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic Report and Governance Report for the year ended 31 December 2020 is consistent with the financial statements and has been prepared in accordance with applicable legal requirements.

In light of the knowledge and understanding of the Group and company and their environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic Report and Governance Report.

Directors' Remuneration

In our opinion, the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006.

Corporate governance statement

The Listing Rules require us to review the Directors' statements in relation to going concern, longer-term viability and that part of the corporate governance statement relating to the company's compliance with the provisions of the UK Corporate Governance Code specified for our review. Our additional responsibilities with respect to the corporate governance statement as other information are described in the reporting on other information section of this report.

Based on the work undertaken as part of our audit, we have concluded that each of the following elements of the corporate governance statement is materially consistent with the financial statements and our knowledge obtained during the audit and we have nothing material to add or draw attention to in relation to:

- The Directors' confirmation that they have carried out a robust assessment of the emerging and principal risks;
- The disclosures in the Annual Report and Accounts that describe those principal risks, what procedures are in place to identify emerging risks and an explanation of how these are being managed or mitigated;
- The Directors' statement in the financial statements about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them and their identification of any material uncertainties to the Group's and company's ability to continue to do so over a period of at least twelve months from the date of approval of the financial statements;

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- The Directors' explanation as to their assessment of the Group's and company's prospects, the period this assessment covers and why the period is appropriate; and
- The Directors' statement as to whether they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period of its assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

Our review of the Directors' statement regarding the longer-term viability of the Group was substantially less in scope than an audit and only consisted of making inquiries and considering the Directors' process supporting their statement; checking that the statement is in alignment with the relevant provisions of the UK Corporate Governance Code; and considering whether the statement is consistent with the financial statements and our knowledge and understanding of the Group and company and their environment obtained in the course of the audit.

In addition, based on the work undertaken as part of our audit, we have concluded that each of the following elements of the corporate governance statement is materially consistent with the financial statements and our knowledge obtained during the audit:

- The Directors' statement that they consider the Annual Report, taken as a whole, is fair, balanced and understandable and provides the information necessary for the members to assess the Group's and company's position, performance, business model and strategy;
- The section of the Annual Report that describes the review of effectiveness of risk management and internal control systems; and
- The section of the Annual Report describing the work of the Audit Committee.

We have nothing to report in respect of our responsibility to report when the Directors' statement relating to the company's compliance with the Code does not properly disclose a departure from a relevant provision of the Code specified under the Listing Rules for review by the auditors.

Responsibilities for the financial statements and the audit

Responsibilities of the Directors for the financial statements

As explained more fully in the Statement of Directors' Responsibilities, the Directors are responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The Directors are also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Directors are responsible for assessing the Group's and the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Group or the company or to cease operations or have no realistic alternative but to do so.

Auditors' responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Our audit testing might include testing complete populations of certain transactions and balances, possibly using data auditing techniques. However, it typically involves selecting a limited number of items for testing, rather than testing complete populations. We will often seek to target particular items for testing based on their size or risk characteristics. In other cases, we will use audit sampling to enable us to draw a conclusion about the population from which the sample is selected.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditors' report.

Use of this report

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.

Other required reporting

Companies Act 2006 exception reporting

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

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

We have no exceptions to report arising from this responsibility.

Appointment

Following the recommendation of the Audit Committee, we were appointed by the members on 6 February 1996 to audit the financial statements for the year ended 31 December 1996 and subsequent financial periods. The period of total uninterrupted engagement is 25 years, covering the years ended 31 December 1996 to 31 December 2020.

Giles Hannam (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London

15 March 2021

Consolidated income statement

Year ended 31 December 2020

All figures in £ millions	Notes	2020	2019
Continuing operations			
Sales	2	**3,397**	3,869
Cost of goods sold	4	**(1,767)**	(1,858)
Gross profit		**1,630**	2,011
Operating expenses	4	**(1,402)**	(1,806)
Other net gains and losses	4	**178**	16
Share of results of joint ventures and associates	12	**5**	54
Operating profit	2	**411**	275
Finance costs	6	**(107)**	(84)
Finance income	6	**50**	41
Profit before tax		**354**	232
Income tax	7	**(44)**	34
Profit for the year		**310**	266
Attributable to:			
Equity holders of the company		**310**	264
Non-controlling interest		**–**	2
Earnings per share attributable to equity holders of the company during the year (expressed in pence per share)			
– basic	8	**41.0p**	34.0p
– diluted	8	**41.0p**	34.0p

Consolidated statement of comprehensive income

Year ended 31 December 2020

All figures in £ millions	Notes	2020	2019
Profit for the year		**310**	266
Items that may be reclassified to the income statement			
Net exchange differences on translation of foreign operations – Group		**(109)**	(113)
Net exchange differences on translation of foreign operations – associates		**–**	(2)
Currency translation adjustment disposed		**(70)**	4
Attributable tax	7	**(13)**	5
Items that are not reclassified to the income statement			
Fair value gain on other financial assets		**14**	20
Attributable tax	7	**(6)**	(4)
Remeasurement of retirement benefit obligations – Group	25	**(23)**	(145)
Remeasurement of retirement benefit obligations – associates		**–**	(4)
Attributable tax	7	**2**	22
Other comprehensive expense for the year	29	**(205)**	(217)
Total comprehensive income for the year		**105**	49
Attributable to:			
Equity holders of the company		**105**	47
Non-controlling interest		**–**	2

Consolidated balance sheet

As at 31 December 2020

All figures in £ millions	Notes	2020	2019
Assets			
Non-current assets			
Property, plant and equipment	10	**515**	618
Intangible assets	11	**2,742**	2,900
Investments in joint ventures and associates	12	**6**	7
Deferred income tax assets	13	**32**	59
Financial assets – derivative financial instruments	16	**45**	29
Retirement benefit assets	25	**410**	429
Other financial assets	15	**138**	122
Trade and other receivables	22	**223**	313
		4,111	4,477
Current assets			
Intangible assets – pre-publication	20	**905**	870
Inventories	21	**129**	169
Trade and other receivables	22	**1,118**	1,275
Financial assets – derivative financial instruments	16	**18**	25
Cash and cash equivalents (excluding overdrafts)	17	**1,097**	437
		3,267	2,776
Assets classified as held for sale	32	**73**	397
Total assets		**7,451**	7,650
Liabilities			
Non-current liabilities			
Financial liabilities – borrowings	18	**(1,397)**	(1,572)
Financial liabilities – derivative financial instruments	16	**(40)**	(24)
Deferred income tax liabilities	13	**(62)**	(48)
Retirement benefit obligations	25	**(85)**	(92)
Provisions for other liabilities and charges	23	**(8)**	(13)
Other liabilities	24	**(80)**	(86)
		(1,672)	(1,835)

Consolidated balance sheet continued

As at 31 December 2020

All figures in £ millions	Notes	2020	2019
Current liabilities			
Trade and other liabilities	24	**(1,196)**	(1,278)
Financial liabilities – borrowings	18	**(254)**	(92)
Financial liabilities – derivative financial instruments	16	**(12)**	(15)
Current income tax liabilities		**(84)**	(55)
Provisions for other liabilities and charges	23	**(25)**	(52)
		(1,571)	(1,492)
Liabilities classified as held for sale	32	**(74)**	–
Total liabilities		**(3,317)**	(3,327)
Net assets		**4,134**	4,323
Equity			
Share capital	27	**188**	195
Share premium	27	**2,620**	2,614
Treasury shares	28	**(7)**	(24)
Capital redemption reserve		**18**	11
Fair value reserve		**53**	39
Translation reserve		**388**	567
Retained earnings		**865**	911
Total equity attributable to equity holders of the company		**4,125**	4,313
Non-controlling interest		**9**	10
Total equity		**4,134**	4,323

These financial statements have been approved for issue by the Board of Directors on 15 March 2021 and signed on its behalf by

Sally Johnson
Chief Financial Officer

Consolidated statement of changes in equity

Year ended 31 December 2020

	Equity attributable to equity holders of the company									
All figures in £ millions	Share capital	Share premium	Treasury shares	Capital redemption reserve	Fair value reserve	Translation reserve	Retained earnings	Total	Non-controlling interest	Total equity
At 1 January 2020	195	2,614	(24)	11	39	567	911	4,313	10	4,323
Profit for the year	–	–	–	–	–	–	310	310	–	310
Other comprehensive income/(expense)	–	–	–	–	14	(179)	(40)	(205)	–	(205)
Total comprehensive income/(expense)	–	–	–	–	14	(179)	270	105	–	105
Equity-settled transactions	–	–	–	–	–	–	29	29	–	29
Tax on equity-settled transactions	–	–	–	–	–	–	–	–	–	–
Issue of ordinary shares under share option schemes	–	6	–	–	–	–	–	6	–	6
Buyback of equity	(7)	–	–	7	–	–	(176)	(176)	–	(176)
Purchase of treasury shares	–	–	(6)	–	–	–	–	(6)	–	(6)
Release of treasury shares	–	–	23	–	–	–	(23)	–	–	–
Dividends	–	–	–	–	–	–	(146)	(146)	(1)	(147)
At 31 December 2020	188	2,620	(7)	18	53	388	865	4,125	9	4,134

	Equity attributable to equity holders of the company									
All figures in £ millions	Share capital	Share premium	Treasury shares	Capital redemption reserve	Fair value reserve	Translation reserve	Retained earnings	Total	Non-controlling interest	Total equity
At 1 January 2019	195	2,607	(33)	11	19	678	961	4,438	9	4,447
Profit for the year	–	–	–	–	–	–	264	264	2	266
Other comprehensive income/(expense)	–	–	–	–	20	(111)	(126)	(217)	–	(217)
Total comprehensive income/(expense)	–	–	–	–	20	(111)	138	47	2	49
Equity-settled transactions	–	–	–	–	–	–	25	25	–	25
Tax on equity-settled transactions	–	–	–	–	–	–	(5)	(5)	–	(5)
Issue of ordinary shares under share option schemes	–	7	–	–	–	–	–	7	–	7
Buyback of equity	–	–	–	–	–	–	–	–	–	–
Purchase of treasury shares	–	–	(52)	–	–	–	–	(52)	–	(52)
Release of treasury shares	–	–	61	–	–	–	(61)	–	–	–
Dividends	–	–	–	–	–	–	(147)	(147)	(1)	(148)
At 31 December 2019	195	2,614	(24)	11	39	567	911	4,313	10	4,323

The capital redemption reserve reflects the nominal value of shares cancelled in the Group's share buyback programme. The fair value reserve arises on revaluation of other financial assets. 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 cash flow statement

Year ended 31 December 2020

All figures in £ millions	Notes	2020	2019
Cash flows from operating activities			
Net cash generated from operations	33	**450**	480
Interest paid		**(63)**	(81)
Tax received/(paid)		**2**	(30)
Net cash generated from operating activities		**389**	369
Cash flows from investing activities			
Acquisition of subsidiaries, net of cash acquired	30	**(6)**	(45)
Additional capital invested in associates		**–**	(40)
Purchase of investments		**(6)**	(12)
Purchase of property, plant and equipment		**(53)**	(55)
Purchase of intangible assets		**(81)**	(138)
Disposal of subsidiaries, net of cash disposed	31	**100**	(101)
Proceeds from sale of joint ventures and associates	31	**531**	–
Proceeds from sale of investments		**–**	5
Proceeds from sale of property, plant and equipment		**–**	1
Lease receivables repaid including disposals		**41**	26
Loans repaid by/(advanced to) related parties		**48**	(49)
Interest received		**13**	17
Investment income		**–**	2
Dividends from joint ventures and associates		**4**	64
Net cash generated from/(used in) investing activities		**591**	(325)
Cash flows from financing activities			
Proceeds from issue of ordinary shares	27	**6**	7
Buyback of equity	27	**(176)**	–
Purchase of treasury shares	28	**(6)**	(52)
Proceeds from borrowings		**346**	230
Repayment of borrowings		**(230)**	(48)
Repayment of lease liabilities		**(92)**	(91)
Dividends paid to company's shareholders	9	**(146)**	(147)
Dividends paid to non-controlling interest		**(1)**	(1)
Net cash used in financing activities		**(299)**	(102)
Effects of exchange rate changes on cash and cash equivalents		**(2)**	(33)
Net increase/(decrease) in cash and cash equivalents		**679**	(91)
Cash and cash equivalents at beginning of year		**434**	525
Cash and cash equivalents at end of year	17	**1,113**	434

Notes to the consolidated financial statements

General information

Pearson plc ('the company'), its subsidiaries and associates (together 'the Group') are international businesses covering educational courseware, assessments and services.

The company is a public limited company incorporated and domiciled in England. The address of its registered office is 80 Strand, London WC2R 0RL.

The company has its primary listing on the London Stock Exchange and is also listed on the New York Stock Exchange.

These consolidated financial statements were approved for issue by the Board of Directors on 15 March 2021.

1a. Accounting policies

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below.

Basis of preparation

These consolidated financial statements, and the company financial statements, have been prepared on the going concern basis (see note 1c) and in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006. In addition, the consolidated financial statements have been prepared in accordance with international financial reporting standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union ('EU-adopted IFRS'). The consolidated financial statements have also been prepared in accordance with the International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB). There is no difference between IFRS in conformity with the Companies Act 2006, the EU-adopted IFRS and IASB issued IFRS.

These consolidated financial statements, and the company financial statements, have been prepared under the historical cost convention as modified by the revaluation of financial assets and liabilities (including derivative financial instruments) at fair value.

These accounting policies have been consistently applied to all years presented, unless otherwise stated.

1. Interpretations and amendments to published standards effective 2020 – No new standards were adopted in 2020.

A number of other new pronouncements are effective from 1 January 2020 but they do not have a material impact on the consolidated financial statements, or the company financial statements. Additional disclosure has been given where relevant. See note 1b for details on the early adoption of amendments to IFRS 16 'Leases'.

2. Standards, interpretations and amendments to published standards that are not yet effective – A number of other new standards and amendments to standards and interpretations are effective for annual periods beginning after 1 January 2021, and have not been applied in preparing these financial statements. None of these is expected to have a material impact on the consolidated financial statements, or the company financial statements.

3. Critical accounting assumptions and judgements – The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting assumptions and estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies.

All assumptions and estimates constitute management's best judgement at the date of the financial statements, however, in the future, actual experience may deviate from these estimates and assumptions.

The areas requiring a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are:

› Intangible assets: Goodwill
› Intangible assets: Pre-publication assets
› Taxation
› Revenue: Provisions for returns
› Employee benefits: Pensions

The valuation of the other receivable which arose on the disposal of the US K-12 business is no longer considered to be an area of key judgement and estimation due to repayments received during 2020.

They key judgements and key areas of estimation are set out below, as well as in the relevant accounting policies and in the notes to the accounts where appropriate.

KJ Key judgements

› The application of tax legislation in relation to provisions for uncertain tax positions (see notes 7 and 34).

› Whether the Group will be eligible to receive the surplus associated with the UK Group Pension Plan in recognising a pension asset (see note 25).

KE Key areas of estimation

› The recoverability of goodwill balances. Key assumptions used in goodwill impairment testing are discount rates, perpetuity growth rates, forecast sales growth rates and forecast operating profits. See note 11 for further details.

› The recoverability of prepublication assets and in particular the assessment of the useful economic lives of pre-publication assets. The key assumption is the estimate of future potential sales. See note 20 for further details.

› The level of provisions required in relation to uncertain tax positions is complex and each matter is separately assessed. The estimation of future settlement amounts is based on a number of factors including the status of the unresolved matter, clarity of legislation, range of possible outcomes and the statute of limitations. See notes 7 and 34 for further details.

› The level of provisions required for anticipated returns is estimated based on historical experiences, customer buying patterns and retailer behaviours including stock levels. See note 3 for further details.

› The determination of the pension cost and defined benefit obligation of the Group's defined benefit pension schemes depends on the selection of certain assumptions, which include the discount rate, inflation rate, salary growth and longevity. See note 25 for further details.

Notes to the consolidated financial statements

1a. Accounting policies continued

Basis of preparation continued

The Group has assessed the impact of the uncertainty presented by the COVID-19 pandemic on the financial statements, specifically considering the impact on key judgements and significant estimates along with other areas of increased risk as follows:

- Recoverable value of right of use assets and investment in finance lease receivable balances
- Financial instruments in particular counterparty risk and hedge effectiveness
- Working capital provisions including expected credit losses on trade and other debtors and inventory obsolescence

No material accounting impacts relating to the areas assessed above were recognised in the year. The Group will continue to monitor these areas of increased judgement, estimation and risk for material changes.

Consolidation

1. Business combinations – The acquisition method of accounting is used to account for business combinations.

The consideration transferred for the acquisition of a subsidiary is the fair value of the assets transferred, the liabilities incurred and the equity interest issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition-related costs are expensed as incurred in the operating expenses line of the income statement. Identifiable assets acquired and identifiable liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The determination of fair values often requires significant judgements and the use of estimates, and, for material acquisitions, the fair value of the acquired intangible assets is determined by an independent valuer. The excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition date fair value of any previous equity interest in the acquiree over the fair value of the identifiable net assets acquired is recorded as goodwill (see note 30).

See the 'Intangible assets' policy for the accounting policy on goodwill. If this is less than the fair value of the net assets of the subsidiary acquired, in the case of a bargain purchase, the difference is recognised directly in the income statement.

On an acquisition-by-acquisition basis, the Group recognises any non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net assets.

IFRS 3 'Business Combinations' has not been applied retrospectively to business combinations before the date of transition to IFRS.

Management exercises judgement in determining the classification of its investments in its businesses, in line with the following:

2. Subsidiaries – Subsidiaries are entities over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are deconsolidated from the date that control ceases.

3. Transactions with non-controlling interests – Transactions with non-controlling interests that do not result in loss of control are accounted for as equity transactions, that is, as transactions with the owners in their capacity as owners. Any surplus or deficit arising from disposals to a non-controlling interest is recorded in equity. For purchases from a non-controlling interest, the difference between consideration paid and the relevant share acquired of the carrying value of the subsidiary is recorded in equity.

4. Joint ventures and associates – Joint ventures are entities in which the Group holds an interest on a long-term basis and has rights to the net assets through contractually agreed sharing of control. Associates are entities over which the Group has significant influence but not the power to control the financial and operating policies, generally accompanying a shareholding of between 20% and 50% of the voting rights. Ownership percentage is likely to be the key indicator of investment classification; however, other factors, such as Board representation, may also affect the accounting classification. Judgement is required to assess all of the qualitative and quantitative factors which may indicate that the Group does, or does not, have significant influence over an investment. Investments in joint ventures and associates are accounted for by the equity method and are initially recognised at the fair value of consideration transferred.

The Group's share of its joint ventures' and associates' post-acquisition profits or losses is recognised in the income statement and its share of post-acquisition movements in reserves is recognised in reserves.

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.

Unrealised gains and losses on transactions between the Group and its joint ventures and associates are eliminated to the extent of the Group's interest in these entities.

5. Contribution of a subsidiary to an associate or joint venture – The gain or loss resulting from the contribution or sale of a subsidiary to an associate or a joint venture is recognised in full. Where such transactions do not involve cash consideration, significant judgements and estimates are used in determining the fair values of the consideration received.

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.

1a. Accounting policies continued

Foreign currency translation continued

3. Group companies – The results and financial position of all Group companies that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

i) Assets and liabilities are translated at the closing rate at the date of the balance sheet

ii) Income and expenses are translated at average exchange rates

iii) All resulting exchange differences are recognised as a separate component of equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities, and of borrowings and other currency instruments designated as hedges of such investments, are taken to shareholders' equity. The Group treats specific inter-company loan balances, which are not intended to be repaid in the foreseeable future, as part of its net investment. When a foreign operation is sold, such exchange differences are recognised in the income statement as part of the gain or loss on sale.

The principal overseas currency for the Group is the US dollar. The average rate for the year against sterling was $1.28 (2019: $1.28) and the year-end rate was $1.37 (2019: $1.32).

Property, plant and equipment

Property, plant and equipment are stated at historical cost less depreciation. Cost includes the original purchase price of the asset and the costs attributable to bringing the asset to its working condition for intended use. Land is not depreciated. Depreciation on other assets is calculated using the straight-line method to allocate their cost less their residual values over their estimated useful lives as follows:

Buildings (freehold):	20–50 years
Buildings (leasehold):	over the period of the lease
Plant and equipment:	3–10 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

The carrying value of an asset is written down to its recoverable amount if the carrying value of the asset is greater than its estimated recoverable amount.

Intangible assets

1. Goodwill – For the acquisition of subsidiaries made on or after 1 January 2010, goodwill represents the excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition date fair value of any previous equity interest in the acquiree over the fair value of the identifiable net assets acquired. For the acquisition of subsidiaries made from the date of transition to IFRS to 31 December 2009, goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets acquired. Goodwill on acquisitions of subsidiaries is included in intangible assets. Goodwill on acquisition of associates and joint ventures represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets acquired. Goodwill on acquisitions of associates and joint ventures is included in investments in associates and joint ventures.

Goodwill is tested at least annually for impairment and carried at cost less accumulated impairment losses. An impairment loss is recognised to the extent that the carrying value of goodwill exceeds the recoverable amount. The recoverable amount is the higher of fair value less costs of disposal and value in use. These calculations require the use of estimates in respect of forecast cash flows and discount rates and significant management judgement in respect of cash-generating unit (CGU) and cost allocation; impairment is a key source of estimation uncertainty and has a significant risk of resulting in a material adjustment to the carrying amount of relevant assets within the next financial year. A summary of these assets by CGU and a description of the key assumptions and sensitivities is included in note 11.

Goodwill is allocated to aggregated CGUs for the purpose of impairment testing. The allocation is made to those aggregated CGUs 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.

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 ten years.

4. Acquired intangible assets – Acquired intangible assets include customer lists, contracts and relationships, trademarks and brands, publishing rights, content, technology and software rights. These assets are capitalised on acquisition at cost and included in intangible assets. Intangible assets acquired in material business combinations are capitalised at their fair value as determined by an independent valuer. Intangible assets are amortised over their estimated useful lives of between two and 20 years, using an amortisation method that reflects the pattern of their consumption.

5. Pre-publication assets – Pre-publication assets represent direct costs incurred in the development of educational programmes and titles prior to their publication. These costs are recognised as current intangible assets where the title will generate probable future economic benefits and costs can be measured reliably.

Pre-publication assets relating to content are amortised upon publication of the title over estimated economic lives of 7 years or less, being an estimate of the expected operating lifecycle of the title, with a higher proportion of the amortisation taken in the earlier years. Pre-publication assets relating to product platforms are amortised over ten years or less being an estimate of the expected useful life.

Notes to the consolidated financial statements

1a. Accounting policies continued

Intangible assets continued

The assessment of the useful economic life and the recoverability of pre-publication assets involves 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.

Pre-publication assets are assessed for impairment triggers on an annual basis or when triggering events occur. The carrying amount of pre-publication assets is set out in note 20.

The investment in pre-publication assets has been disclosed as part of cash generated from operations in the cash flow statement (see note 33).

Other financial assets

Other financial assets are non-derivative financial assets classified and measured at estimated fair value.

Marketable securities and cash deposits with maturities of greater than three months are classified and subsequently measured at fair value through profit and loss.

They are remeasured at each balance sheet date by using market data and the use of established valuation techniques. Any movement in the fair value is immediately recognised in finance income or finance costs in the income statement.

Investments in the equity instruments of other entities are classified and subsequently measured at fair value through other comprehensive income. Changes in fair value are recorded in equity in the fair value reserve via other comprehensive income. On subsequent disposal of the asset, the net fair value gains or losses are reclassified from the fair value reserve to retained earnings. Any dividends received from equity investments classified as fair value through other comprehensive income are recognised in the income statement unless they represent a return of capital.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the weighted average method or an approximation thereof, such as 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.

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 estimation 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.

Cash and cash equivalents

Cash and cash equivalents in the cash flow statement include cash in hand, deposits held on call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts. Bank overdrafts are included in borrowings in current liabilities in the balance sheet.

Short-term deposits and marketable securities with maturities of greater than three months do not qualify as cash and cash equivalents and are reported as financial assets. Movements on these financial assets are classified as cash flows from financing activities in the cash flow statement where these amounts are used to offset the borrowings of the Group or as cash flows from investing activities where these amounts are held to generate an investment return.

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.

Ordinary shares purchased under a buyback programme are cancelled and the nominal value of the shares is transferred to a capital redemption reserve.

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.

Where a debt instrument is in a net investment hedge relationship gains and losses on the effective portion of the hedge are recognised in other comprehensive income.

1a. Accounting policies continued

Derivative financial instruments

Derivatives are recognised at fair value and remeasured at each balance sheet date. The fair value of derivatives is determined by using market data and the use of established estimation techniques such as discounted cash flow and option valuation models.

For derivatives in a hedge relationship, the currency basis spread is excluded from the designation as a hedging instrument.

Changes in the fair value of derivatives are recognised immediately in finance income or costs. However, derivatives relating to borrowings and certain foreign exchange contracts are designated as part of a hedging transaction.

The accounting treatment is summarised as follows:

Typical reason for designation	Reporting of gains and losses on effective portion of the hedge	Reporting of gains and losses on disposal
Net investment hedge		
The derivative creates a foreign currency liability which is used to hedge changes in the value of a subsidiary which transacts in that currency.	Recognised in other comprehensive income.	On disposal, the accumulated value of gains and losses reported in other comprehensive income is transferred to the income statement.
Fair value hedges		
The derivative transforms the interest profile on debt from fixed rate to floating rate. Changes in the value of the debt as a result of changes in interest rates and foreign exchange rates are offset by equal and opposite changes in the value of the derivative. When the Group's debt is swapped to floating rates, the contracts used are designated as fair value hedges.	Gains and losses on the derivative are reported in finance income or finance costs. However, an equal and opposite change is made to the carrying value of the debt (a 'fair value adjustment') with the benefit/cost reported in finance income or finance costs. The net result should be a zero charge on a perfectly effective hedge.	If the debt and derivative are disposed of, the value of the derivative and the debt (including the fair value adjustment) are reset to zero. Any resultant gain or loss is recognised in finance income or finance costs.
Non-hedge accounted contracts		
These are not designated as hedging instruments. Typically, these are short-term contracts to convert debt back to fixed rates or foreign exchange contracts where a natural offset exists.	No hedge accounting applies.	

Taxation

Current tax is recognised at 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 balance sheet 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, associates and joint ventures other than where it is intended that those undistributed earnings will not be remitted in the foreseeable future.

Current and deferred tax are recognised in the income statement, except when the tax relates to items charged or credited directly to equity or other comprehensive income, in which case the tax is also recognised in equity or other comprehensive income.

The Group is subject to income taxes in numerous jurisdictions. Significant judgement is required in determining the estimates in relation to the worldwide provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Group recognises tax provisions when it is considered probable that there will be a future outflow of funds to a tax authority. The provisions are based on management's best judgement of the application of tax legislation and best estimates of future settlement amounts (see note 7). 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 and estimation in determining the amounts to be recognised. In particular, when assessing the extent to which deferred tax assets should be recognised, significant judgement is used when considering the timing of the recognition and estimation is used to determine the level of future taxable income together with any future tax planning strategies (see note 13).

Employee benefits

1. Pensions – The retirement benefit asset and obligation recognised in the balance sheet represent the net of the present value of the defined benefit obligation and the fair value of plan assets at the balance sheet date. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting estimated future cash flows using yields on high-quality corporate bonds which have terms to maturity approximating the terms of the related liability.

When the calculation results in a potential asset, the recognition of that asset is limited to the asset ceiling – that is the present value of any economic benefits available in the form of refunds from the plan or a reduction in future contributions. Management uses judgement to determine the level of refunds available from the plan in recognising an asset.

The determination of the pension cost and defined benefit obligation of the Group's defined benefit pension schemes depends on the selection of certain assumptions, which include the discount rate, inflation rate, salary growth and longevity (see note 25).

Notes to the consolidated financial statements

1a. Accounting policies continued

Employee benefits continued

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to equity in other comprehensive income in the period in which they arise. The service cost, representing benefits accruing over the year, is included in the income statement as an operating cost. Net interest is calculated by applying the discount rate to the net defined benefit obligation and is presented as finance costs or finance income.

Obligations for contributions to defined contribution pension plans are recognised as an operating expense in the income statement as incurred.

2. Other post-retirement obligations – The expected costs of post-retirement medical and life assurance benefits are accrued over the period of employment, using a similar accounting methodology as for defined benefit pension obligations. The liabilities and costs relating to significant other post-retirement obligations are assessed annually by independent qualified actuaries.

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.

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.

Revenue recognition

The Group's revenue streams are courseware, assessments and services. Courseware includes curriculum materials provided in book form and/or via access to digital content. Assessments includes test development, processing and scoring services provided to governments, educational institutions, corporations and professional bodies. Services includes the operation of schools, colleges and universities, including sistemas G in Brazil, as well as the provision of online learning services in partnership with universities and other academic institutions.

Revenue is recognised in order to depict the transfer of control of promised goods and services to customers in an amount that reflects the consideration to which we expect to be entitled in exchange for those goods and services. This process begins with the identification of our contract with a customer, which is generally through a master services agreement, customer purchase order, or a combination thereof. Within each contract, judgement is applied to determine the extent to which activities within the contract represent distinct performance obligations to be delivered and the total amount of transaction price to which we expect to be entitled.

The transaction price determined is net of sales taxes, rebates and discounts, and after eliminating sales within the Group. Where a contract contains multiple performance obligations such as the provision of supplementary materials or online access with textbooks, revenue is allocated on the basis of relative standalone selling prices. Where a contract contains variable consideration, significant estimation is required to determine the amount to which the Group is expected to be entitled.

Revenue is recognised on contracts with customers when or as performance obligations are satisfied which is the period or the point in time where control of goods or services transfers to the customer. Judgement is applied to determine first whether control passes over time and if not, then the point in time at which control passes. Where revenue is recognised over time judgement is used to determine the method which best depicts the transfer of control. Where an input method is used significant estimation is required to determine the progress towards delivering the performance obligation.

Revenue from the sale of books is recognised net of a provision for anticipated returns. This provision is based primarily on historical return rates, customer buying patterns and retailer behaviours including stock levels (see note 24). If these estimates do not reflect actual returns in future periods then revenues could be understated or overstated for a particular period. When the provision for returns is remeasured at each reporting date to reflect changes in estimates, a corresponding adjustment is also recorded to revenue.

The Group may enter into contracts with another party in addition to our customer. In making the determination as to whether revenue should be recognised on a gross or net basis, the contract with the customer is analysed to understand which party controls the relevant good or service prior to transferring to the customer. This judgement is informed by facts and circumstances of the contract in determining whether the Group has promised to provide the specified good or service or whether the Group is arranging for the transfer of the specified good or service, including which party is responsible for fulfilment, has discretion to set the price to the customer and is responsible for inventory risk. On certain contracts, where the Group acts as an 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.

Additional details on the Group's revenue streams are also included in note 3.

Leases

The Group as a lessee

The Group assesses whether a contract is or contains a lease at the inception of the contract. A contract is, or contains a lease, if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. The Group recognises a right-of-use asset and a lease liability at the lease commencement date with respect to all lease arrangements except for short-term leases (leases with a lease term of 12 months or less) and leases of low value assets. For these leases, the lease payments are recognised as an operating expense on a straight-line basis over the term of the lease.

1a. Accounting policies continued

Leases continued

The right-of-use asset is initially measured at cost, comprising the initial amount of the lease liability plus any initial direct costs incurred and an estimate of costs to restore the underlying asset, less any lease incentives received. The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the earlier of the end of the useful life of the asset or the end of the lease term. The Group applies IAS 36 to determine whether a right-of-use asset is impaired. The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the incremental borrowing rate. The lease liability is measured at amortised cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in an index or a rate or a change in the Group's assessment of whether it will exercise an extension or termination option. When the lease liability is remeasured, a corresponding adjustment is made to the right-of-use asset.

Management uses judgement to determine the lease term where extension and termination options are available within the lease.

The Group as a lessor

When the Group is an intermediate lessor, the head lease and sub-lease are accounted for as two separate contracts. The head lease is accounted for as per the lessee policy above. The sub-lease is classified as a finance lease or operating lease by reference to the right-of-use asset arising from the head lease. Where the lease transfers substantially all the risks and rewards of ownership to the lessee the contract is classified as a finance lease; all other leases are classified as operating leases. Rental income from operating leases is recognised on a straight-line basis over the term of the relevant lease. Amounts due from lessees under finance sub-leases are recognised as receivables at the amount of the Group's net investment in the leases discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the discount rate used in the head lease.

Dividends

Final 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 when paid.

Discontinued operations

A discontinued operation is a component of the Group's business that represents a separate major line of business or geographical area of operations that has been disposed of or meets the criteria to be classified as held for sale.

When applicable, discontinued operations are presented in the income statement as a separate line and are shown net of tax.

Assets and liabilities held for sale

Assets and liabilities are classified as held for sale and stated at the lower of carrying amount and fair value less costs to sell if it is highly probable that the carrying amount will be recovered principally through a sale transaction rather than through continuing use. No depreciation is charged in respect of non-current assets classified as held for sale. Amounts relating to non-current assets and liabilities held for sale are classified as discontinued operations in the income statement where appropriate.

Trade receivables

Trade receivables are stated at fair value after provision for bad and doubtful debts. Provisions for bad and doubtful debts are based on the expected credit loss model. The 'simplified approach' is used with the expected loss allowance measured at an amount equal to the lifetime expected credit losses. A provision for anticipated future sales returns is included within trade and other liabilities (also see Revenue recognition policy).

1b. Change of accounting policy: Amendment to IFRS 16

The Group early adopted COVID-19 Related Rent Concessions – Amendment to IFRS 16, issued on 28 May 2020. The amendment introduces an optional practical expedient for leases in which the Group is a lessee. For leases to which the Group applies the amendment, the Group is not required to assess whether eligible rent concessions that are a direct consequence of the COVID-19 pandemic are lease modifications. The Group has applied the amendment retrospectively to all rent concessions that meet the conditions in the amendment. The amendment has no impact on retained earnings at 1 January 2020. The eligible rent concessions granted to the Group have no material impact on the Group's financial statements.

1c. Going concern

In assessing the Group's ability to continue as a going concern for the period to 30 June 2022, the board analysed a variety of downside scenarios including a severe but plausible scenario where the Group is impacted by all principal risks from 2021 (weighted for probability of occurrence) as well as reverse stress testing to identify what would be required to either breach covenants or run out of liquidity. The severe but plausible scenario modelled a severe reduction in revenue, profit and operating cash flow from COVID-19 and other risks which in aggregate were significantly greater than seen in 2020 continuing throughout 2021 to 2022.

At 31 December 2020, the Group had available liquidity of c£1.9bn, comprising central cash balances and its undrawn $1.19bn Revolving Credit Facility (RCF) maturing February 2024. Even under a severe downside case where further declines in profitability compared to 2020 are modelled in 2021 and 2022, the Group would maintain liquidity headroom in excess of £800m and sufficient headroom against covenant requirements during the period under assessment even before modelling the mitigating effect of actions that management would take in the event that these downside risks were to crystallise.

The directors have confirmed that there are no material uncertainties that cast doubt on the Group's going concern status and that they have a reasonable expectation that the Group has adequate resources to continue in operational existence for a minimum of the next 12 months.

Notes to the consolidated financial statements

2. Segment information

From 1 January 2020, the Group has reorganised and is reporting for the first time new segmental analyses to reflect the new management structure and operating model. The primary segments for management and reporting purposes are Global Online Learning, Global Assessment, North American Courseware and International. The Group separately reports the costs of Enabling Functions such as enterprise technology, finance, human resources and other corporate functions. In addition, the Group has separately disclosed the results from the Penguin Random House associate to the point of disposal in April 2020. Comparative figures for 2019 have been restated to reflect the new segments.

The chief operating decision-maker is the Pearson Executive Management team.

Global Online Learning – Virtual Schools and Online Program Management.

Global Assessment – Pearson VUE, US Student Assessment and Clinical Assessment.

North American Courseware – Courseware and services businesses in the US and Canada.

International – Courseware and other businesses outside North America and including UK Qualifications and English.

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

								2020
All figures in £ millions	**Notes**	**Global Online Learning**	**Global Assessment**	**North American Courseware**	**International**	**Enabling Functions**	**Penguin Random House**	**Group**
Sales	3	**697**	**892**	**894**	**914**	**–**	**–**	**3,397**
Adjusted operating profit		**99**	**245**	**190**	**182**	**(404)**	**1**	**313**
Cost of major restructuring		**–**	**–**	**–**	**–**	**–**	**–**	**–**
Intangible charges		**(29)**	**(36)**	**–**	**(15)**	**–**	**–**	**(80)**
Other net gains and losses		**–**	**–**	**3**	**(5)**	**–**	**180**	**178**
Operating profit/(loss)		**70**	**209**	**193**	**162**	**(404)**	**181**	**411**
Finance costs	6							**(107)**
Finance income	6							**50**
Profit before tax								**354**
Income tax	7							**(44)**
Profit for the year								**310**
Other segment items								
Share of results of joint ventures and associates	12	**–**	**–**	**–**	**4**	**–**	**1**	**5**
Depreciation	10	**12**	**39**	**28**	**39**	**7**	**–**	**125**
Amortisation	11, 20	**56**	**111**	**175**	**77**	**53**	**–**	**472**

2. Segment information continued

All figures in £ millions	Notes	Global Online Learning	Global Assessment	North American Courseware	International	Enabling Functions	Penguin Random House	Group
								2019
Sales	3	586	1,031	1,091	1,161	–	–	3,869
Adjusted operating profit		84	351	231	299	(449)	65	581
Cost of major restructuring		–	(7)	(51)	(24)	(75)	(2)	(159)
Intangible charges		(35)	(27)	–	(89)	–	(12)	(163)
Other net gains and losses		–	–	13	3	–	–	16
Operating profit/(loss)		49	317	193	189	(524)	51	275
Finance costs	6							(84)
Finance income	6							41
Profit before tax								232
Income tax	7							34
Profit for the year								266
Other segment items								
Share of results of joint ventures and associates	12	–	–	–	3	–	51	54
Depreciation	10	11	38	32	42	–	–	123
Amortisation	11, 20	55	94	187	144	57	–	537

There were no material inter-segment sales in either 2020 or 2019.

Corporate costs are allocated to business segments on an appropriate basis depending on the nature of the cost and therefore the total segment result is equal to the Group operating profit.

For additional detailed information on the calculation of adjusted operating profit as shown in the above tables, see pp212–216 (Financial key performance indicators).

Adjusted operating profit is shown in the above tables as it is the key financial measure used by management to evaluate the performance of the Group and allocate resources to business segments. The measure also enables investors to more easily, and consistently, track the underlying operational performance of the Group and its business segments over time by separating out those items of income and expenditure relating to acquisition and disposal transactions, major restructuring programmes and certain other items that are also not representative of underlying performance, which are explained below and reconciled in note 8.

Cost of major restructuring – In May 2017, the Group announced a restructuring programme, to run between 2017 and 2019, to drive significant cost savings. This programme began in the second half of 2017 and costs incurred relate to delivery of cost efficiencies in the US Higher Education Courseware business and enabling functions together with further rationalisation of the property and supplier portfolio. The restructuring costs in 2019 of £159m relate predominantly to staff redundancies. The costs of this restructuring programme are significant enough to exclude from the adjusted operating profit measure so as to better highlight the underlying performance (see note 4).

Intangible charges – These represent charges relating to acquired intangibles, acquisition costs and movements in contingent acquisition and disposal consideration. These charges are excluded as they reflect past acquisition activity and do not necessarily reflect the current year performance of the Group. Intangible amortisation charges in 2020 were £80m including impairment charges of £12m. In 2019, intangible charges were £163m including impairment charges of £65m.

Other net gains and losses – These represent profits and losses on the sale of subsidiaries, joint ventures, associates and other financial assets and are excluded from adjusted operating profit as they distort the performance of the Group as reported on a statutory basis. Other net gains in 2020 largely relate to the sale of the remaining interest in Penguin Random House (£180m gain) and impairments of assets and other costs relating to the disposal of Pearson Institute of Higher Education (£8m loss). In 2019, other net gains largely relate to the sale of the US K-12 business.

Notes to the consolidated financial statements

2. Segment information continued

The Group operates in the following main geographic areas:

All figures in £ millions	Sales 2020	Sales 2019	Non-current assets 2020	Non-current assets 2019
UK	**319**	385	**669**	694
Other European countries	**216**	244	**129**	125
US	**2,335**	2,417	**2,362**	2,604
Canada	**91**	105	**147**	163
Asia Pacific	**251**	441	**149**	149
Other countries	**185**	277	**30**	103
Total	**3,397**	3,869	**3,486**	3,838

Sales are allocated based on the country in which the customer is located. This does not differ materially from the location where the order is received. The geographical split of non-current assets is based on the subsidiary's country of domicile. This is not materially different to the location of the assets. Non-current assets comprise property, plant and equipment, intangible assets, investments in joint ventures and associates and trade and other receivables.

3. Revenue from contracts with customers

The following tables analyse the Group's revenue streams. Courseware includes curriculum materials provided in book form and/or via access to digital content. Assessments includes integrated test development, processing and scoring services provided to governments, educational institutions, corporations and professional bodies. Services includes the operation of schools, colleges and universities, including sistemas in Brazil, as well as the provision of online learning services in partnership with universities and other academic institutions. Comparative figures for 2019 have been restated to reflect the new segments.

					2020
All figures in £ millions	Global Online Learning	Global Assessment	North American Courseware	International	Group
Sales:					
Courseware					
School Courseware	–	–	29	247	276
Higher Education Courseware	–	–	853	105	958
English Courseware[1]	–	–	–	132	132
	–	–	882	484	1,366
Assessments					
School and Higher Education Assessments	–	255	–	218	473
Clinical Assessments	–	146	–	48	194
Professional and English Certification	–	491	–	61	552
	–	892	–	327	1,219
Services					
School Services	413	–	–	29	442
Higher Education Services	284	–	12	50	346
English Services	–	–	–	24	24
	697	–	12	103	812
Total	697	892	894	914	3,397

1 English Courseware within North American Courseware was transferred to the International segment in 2020.

3. Revenue from contracts with customers continued

All figures in £ millions	Global Online Learning	Global Assessment	North American Courseware	International	2019 Group
Sales:					
Courseware					
School Courseware	–	–	86	287	373
Higher Education Courseware	–	–	975	125	1,100
English Courseware	–	–	14	163	177
	–	–	1,075	575	1,650
Assessments					
School and Higher Education Assessments	–	309	–	290	599
Clinical Assessments	–	175	–	52	227
Professional and English Certification	–	547	–	91	638
	–	1,031	–	433	1,464
Services					
School Services	319	–	–	48	367
Higher Education Services	267	–	16	54	337
English Services	–	–	–	51	51
	586	–	16	153	755
Total	586	1,031	1,091	1,161	3,869

The Group derived revenue from the transfer of goods and services over time and at a point in time in the following major product lines:

All figures in £ millions	Global Online Learning	Global Assessment	North American Courseware	International	2020 Total
Courseware[1]					
Products transferred at a point in time	–	–	261	409	670
Products and services transferred over time	–	–	621	75	696
	–	–	882	484	1,366
Assessments					
Products transferred at a point in time	–	96	–	52	148
Products and services transferred over time	–	796	–	275	1,071
	–	892	–	327	1,219
Services					
Products transferred at a point in time	–	–	–	44	44
Products and services transferred over time	697	–	12	59	768
	697	–	12	103	812
Total	697	892	894	914	3,397

Notes to the consolidated financial statements

3. Revenue from contracts with customers continued

All figures in £ millions	Global Online Learning	Global Assessment	North American Courseware	International	Total
					2019
Courseware[1]					
Products transferred at a point in time	–	–	448	506	954
Products and services transferred over time	–	–	627	69	696
	–	–	1,075	575	1,650
Assessments					
Products transferred at a point in time	–	113	–	61	174
Products and services transferred over time	–	918	–	372	1,290
	–	1,031	–	433	1,464
Services[2]					
Products transferred at a point in time	–	–	–	86	86
Products and services transferred over time	586	–	16	67	669
	586	–	16	153	755
Total	586	1,031	1,091	1,161	3,869

1 Previous classifications within Courseware of 'Point in Time (Sale or Return)' and 'Point in time (other)' have been combined in both 2020 and 2019 as these two categories contained similar types of customers, risks and obligations.

2 2019 International revenue split between 'Services Over Time' to 'Services Point in Time' restated by £60m primarily due to a change in classification of certain revenues within the Brazilian Sistemas Franchise business.

a. Nature of goods and services

The following is a description of the nature of the Group's performance obligations within contracts with customers broken down by revenue stream, along with significant judgements and estimates made within each of those revenue streams.

Courseware

KE Key areas of estimation

› The level of provisions required for anticipated returns is estimated based on historical experiences, customer buying patterns and retailer behaviours including stock levels.

Revenue is generated from customers through the sales of print and digital courseware materials to schools, bookstores and direct to individual learners. Goods and services may be sold separately or purchased together in bundled packages. The goods and services included in bundled arrangements are considered distinct performance obligations, except for where Pearson provides both a licence of intellectual property and an ongoing hosting service. As the licence of intellectual property is only available with the concurrent hosting service, the licence is not treated as a distinct performance obligation separate from the hosting service.

The transaction price is allocated between distinct performance obligations on the basis of their relative standalone selling prices.

In determining the transaction price, variable consideration exists in the form of discounts and anticipated returns. Discounts reduce the transaction price on a given transaction. A provision for anticipated returns is made based primarily on historical return rates, customer buying patterns and retailer behaviours including stock levels (see note 24). If these estimates do not reflect actual returns in future periods then revenues could be understated or overstated for a particular period. Variable consideration as described above is determined using the expected value approach. The sales return liability at the end of 2020 was £86m (2019: £122m) (see note 24). This represents 2% of annual sales subject to sale or return.

While payment for these goods and services generally occurs at the start of these arrangements, the length of time between payment and delivery of the performance obligations is generally short-term in nature or the reason for early payment relates to reasons other than financing, including customers securing a vendor in a longer-term arrangement or the transfer of goods or services is at the discretion of the customer. For these reasons and the use of the practical expedient on short-term financing, significant financing components are not recognised within Courseware transactions.

Revenue from the sale of physical books is recognised at a point in time when control passes. This is generally at the point of shipment when title passes to the customer, when the Group has a present right to payment and the significant risks and rewards of ownership have passed to the customer. Revenue from physical books sold through the direct print rental method is recognised over the rental period, as the customer is simultaneously receiving and consuming the benefits of this rental service through the passage of time.

Revenue from the sale of digital courseware products is recognised on a straight-line basis over the subscription period, unless hosted by a third party or representative of a downloadable product, in which case Pearson has no ongoing obligation and recognises revenue when control transfers as the customer is granted access to the digital product.

Revenue from the sale of 'off-the-shelf' software is recognised on delivery or on installation of the software where that is a condition of the contract. In certain circumstances, where installation is complex, revenue is recognised when the customer has completed their acceptance procedures.

Assessments

Revenue is primarily generated from multi-year contractual arrangements related to large-scale assessment delivery, such as contracts to process qualifying tests for individual professions and government departments, and is recognised as performance occurs. Under these arrangements, while the agreement spans multiple years, the contract duration has been determined to be each testing cycle based on contract structure, including clauses regarding termination.

3. Revenue from contracts with customers continued

a. Nature of goods and services continued

While in some cases the customer may have the ability to terminate during the term for convenience, significant financial or qualitative barriers exist limiting the potential for such terminations in the middle of a testing cycle.

Within each testing cycle, a variety of service activities are performed such as test administration, delivery, scoring, reporting, item development, operational services and programme management. These services are not treated as distinct in the context of the customer contract as Pearson provides an integrated managed service offering and these activities are accounted for together as one comprehensive performance obligation.

Within each testing cycle, the transaction price may contain both fixed and variable amounts. Variable consideration within these transactions primarily relates to expected testing volumes to be delivered in the cycle. The assumptions, risks and uncertainties inherent to long-term contract accounting can affect the amounts and timing of revenue and related expenses reported. Variable consideration is measured using the expected value method, except where amounts are contingent upon a future event's occurrence, such as performance bonuses. Such event-driven contingency payments are measured using the most likely amount approach. In estimating and constraining variable consideration; historical experiences, current trends and local market conditions are considered. To the extent that a higher degree of uncertainty exists regarding variable consideration, these amounts are excluded from the transaction price and recognised when the uncertainty is reasonably removed.

Customer payments are generally defined in the contract through a payment schedule, which may require customer acceptance for services rendered. Pearson has a history of providing satisfactory services which are accepted by the customer. While a delay between rendering of services and payment may exist, payment terms are within 12 months and the Group has elected to use the practical expedient available in IFRS 15 'Revenue from Contracts with Customers' and not identify a significant financing component on these transactions.

Revenue is recognised for Assessment contracts over time as the customer is benefiting as performance takes place through a continuous transfer of control to the customer. This continuous transfer of control to the customer is supported by clauses in the contracts which may allow the customer to terminate for convenience, compensate us for work performed to date, and take possession of work in process.

As control transfers over time, revenue is recognised based on the extent of progress towards completion of the performance obligation. The selection of the method to measure progress towards completion requires judgement and is based on the nature of the services provided. Revenue is recognised on a percentage completion basis, calculated using the proportion of the total estimated costs incurred to date. Percentage of completion is used to recognise the transfer of control of services provided as these services are not provided evenly throughout the testing cycle and involve varying degrees of effort during the term.

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.

In Assessments contracts driven primarily by transactions directly to end users, Pearson's main obligation to the customer involves test delivery and scoring. Test delivery and scoring are defined as a single performance obligation delivered over time whether the test is subsequently manually scored or digitally scored on the day of the assessment. Customers may also purchase print and digital supplemental materials. Print products in this revenue stream are recognised at a point in time when control passes to the customer upon shipment. Recognition of digital revenue will occur based on the extent of Pearson's ongoing hosting obligation.

Services

Revenue is primarily generated from multi-year contractual arrangements related to large-scale educational service delivery to academic institutions, such as schools and higher education universities. Under these arrangements, while an agreement may span multiple years, the contract duration has been determined to be each academic period based on the structure of contracts, including clauses regarding termination. While in some cases the customer may have the ability to terminate during the term for convenience, significant financial or qualitative barriers exist limiting the potential for such terminations in the middle of an academic period. The academic period for this customer base is normally an academic year for schools and a semester for higher education universities.

Within each academic period, a variety of services are provided such as programme development, student acquisition, education technology and student support services. These services are not distinct in the context of the customer contract as Pearson provides an integrated managed service offering and these activities are accounted for together as a comprehensive performance obligation.

Where Services are provided to university customers, volume and transaction price are fixed at the start of the semester. Where Services are provided to school customers, the transaction price may contain both fixed and variable amounts which require estimation during the academic period. Estimation is required where consideration is based upon average enrolments or other metrics which are not known at the start of the academic year. Variable consideration is measured using the expected value method. Historical experience, current trends, local circumstances and customer-specific funding formulas are considered in estimating and constraining variable consideration. To the extent that a higher degree of uncertainty exists regarding variable consideration, these amounts are excluded from the transaction price and recognised when the uncertainty is reasonably removed.

Customer payments are generally defined in the contract as occurring shortly after invoicing. Where there is a longer payment term offered to a customer through a payment schedule, payment terms are within 12 months and the Group has elected to use the practical expedient available in IFRS 15 and not identify a significant financing component on these transactions.

Revenue is recognised for Service contracts over time as the customer is benefiting as performance takes place through a continuous transfer of control to the customer. This continuous transfer of control to the customer is supported by clauses in the contracts which may allow the customer to terminate for convenience, compensate for work performed to date, and take possession of work in process.

Notes to the consolidated financial statements

3. Revenue from contracts with customers continued

a. Nature of goods and services continued

As control transfers over time, revenue is recognised based on the extent of progress towards completion of the performance obligation. The selection of the method to measure progress towards completion requires judgement and is based on the nature of the products or services provided. Within the comprehensive service obligation, the timing of services occurs relatively evenly over each academic period and, as such, time elapsed is used to recognise the transfer of control to the customer on a straight-line 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.

In cases of optional or add-on purchases, institutions may purchase physical goods priced at their standalone value, which are accounted for separately and recognised at the point in time when control passes to the customer upon shipment.

b. Disaggregation of revenue

The tables in notes 2 and 3 show revenue from contracts with customers disaggregated by operating segment, geography and revenue stream. These disaggregation categories are appropriate as they represent the key groupings used in managing and evaluating underlying performance of each of the businesses. The categories also reflect groups of similar types of transactional characteristics, among similar customers, with similar accounting conclusions.

c. Contract balances

Transactions within the Courseware revenue stream generally entail customer billings at or near the contract's inception and accordingly Courseware deferred income balances are primarily related to subscription performance obligations to be delivered over time.

Transactions within the Assessments and Services revenue streams generally entail customer billings over time based on periodic intervals, progress towards milestones or enrolment census dates. As the performance obligations within these arrangements are delivered over time, the extent of accrued income or deferred income will ultimately depend upon the difference between revenue recognised and billings to date.

Refer to note 22 for opening and closing balances of accrued income. Refer to note 24 for opening and closing balances of deferred income. Revenue recognised during the period from changes in deferred income was driven primarily by the release of revenue over time from digital subscriptions.

d. Contract costs

The Group capitalises incremental costs to obtain contracts with customers where it is expected these costs will be recoverable. Incremental costs to obtain contracts with customers are considered those which would not have been incurred if the contract had not been obtained. For the Group, these costs relate primarily to sales commissions. The Group has elected to use the practical expedient as allowable by IFRS 15 whereby such costs will be expensed as incurred where the expected amortisation period is one year or less. Where the amortisation period is greater than one year, these costs are amortised over the contract term on a systematic basis consistent with the transfer of the underlying goods and services within the contract to which these costs relate, which will generally be on a ratable basis.

The Group does not recognise any material costs to fulfil contracts with customers as these types of activities are governed by other accounting standards.

There were no deferred contract costs in 2020 or 2019.

e. Remaining transaction price

The below table depicts the remaining transaction price on unsatisfied or partially unsatisfied performance obligations from contracts with customers.

							2020
All figures in £ millions	**Sales**	**Deferred income**	**Committed sales**	**Total remaining transaction price**	**2021**	**2022**	**2023 and later**
Courseware							
Products transferred at a point in time	670	–	–	–	–	–	–
Products and services transferred over time	696	105	14	119	84	14	21
Assessments							
Products transferred at a point in time	148	1	–	1	1	–	–
Products and services transferred over time	1,071	217	413	630	426	203	1
Services							
Products transferred at a point in time	44	–	–	–	–	–	–
Products and services transferred over time – subscriptions	323	18	10	28	27	1	–
Products and services transferred over time – other ongoing performance obligations	445	18	195	213	213	–	–
Total	3,397	359	632	991	751	218	22

3. Revenue from contracts with customers continued

e. Remaining transaction price continued

							2019
All figures in £ millions	Sales	Deferred income	Committed sales	Total remaining transaction price	2020	2021	2022 and later
Courseware							
Products transferred at a point in time	954	2	–	2	2	–	–
Products and services transferred over time	696	118	–	118	82	13	23
Assessments							
Products transferred at a point in time	174	–	–	–	–	–	–
Products and services transferred over time	1,290	206	375	581	433	146	2
Services[1]							
Products transferred at a point in time	86	2	–	2	2	–	–
Products and services transferred over time – subscriptions	310	11	–	11	11	–	–
Products and services transferred over time – other ongoing performance obligations	359	21	106	127	126	1	–
Total	3,869	360	481	841	656	160	25

1 2019 International revenue split between 'Services Over Time' to 'Services Point in Time' restated by £60m primarily due to a change in classification of certain revenues within the Brazilian Sistemas Franchise business.

Committed sales amounts are equal to the transaction price from contracts with customers, excluding those amounts previously recognised as revenue and amounts currently recognised in deferred income. The total of committed sales and deferred income is equal to the remaining transaction price. Time bands stated above represent the expected timing of when the remaining transaction price will be recognised as revenue.

4. Operating expenses

All figures in £ millions	2020	2019
By function:		
Cost of goods sold	**1,767**	1,858
Operating expenses		
Distribution costs	**59**	73
Selling, marketing and product development costs	**572**	631
Administrative and other expenses	**816**	999
Restructuring costs	**–**	157
Other income	**(45)**	(54)
Total net operating expenses	**1,402**	1,806
Other net gains and losses	**(178)**	(16)
Total	**2,991**	3,648

Other income includes freight income and sublet income. In 2019, other income included service fee income from the Group's then associate Penguin Random House of £4m. Included in administrative and other expenses are research and efficacy costs of £11m (2019: £13m). In 2019, in addition to the restructuring costs shown above, there were restructuring costs in relation to associates of £2m. Other net gains and losses in 2020 largely relate to the sale of the remaining interest in Pearson Random House (£180m gain) and impairments of assets and other costs relating to the disposal of Pearson Institute of Higher Education (£8m loss). In 2019, other net gains and losses largely relate to the sale of the US K12 business.

Notes to the consolidated financial statements

4. Operating expenses continued

An analysis of major restructuring costs is as follows:

All figures in £ millions	2020	2019
By nature:		
Product costs	–	16
Employee costs	–	90
Depreciation and amortisation	–	14
Property and facilities	–	12
Technology and communications	–	2
Professional and outsourced services	–	17
General and administrative costs	–	6
Total restructuring – operating expenses	–	157
Share of associate restructuring	–	2
Total	–	159

In May 2017, the Group announced a major restructuring programme to run between 2017 and 2019 to drive further significant cost savings. The costs of this programme have been excluded from adjusted operating profit so as to better highlight the underlying performance (see note 8).

All figures in £ millions	Notes	2020	2019
By nature:			
Royalties expensed		**191**	242
Other product costs		**349**	466
Employee benefit expense	5	**1,337**	1,452
Contract labour		**67**	139
Employee-related expense		**30**	94
Promotional costs		**233**	254
Depreciation of property, plant and equipment	10	**125**	123
Amortisation of intangible assets – pre-publication	20	**280**	271
Amortisation of intangible assets – software	11	**112**	115
Amortisation and impairment of intangible assets – other	11	**80**	151
Property and facilities		**85**	96
Technology and communications		**216**	196
Professional and outsourced services		**498**	480
Other general and administrative costs		**71**	104
Costs capitalised		**(460)**	(465)
Other net gains and losses		**(178)**	(16)
Other income		**(45)**	(54)
Total		**2,991**	3,648

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

All figures in £ millions	2020	2019
The audit of parent company and consolidated financial statements	**5**	5
The audit of the company's subsidiaries	**2**	2
Total audit fees	**7**	7
Audit-related and other assurance services	–	–
Other non-audit services	–	–
Total other services	–	–
Total non-audit services	–	–
Total	**7**	7

4. Operating expenses continued

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

All figures in £ millions	2020	2019
Group audit fees including fees for attestation under section 404 of the Sarbanes-Oxley Act	**7**	7
Non-audit fees	**–**	–
Total	**7**	7

Fees for attestation under section 404 of the Sarbanes-Oxley Act are allocated between fees payable for the audits of consolidated and subsidiary accounts. Included in Group audit fees for 2020 are additional fees in relation to prior year audit work.

5. Employee information

All figures in £ millions	Notes	2020	2019
Employee benefit expense			
Wages and salaries (including termination costs)		**1,152**	1,258
Social security costs		**96**	100
Share-based payment costs	26	**29**	25
Retirement benefits – defined contribution plans	25	**47**	57
Retirement benefits – defined benefit plans	25	**13**	13
Other post-retirement medical benefits	25	**–**	(1)
Total		**1,337**	1,452

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

Average number employed	2020	2019
Employee numbers		
UK	**4,204**	4,345
Other European countries	**865**	852
US	**10,916**	12,226
Canada	**323**	398
Asia Pacific	**3,133**	2,748
Other countries	**1,894**	2,165
Total	**21,335**	22,734

6. Net finance costs

All figures in £ millions	Notes	2020	2019
Interest payable on financial liabilities at amortised cost and associated derivatives		**(38)**	(22)
Interest on lease liabilities		**(41)**	(45)
Net foreign exchange losses		**(6)**	(5)
Derivatives not in a hedge relationship		**(22)**	(12)
Finance costs		**(107)**	(84)
Interest receivable on financial assets at amortised cost		**9**	15
Interest on lease receivables		**9**	11
Net finance income in respect of retirement benefits	25	**6**	13
Fair value remeasurement of disposal proceeds		**26**	–
Derivatives not in a hedge relationship		**–**	2
Finance income		**50**	41
Net finance costs		**(57)**	(43)
Analysed as:			
Net interest payable reflected in adjusted earnings		**(61)**	(41)
Other net finance income/(costs)		**4**	(2)
Net finance costs		**(57)**	(43)

Included in interest receivable is £nil (2019: £1m) of interest receivable from related parties. Net movement in fair value of hedges is explained in note 16. For further information on adjusted measures above, see note 8.

Notes to the consolidated financial statements

7. Income tax

All figures in £ millions	Notes	2020	2019
Current tax			
Charge in respect of current year		**(18)**	(51)
Adjustments in respect of prior years		**4**	21
Total current tax charge		**(14)**	(30)
Deferred tax			
In respect of temporary differences		**(28)**	59
Other adjustments in respect of prior years		**(2)**	5
Total deferred tax (charge)/credit	13	**(30)**	64
Total tax (charge)/credit		**(44)**	34

The adjustments in respect of prior years in both 2020 and 2019 primarily arise from revising the previous year's reported tax provision to reflect the tax returns subsequently filed. This results in a change between deferred and current tax as well as an absolute benefit to the total tax charge.

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	2020	2019
Profit before tax	**354**	232
Tax calculated at UK rate (2020: 19%, 2019: 19%)	**(67)**	(44)
Effect of overseas tax rates	**(6)**	(2)
Effect of UK rate change	**(5)**	–
Joint venture and associate income reported net of tax	**1**	10
Intra-group financing benefit	**14**	11
Movement in provisions for tax uncertainties	**24**	3
Net expense not subject to tax	**(7)**	(10)
Gains and losses on sale of businesses not subject to tax	**21**	57
Unrecognised tax losses	**(21)**	(17)
Adjustments in respect of prior years	**2**	26
Total tax (charge)/credit	**(44)**	34
UK	**23**	(12)
Overseas	**(67)**	46
Total tax (charge)/credit	**(44)**	34
Tax rate reflected in earnings	**12.5%**	(14.7)%

Included in net expense not subject to tax are foreign taxes not creditable, the tax impact of share-based payments and other expenses not deductible.

KJ Key judgements

› The application of tax legislation in relation to provisions for uncertain tax positions.

KE Key areas of estimation

› The level of provisions required in relation to uncertain tax positions is complex and each matter is separately assessed. The estimation of future settlement amounts is based on a number of factors including the status of the unresolved matter, clarity of legislation, range of possible outcomes and the statute of limitations.

Factors which may affect future tax charges include changes in tax legislation, transfer pricing regulations, the level and mix of profitability in different countries, and settlements with tax authorities.

The movement in provisions for tax uncertainties primarily reflects releases due to the expiry of relevant statutes of limitation, settlement of certain audits and the establishment of provisions for new uncertain tax positions. The current tax liability of £84m (2019: £55m) includes £104m (2019: £152m) of provisions for tax uncertainties principally in respect of several matters in the US, the UK and China. The matters provided for include the allocation between territories of proceeds of historical business disposals and the potential disallowance of intra-group recharges. The Group is currently under audit in several countries, and the timing of any resolution of these audits is uncertain. Of the balance of £104m, £57m relates to 2015 and earlier and is mostly under audit. In most countries, tax years up to and including 2014 are now statute barred from examination by tax authorities. Of the remaining balance, £17m relates to 2016, £14m to 2017, £3m to 2018, £10m to 2019 and £3m to 2020.

If relevant enquiry windows pass with no audit, management believes it is reasonably possible that provision levels will reduce by an estimated £10m within the next 12 months. However, the tax authorities may take a different view from management and the final liability may be greater than provided.

Contingent liabilities relating to tax are disclosed in note 34.

7. Income tax continued

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

All figures in £ millions	2020	2019
Profit before tax	**354**	232
Adjustments:		
Cost of major restructuring	–	159
Other net gains and losses	**(178)**	(16)
Intangible charges	**80**	163
Other net finance (income)/costs	**(4)**	2
Adjusted profit before tax	**252**	540
Total tax (charge)/credit	**(44)**	34
Adjustments:		
Tax benefit on cost of major restructuring	–	(35)
Tax charge/(benefit) on other net gains and losses	**3**	(68)
Tax benefit on intangible charges	**(22)**	(48)
Tax charge on other net finance costs	**4**	–
Tax amortisation benefit on goodwill and intangibles	**24**	28
Adjusted tax charge	**(35)**	(89)
Tax rate reflected in adjusted earnings	**13.7%**	16.5%

For further information on adjusted measures above, see note 8.

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

All figures in £ millions	2020	2019
Net exchange differences on translation of foreign operations	**(13)**	5
Fair value gain on other financial assets	**(6)**	(4)
Remeasurement of retirement benefit obligations	**2**	22
	(17)	23

Notes to the consolidated financial statements

8. Earnings per share

Basic

Basic earnings per share is calculated by dividing the profit or loss attributable to equity shareholders of the company (earnings) 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. A dilution is not calculated for a loss.

All figures in £ millions	**2020**	**2019**
Earnings for the year	**310**	266
Non-controlling interest	**–**	(2)
Earnings attributable to equity shareholders	**310**	264
Weighted average number of shares (millions)	**755.4**	777.0
Effect of dilutive share options (millions)	**–**	0.5
Weighted average number of shares (millions) for diluted earnings	**755.4**	777.5
Earnings per share (in pence per share)		
Basic	**41.0p**	34.0p
Diluted	**41.0p**	34.0p

Adjusted

For additional detailed information on the calculation of adjusted measures, see pp212-216 (Financial key performance indicators). See note 2 for details of specific items excluded from or included in adjusted operating profit in 2020 and 2019.

In order to show results from operating activities on a consistent basis, an adjusted earnings per share is presented. The Group's definition of adjusted earnings per share may not be comparable with other similarly titled measures reported by other companies.

Adjusted earnings is a non-GAAP (non-statutory) financial measure and is included as it is a key financial measure used by management to evaluate the performance of the Group and allocate resources to business segments. The measure also enables investors to more easily, and consistently, track the underlying operational performance of the Group and its business segments over time by separating out those items of income and expenditure relating to acquisition and disposal transactions, major restructuring programmes and certain other items that are also not representative of underlying performance.

Adjusted earnings per share is calculated as adjusted earnings divided by the weighted average number of shares in issue on an undiluted basis. The following items are excluded from or included in adjusted earnings:

Cost of major restructuring – In May 2017, the Group announced a restructuring programme, to run between 2017 and 2019, to drive significant cost savings. This programme began in the second half of 2017 and costs incurred to date relate to delivery of cost efficiencies in our enabling functions and US Higher Education Courseware business together with further rationalisation of the property and supplier portfolio. The restructuring costs in 2019 of £159m relate predominantly to staff redundancies. The costs of this restructuring programme are significant enough to exclude from the adjusted operating profit measure so as to better highlight the underlying performance (see note 4).

Other net gains and losses – These represent profits and losses on the sale of subsidiaries, joint ventures, associates and other financial assets and are excluded from adjusted earnings as they distort the performance of the Group as reported on a statutory basis. Other net gains in 2020 largely relate to the sale of the remaining interest in Penguin Random House (£180m gain) and impairments of assets and other costs relating to the disposal of Pearson Institute of Higher Education (£8m loss). In 2019, other net gains largely relate to the sale of the US K-12 business. There is no tax associated with the Penguin Random House disposal. The tax charge of £3m in 2020 relates to other gains and losses.

Intangible charges – These represent charges in respect of intangible assets acquired through business combinations and the direct costs of acquiring those businesses. These charges are excluded as they reflect past acquisition activity and do not necessarily reflect the current year performance of the Group. Intangible amortisation charges in 2020 were £80m including impairment charges of £12m. In 2019, intangible charges were £163m including impairment charges of £65m.

Other net finance income/costs – These include finance costs in respect of retirement benefits, finance costs relating to acquisition and disposal transactions and foreign exchange and other net gains and losses. Net finance income relating to retirement benefits is excluded as management does not believe that the consolidated income statement presentation under IAS 19 reflects the economic substance of the underlying assets and liabilities. Finance costs associated with acquisition and disposal transactions are excluded as these relate to future earn-outs or acquisition expenses and are not part of the underlying financing. In 2020, the fair value re-measurement of disposal proceeds relates to the US K-12 disposal in 2019. Foreign exchange and other net gains and losses are excluded as they represent short-term fluctuations in market value and are subject to significant volatility. Other net gains and losses may not be realised in due course as it is normally the intention to hold the related instruments to maturity. In 2020 and 2019, the foreign exchange gains and losses largely relate to foreign exchange differences on unhedged intercompany loans and cash and cash equivalents. Losses on derivatives not in a hedge relationship represent the unrealised mark to market of long-term interest rate hedges used to fix the interest rate of borrowings.

8. Earnings per share continued

Adjusted continued

Tax – Tax on the above items is excluded from adjusted earnings. Where relevant, the Group also excludes the benefit from recognising previously unrecognised pre-acquisition and capital losses. The tax benefit from tax deductible goodwill and intangibles is added to the adjusted income tax charge as this benefit more accurately aligns the adjusted tax charge with the expected rate of cash tax payments.

Non-controlling interest – Non-controlling interest for the above items is excluded from adjusted earnings.

The following tables reconcile the statutory income statement to the adjusted income statement.

							2020
All figures in £ millions	**Statutory income statement**	**Cost of major restructuring**	**Other net gains and losses**	**Intangible charges**	**Other net finance income/ costs**	**Tax amortisation benefit**	**Adjusted income statement**
Operating profit	411	–	(178)	80	–	–	313
Net finance costs	(57)	–	–	–	(4)	–	(61)
Profit before tax	354	–	(178)	80	(4)	–	252
Income tax	(44)	–	3	(22)	4	24	(35)
Profit for the year	310	–	(175)	58	–	24	217
Non-controlling interest	–	–	–	–	–	–	–
Earnings	310	–	(175)	58	–	24	217
Weighted average number of shares (millions)	755.4						755.4
Weighted average number of shares (millions) for diluted earnings	755.4						755.4
Earnings per share (basic)	41.0p						28.7p
Earnings per share (diluted)	41.0p						28.7p

							2019
All figures in £ millions	**Statutory income statement**	**Cost of major restructuring**	**Other net gains and losses**	**Intangible charges**	**Other net finance income/ costs**	**Tax amortisation benefit**	**Adjusted income statement**
Operating profit	275	159	(16)	163	–	–	581
Net finance costs	(43)	–	–	–	2	–	(41)
Profit before tax	232	159	(16)	163	2	–	540
Income tax	34	(35)	(68)	(48)	–	28	(89)
Profit for the year	266	124	(84)	115	2	28	451
Non-controlling interest	(2)	–	–	–	–	–	(2)
Earnings	264	124	(84)	115	2	28	449
Weighted average number of shares (millions)	777.0						777.0
Weighted average number of shares (millions) for diluted earnings	777.5						777.5
Earnings per share (basic)	34.0p						57.8p
Earnings per share (diluted)	34.0p						57.7p

Notes to the consolidated financial statements

9. Dividends

All figures in £ millions	2020	2019
Final paid in respect of prior year 13.5p (2019: 13.5p)	**101**	101
Interim paid in respect of current year 6p (2019: 6p)	**45**	46
	146	147

The Directors are proposing a final dividend in respect of the financial year ended 31 December 2020 of 13.5p per equity share which will absorb an estimated £102m of shareholders' funds. It will be paid on 7 May 2021 to shareholders who are on the register of members on 26 March 2021. These financial statements do not reflect this dividend.

10. Property, plant and equipment

	Right-of-use assets		Owned assets			
All figures in £ millions	**Land and buildings**	**Plant and equipment**	**Land and buildings**	**Plant and equipment**	**Assets in course of construction**	**Total**
Cost						
At 1 January 2019	418	6	317	458	18	1,217
Exchange differences	(9)	–	(8)	(15)	–	(32)
Additions	64	2	–	18	40	124
Disposals	(13)	(4)	(13)	(108)	(8)	(146)
Reclassifications	–	–	4	(4)	–	–
Transfer of finance leases	–	19	–	(19)	–	–
Transfer to intangible assets	–	–	–	(3)	(4)	(7)
Transfer to intangible assets – pre-publication	–	–	–	(2)	(10)	(12)
At 31 December 2019	460	23	300	325	36	1,144
Exchange differences	**(11)**	**(2)**	**(7)**	**(11)**	**(1)**	**(32)**
Additions	**62**	**–**	**7**	**5**	**37**	**111**
Disposals	**(13)**	**(9)**	**(23)**	**(29)**	**(1)**	**(75)**
Reclassifications	**–**	**–**	**20**	**21**	**(41)**	**–**
Transfer to intangible assets	**–**	**–**	**–**	**–**	**(9)**	**(9)**
Transfer to assets classified as held for sale	**(59)**	**–**	**(1)**	**(3)**	**–**	**(63)**
At 31 December 2020	**439**	**12**	**296**	**308**	**21**	**1,076**

	Right-of-use assets		Owned assets			
All figures in £ millions	**Land and buildings**	**Plant and equipment**	**Land and buildings**	**Plant and equipment**	**Assets in course of construction**	**Total**
Depreciation						
At 1 January 2019	–	–	(195)	(361)	–	(556)
Exchange differences	2	–	6	13	–	21
Charge for the year	(60)	(4)	(21)	(38)	–	(123)
Disposals	–	–	10	116	–	126
Transfer of finance leases	–	(12)	–	12	–	–
Transfer to intangible assets	–	–	–	3	–	3
Transfer to intangible assets – pre-publication	–	–	–	3	–	3
At 31 December 2019	(58)	(16)	(200)	(252)	–	(526)
Exchange differences	**2**	**1**	**6**	**9**	**–**	**18**
Charge for the year	**(65)**	**(3)**	**(25)**	**(32)**	**–**	**(125)**
Disposals	**1**	**9**	**22**	**29**	**–**	**61**
Reclassifications	**–**	**–**	**(2)**	**2**	**–**	**–**
Impairment in advance of transfer to assets classified as held for sale	**(4)**	**–**	**–**	**–**	**–**	**(4)**
Transfer to assets classified as held for sale	**14**	**–**	**–**	**1**	**–**	**15**
At 31 December 2020	**(110)**	**(9)**	**(199)**	**(243)**	**–**	**(561)**
Carrying amounts						
At 1 January 2019	418	6	122	97	18	661
At 31 December 2019	402	7	100	73	36	618
At 31 December 2020	**329**	**3**	**97**	**65**	**21**	**515**

10. Property, plant and equipment continued

Depreciation expense of £44m (2019: £42m) has been included in the income statement in cost of goods sold and £81m (2019: £81m) in operating expenses.

11. Intangible assets

All figures in £ millions	Goodwill	Software	Acquired customer lists, contracts and relationships	Acquired trademarks and brands	Acquired publishing rights	Other intangibles acquired	Total
Cost							
At 1 January 2019	2,111	959	910	267	184	457	4,888
Exchange differences	(57)	(22)	(29)	(10)	(5)	(20)	(143)
Additions – internal development	–	137	–	–	–	–	137
Additions – purchased	–	1	–	–	–	–	1
Disposals	–	(15)	(88)	(19)	–	(47)	(169)
Acquisition through business combination	18	–	–	–	–	23	41
Transfer from property, plant and equipment	–	7	–	–	–	–	7
Transfer to intangible assets – pre-publication	–	(28)	–	–	–	–	(28)
Movement in held for sale	67	–	–	–	–	–	67
At 31 December 2019	2,139	1,039	793	238	179	413	4,801
Exchange differences	**(45)**	**(24)**	**(25)**	**(19)**	**(2)**	**(48)**	**(163)**
Additions – internal development	**–**	**80**	**–**	**–**	**–**	**–**	**80**
Additions – purchased	**–**	**1**	**–**	**–**	**–**	**–**	**1**
Disposals	**–**	**(6)**	**(17)**	**(21)**	**(80)**	**(16)**	**(140)**
Transfer from property, plant and equipment	**–**	**9**	**–**	**–**	**–**	**–**	**9**
Transfer from intangible assets – pre-publication	**–**	**5**	**–**	**–**	**–**	**–**	**5**
At 31 December 2020	**2,094**	**1,104**	**751**	**198**	**97**	**349**	**4,593**

All figures in £ millions	Goodwill	Software	Acquired customer lists, contracts and relationships	Acquired trademarks and brands	Acquired publishing rights	Other intangibles acquired	Total
Amortisation							
At 1 January 2019	–	(512)	(647)	(181)	(178)	(361)	(1,879)
Exchange differences	–	16	22	7	4	19	68
Charge for the year	–	(115)	(51)	(11)	(2)	(22)	(201)
Impairment charge	–	–	–	(12)	–	(53)	(65)
Disposals	–	10	88	19	–	46	163
Transfer from property, plant and equipment	–	(3)	–	–	–	–	(3)
Transfer to intangible assets – pre-publication	–	16	–	–	–	–	16
At 31 December 2019	–	(588)	(588)	(178)	(176)	(371)	(1,901)
Exchange differences	**–**	**18**	**23**	**13**	**2**	**46**	**102**
Charge for the year	**–**	**(112)**	**(44)**	**(14)**	**(2)**	**(8)**	**(180)**
Impairment charge	**–**	**–**	**(2)**	**–**	**–**	**(10)**	**(12)**
Disposals	**–**	**6**	**17**	**21**	**81**	**15**	**140**
At 31 December 2020	**–**	**(676)**	**(594)**	**(158)**	**(95)**	**(328)**	**(1,851)**
Carrying amounts							
At 1 January 2019	2,111	447	263	86	6	96	3,009
At 31 December 2019	2,139	451	205	60	3	42	2,900
At 31 December 2020	**2,094**	**428**	**157**	**40**	**2**	**21**	**2,742**

The 2019 amortisation table has been restated to show the £65m impairment charge separately from the charge for the year.

Notes to the consolidated financial statements

11. Intangible assets continued

Goodwill

The goodwill carrying value of £2,094m relates to acquisitions completed after 1 January 1998. Prior to 1 January 1998, all goodwill was written off to reserves on the date of acquisition. For acquisitions completed between 1 January 1998 and 31 December 2002, no value was ascribed to intangibles other than goodwill which was amortised over a period of up to 20 years. On adoption of IFRS on 1 January 2003, the Group chose not to restate the goodwill balance and at that date the balance was frozen (i.e. amortisation ceased). If goodwill had been restated, then a significant value would have been ascribed to other intangible assets, which would be subject to amortisation, and the carrying value of goodwill would be significantly lower. For acquisitions completed after 1 January 2003, value has been ascribed to other intangible assets which are amortised.

Other intangible assets

Other intangibles acquired include technology and process rights.

Intangible assets are valued separately for each acquisition and the primary method of valuation used is the discounted cash flow method. The majority of acquired intangibles are amortised using an amortisation profile based on the projected cash flows underlying the acquisition date valuation of the intangible asset, which generally results in a larger proportion of amortisation being recognised in the early years of the asset's life. The Group keeps the expected pattern of consumption under review.

Amortisation of £22m (2019: £19m) is included in the income statement in cost of goods sold and £158m (2019: £182m) in operating expenses. Impairment of £12m (2019: £65m), of which £2m (2019: £nil) relates to customer lists, contracts and relationships, £nil (2019: £12m) to acquired trademarks and brands and £10m (2019: £53m) to other intangibles acquired, is included in operating expenses.

The range of useful economic lives for each major class of intangible asset (excluding goodwill and software) is shown below:

	2020
	Useful economic life
Class of intangible asset	
Acquired customer lists, contracts and relationships	3–20 years
Acquired trademarks and brands	2–20 years
Acquired publishing rights	5–20 years
Other intangibles acquired	2–20 years

The expected amortisation profile of acquired intangible assets is shown below:

	2020			
All figures in £ millions	One to five years	Six to ten years	More than ten years	Total
Class of intangible asset				
Acquired customer lists, contracts and relationships	116	40	1	157
Acquired trademarks and brands	30	9	1	40
Acquired publishing rights	2	–	–	2
Other intangibles acquired	13	8	–	21

Impairment tests for cash-generating units (CGUs) containing goodwill

Impairment tests have been carried out where appropriate as described below. Goodwill was allocated to CGUs, or an aggregation of CGUs, where goodwill could not be reasonably allocated to individual business units. CGUs have been revised in 2019 and 2020. Impairment reviews were conducted on these revised CGUs as summarised below:

2020 CGUs

	2020	2019
All figures in £ millions	Goodwill	Goodwill
North American Courseware	–	–
OPM	18	18
Virtual Schools	374	386
Assessments	1,002	1,035
International (includes the separate CGUs of Brazil, China, India and South Africa)	700	700
Total	2,094	2,139

Goodwill is tested at least annually for impairment. The recoverable amount of each aggregated CGU is based on the higher of value in use and fair value less costs of disposal. The impairment assessment is based on value in use with the exception of Pearson Institute of Higher Education as explained below. Other than goodwill there are no intangible assets with indefinite lives.

11. Intangible assets continued

KE Key areas of estimation

› The recoverability of goodwill balances. Key assumptions used in goodwill impairment testing are discount rates, perpetuity growth rates, forecast sales growth rates and forecast operating profits.

No impairments of goodwill were recorded in 2020. Impairment charges of £12m have been recognised in relation to acquired intangibles. In 2019, following a reassessment of the relative risk in the Brazil CGU compared to Pearson as a whole, it was determined in the course of the impairment review that neither the value in use nor the fair value less costs of disposal of the Brazil CGU supported the carrying value of the CGU. As the goodwill related to the Brazil CGU was fully impaired in prior years, the acquired intangibles of the Brazil CGU were impaired by £65m, bringing their carrying value to £27m.

Determination of CGUs and reallocation of goodwill

Pearson identifies its CGUs based on its operating model and how data is collected and reviewed for management reporting and strategic planning purposes in accordance with IAS 36 'Impairment of Assets'. In 2019, the CGUs and aggregation of CGUs was revised to take account of the following:

› The implementation of a new Enterprise Resource Planning (ERP) system in North America meant that ledgers are structured on a legal entity basis rather than the previous divisional basis. This has meant it is no longer possible to identify the carrying values of the Pearson VUE business separately from the wider Assessments business. As a result, the Pearson VUE business has been combined with the Assessments business as one CGU for impairment testing

› The disposal of the US K-12 business in 2019 caused management to disaggregate the North America CGU.

At 1 January 2019, the goodwill of the previous North America and Pearson VUE CGUs was therefore reallocated between North American Courseware, OPM, Virtual Schools and Assessments, based on their relative fair value at 1 January 2019 amended to take into account previous impairments taken. No goodwill was allocated to the North American Courseware CGU reflecting the significant impairments taken in 2015 and 2016.

In 2020, due to the new structure of the business and the consequent change in management responsibilities, the Other Growth aggregation of CGUs has been combined with the Core aggregation to form a larger aggregation as Other International. The Other Growth aggregation had no goodwill or intangibles prior to the combination.

Furthermore, the cash flows and assets related to Pearson Institute of Higher Education (PIHE) were extracted from the South Africa CGU and assessed on a fair value less costs to sell basis reflecting the expected disposal of PIHE.

Key assumptions

For the purpose of estimating the value in use of the CGUs, management has used an income approach based on present value techniques. The calculations use cash flow projections based on financial budgets approved by management covering a three-year period.

Previously, longer forecast periods for OPM were used, however, profitability improvements in the OPM division mean that it is currently sensible to use a three year analysis, consistent with the rest of the Group. OPM relies on contracts with key customers and the forecasts used assume these are renewed or replaced.

The key assumptions used by management in the value in use calculations were:

Discount rates – The discount rate is based on the risk-free rate for government bonds, adjusted for a risk premium to reflect the increased risk in investing in equities. The risk premium adjustment is assessed for each CGU. The average pre-tax discount rates range from 9.3% to 17.2% (2019: pre-tax 9.5% to 17%). Discount rates are lower for those businesses which operate in more mature markets with low inflation and higher for those operating in emerging markets with higher inflation.

Perpetuity growth rates – The perpetuity growth rates are based on inflation trends. A perpetuity growth rate of 2% (2019: 2%) was used for cash flows subsequent to the approved budget period for CGUs operating in mature markets. This perpetuity growth rate is a conservative rate and is considered to be lower than the long-term historical growth rates of the underlying territories in which the CGU operates and the long-term growth rate prospects of the sectors in which the CGU operates. CGU growth rates between 2.2% to 4.5% (2019: 3.2% to 6.5%) were used for cash flows subsequent to the approved budget period for CGUs operating in emerging markets with high inflation. These growth rates are also generally below the long-term historical growth rates in these markets.

The key assumptions used by management in setting the financial budgets were as follows:

Forecast sales growth rates – Forecast sales growth rates are based on past experience adjusted for the strategic direction and near-term investment priorities within each CGU. Key assumptions include continued growth in OPM and Virtual Schools, ongoing pressures in the US Higher Education Courseware market, and recovery across all of our other CGUs following the impacts of COVID-19 in 2020. The sales forecasts use average nominal growth rates between 11% and 17% for emerging businesses in mature markets (2019: 6% and 11%) and 0% and 13% for mature businesses in mature markets (2019: (5)% and 4%) and between 2% and 18% (2019: 5% and 11%) for emerging markets with high inflation. These growth rates between 2021 and 2023 are inflated due to the impact of COVID-19 on sales in 2020. For those businesses that declined in 2020 the normalised growth rate using 2019 actuals as the starting point would be between (4)% and 3% for mature businesses in mature markets and between (4)% and 4% in emerging markets.

Operating profits – Operating profits are forecast based on historical experience of operating margins, adjusted for the impact of changes to product costs, committed restructuring plans, strategic developments and new business cases to the extent they have been formally approved prior to the balance sheet date. Management applies judgement in allocating corporate costs on a reasonable and consistent basis in order to determine operating profit at a CGU level. Forecasts include assumptions relating to the COVID-19 pandemic. It is assumed that restrictions ease in Q2 2021 with a phased return to normality in H2 2021 as the vaccine roll-out progresses.

Notes to the consolidated financial statements

11. Intangible assets continued

Key assumptions continued

The table below shows the key assumptions for those CGUs for which the carrying value of goodwill is significant in comparison to the total carrying value of goodwill:

	Discount rate	Perpetuity growth rate
Virtual Schools	9.5%	2.0%
Other International	9.3%	2.2%
Assessments	9.5%	2.0%

Sensitivities

Impairment testing for the year ended 31 December 2020 has identified the following CGUs, or groups of CGUs, as being sensitive to reasonably possible changes in key assumptions. The table below shows the headroom at 31 December 2020 and the changes in the key assumptions required in order for the recoverable amount to equal the carrying value.

	Headroom at 31 December 2020	Discount rate	Discount rate for zero headroom	Perpetuity growth rate	Perpetuity growth rate for zero headroom	Contribution* reduction p.a. for zero headroom
North American Courseware	£424m	9.5%	10.7%	2.0%	1.0%	£32m
OPM	£176m	9.5%	11.4%	2.0%	0.3%	£13m
Brazil	£42m	13.6%	16.2%	3.5%	1.5%	£5m
Other International	£368m	9.3%	10.5%	2.2%	1.3%	£27m

* CGU contribution is operating profit excluding corporate overheads.

12. Investments in joint ventures and associates

The amounts recognised in the balance sheet are as follows:

All figures in £ millions	2020	2019
Associates	6	7
Associates classified as held for sale	–	397
Total	6	404

The amounts recognised in the income statement are as follows:

All figures in £ millions	2020	2019
Associates	5	54
Total	5	54

The Group has no material associates or joint ventures.

The Group's 25% interest in Penguin Random House was disposed of in April 2020 (see note 31). At 31 December 2019, the Group's share of the assets of Penguin Random House were classified as held for sale on the balance sheet (see note 32). Funds loaned to Penguin Random House were repaid at the point of disposal. Prior to the completion of the sale of Penguin Random House, the Group received dividends of £1m (2019: £64m) from Penguin Random House.

There were no other material transactions with associates or joint ventures during 2020.

13. Deferred income tax

All figures in £ millions	2020	2019
Deferred income tax assets	**32**	59
Deferred income tax liabilities	**(62)**	(48)
Net deferred income tax (liability)/asset	**(30)**	11

Substantially all of the deferred income tax assets are expected to be recovered after more than one year.

Deferred income tax assets and liabilities shall be offset when there is a legally enforceable right to offset current income tax assets with current income tax liabilities and where the deferred income taxes relate to the same fiscal authority. At 31 December 2020, the Group has gross tax losses for which no deferred tax asset is recognised of £166m (2019: £168m) in respect of UK losses, £369m (2019: £362m) in respect of US losses and approximately £300m (2019: £315m) in respect of losses in other territories. The UK losses are capital losses which can be carried forward indefinitely. The US losses relate to federal and state taxes. Federal tax losses can be carried forward indefinitely; certain state tax losses may have expiry periods between one and 20 years.

Other gross deductible temporary differences for which no deferred tax asset is recognised total £56m (2019: £82m). As at 31 December 2020, £27m of tax losses and other deductible temporary differences included in the disclosed amounts above had been offered in settlement of various tax assessments in India

The amount of temporary differences associated with subsidiaries for which no deferred tax has been provided is not material

Deferred income tax assets of £20m (2019: £41m) have been recognised in countries that reported a tax loss in either the current or preceding year. The majority arises in Brazil in respect of tax deductible goodwill. It is considered more likely than not that there will be sufficient future taxable profits to realise these assets.

The recognition of the deferred income tax assets is supported by management's forecasts of the future profitability of the relevant countries. In some cases deferred income tax assets are forecast to be recovered through taxable profits over a period that exceeds five years. Management consider these forecasts are sufficiently reliable to support the recovery of the assets. Where there are insufficient forecasts of future profits, deferred income tax assets have not been recognised.

The movement in deferred income tax assets and liabilities during the year is as follows:

All figures in £ millions	Trading losses	Returns provisions	Retirement benefit obligations	Deferred revenue	Goodwill and intangibles	Interest limitations	Other	Total
Deferred income tax assets/(liabilities)								
At 1 January 2019	20	31	(55)	68	(205)	28	52	(61)
Exchange differences	(1)	(1)	(1)	(3)	6	(2)	(3)	(5)
Income statement benefit/(charge)	70	(10)	(4)	(24)	–	31	1	64
Tax benefit/(charge) in other comprehensive income	–	–	22	–	–	–	(4)	18
Tax charge in equity	–	–	–	–	–	–	(5)	(5)
At 31 December 2019	89	20	(38)	41	(199)	57	41	11
Exchange differences	**2**	**–**	**(1)**	**(2)**	**2**	**(4)**	**(5)**	**(8)**
Income statement (charge)/benefit	**(44)**	**(12)**	**(12)**	**6**	**(12)**	**23**	**21**	**(30)**
Tax benefit/(charge) in other comprehensive income	**–**	**–**	**2**	**–**	**–**	**–**	**(5)**	**(3)**
At 31 December 2020	**47**	**8**	**(49)**	**45**	**(209)**	**76**	**52**	**(30)**

Other deferred income tax items include temporary differences in respect of share-based payments, provisions, depreciation and royalty advances.

As at 31 December 2020, no deferred income tax assets or liabilities were classified as held for sale (2019: £nil).

Notes to the consolidated financial statements

14. Classification of financial instruments

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

All figures in £ millions	Notes	2020 FVOCI	2020 Fair value FVTPL	2020 Fair value Fair value – hedging instrument	2020 Amortised cost Financial assets	2020 Total carrying value	2019 FVOCI	2019 Fair value FVTPL	2019 Fair value Fair value – hedging instrument	2019 Amortised cost Financial assets	2019 Total carrying value
Investments in unlisted securities	15	138	–	–	–	138	122	–	–	–	122
Cash and cash equivalents[1]	17	–	93	–	1,004	1,097	–	48	–	389	437
Derivative financial instruments	16	–	2	61	–	63	–	6	48	–	54
Trade receivables	22	–	–	–	803	803	–	–	–	918	918
Investment in finance lease receivable	22	–	–	–	130	130	–	–	–	196	196
Other receivable	22	–	96	–	–	96	–	182	–	–	182
Total financial assets		138	191	61	1,937	2,327	122	236	48	1,503	1,909

1 In 2019, cash and cash equivalents of £48m have been reclassified from amortised cost to FVTPL (classified as level 1) as they relate to money market funds.

The carrying value of the Group's financial assets is equal to, or approximately equal to, the market value. The other receivable relates to the receivable which arose on the disposal of the US K-12 business and is included in other receivables, non-current and current, in note 22.

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

All figures in £ millions	Notes	2020 Fair value FVTPL	2020 Fair value Fair value – hedging instrument	2020 Amortised cost Other financial liabilities	2020 Total carrying value	2020 Total market value	2019 Fair value FVTPL	2019 Fair value Fair value – hedging instrument	2019 Amortised cost Other financial liabilities	2019 Total carrying value	2019 Total market value
Derivative financial instruments	16	(30)	(22)	–	(52)	(52)	(7)	(32)	–	(39)	(39)
Trade payables	24	–	–	(340)	(340)	(340)	–	–	(358)	(358)	(358)
Bank loans and overdrafts	18	–	–	(3)	(3)	(3)	–	–	(3)	(3)	(3)
Other borrowings due within one year	18	–	–	(251)	(251)	(249)	–	–	(89)	(89)	(89)
Borrowings due after more than one year	18	–	–	(1,397)	(1,397)	(1,451)	–	–	(1,572)	(1,572)	(1,574)
Total financial liabilities		(30)	(22)	(1,991)	(2,043)	(2,095)	(7)	(32)	(2,022)	(2,061)	(2,063)

The market value of leases has been stated at book value.

Fair value measurement

As shown above, the Group's derivative assets and liabilities, unlisted securities and marketable securities are held at fair value. Financial instruments that are measured subsequently to initial recognition at fair value are grouped into levels 1 to 3, based on the degree to which the fair value is observable, as follows:

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).

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).

The Group's bonds valued at £965m (2019: £595m) and money market funds of £93m (2019: £48m) included within cash and cash equivalents are classified as level 1. The Group's derivative assets valued at £63m (2019: £54m) and derivative liabilities valued at £52m (2019: £39m) are classified as level 2. The Group's investments in unlisted securities are valued at £138m (2019: £122m) and the other receivable is valued at £96m (2019: £182m); both are classified as level 3.

14. Classification of financial instruments continued

The following table analyses the movements in level 3 fair value remeasurements:

All figures in £ millions	2020 Other receivable	2020 Investments in unlisted securities	2020 Total	2019 Total
At beginning of year	**182**	**122**	**304**	93
Exchange differences	**(7)**	**(4)**	**(11)**	(2)
Acquisition of investments and other receivable	**–**	**6**	**6**	193
Repayment	**(105)**	**–**	**(105)**	–
Fair value movements	**26**	**14**	**40**	20
At end of year	**96**	**138**	**234**	304

The fair value of the investments in unlisted securities is determined by reference to the financial performance of the underlying asset, recent funding rounds and amounts realised on the sale of similar assets.

The fair value of the other receivable, which arose on the disposal of the US K-12 business, is determined using present value techniques whereby the expected value of future cash flows is discounted using a rate which is representative of the creditworthiness of the US K-12 business.

15. Other financial assets

All figures in £ millions	2020	2019
At beginning of year	**122**	93
Exchange differences	**(4)**	(3)
Acquisition of investments	**6**	12
Fair value movements	**14**	20
At end of year	**138**	122

Other financial assets are unlisted securities of £138m (2019: £122m) that are classified at fair value through other comprehensive income (FVOCI). The assets, which are not held for trading, relate to the Group's interests in new and innovative educational ventures across the world. These are strategic investments and the Group considers the classification as FVOCI to be more relevant. None of the investments are individually significant to the financial statements.

16. Derivative financial instruments and hedge accounting

The Group's approach to the management of financial risks is set out in note 19. The Group's outstanding derivative financial instruments are as follows:

All figures in £ millions	2020 Gross notional amounts	2020 Assets	2020 Liabilities	2019 Gross notional amounts	2019 Assets	2019 Liabilities
Interest rate derivatives – in a fair value hedge relationship	**354**	**12**	**–**	336	13	–
Interest rate derivatives – not in a hedge relationship	**550**	**–**	**(27)**	557	2	(6)
Cross-currency rate derivatives – in a hedge relationship	**516**	**44**	**(20)**	502	29	(31)
FX derivatives – in a hedge relationship	**193**	**5**	**(2)**	555	6	(1)
FX derivatives – not in a hedge relationship	**361**	**2**	**(3)**	386	4	(1)
Total	**1,974**	**63**	**(52)**	2,336	54	(39)
Analysed as expiring:						
In less than one year	**1,238**	**18**	**(12)**	1,167	25	(15)
Later than one year and not later than five years	**663**	**45**	**(32)**	694	13	(6)
Later than five years	**73**	**–**	**(8)**	475	16	(18)
Total	**1,974**	**63**	**(52)**	2,336	54	(39)

Notes to the consolidated financial statements

16. Derivative financial instruments and hedge accounting continued

The Group's treasury policies only allow derivatives to be traded where the objective is risk mitigation. These are then designated for hedge accounting using the following criteria:

› Where interest rate and cross currency interest rate swaps are used to convert fixed rate debt to floating and we expect to receive inflows equal to the fixed rate debt interest, these are classified as fair value hedges

› Where derivatives are used to create a future foreign currency liability to provide protection against currency movements affecting the valuation of an overseas investment, these are designated as a net investment hedge

› If the derivative and the underlying hedged exposure would normally be revalued through the income statement and valuation changes are expected to be perfectly or near perfectly equal and opposite, these will not be classified in a hedge relationship.

The Group's fixed rate USD debt is held as fixed rate instruments at amortised cost.

The majority of the Group's fixed rate euro debt is converted to a floating rate exposure using interest rate and cross-currency swaps. The Group receives interest under its euro debt related swap contracts to match the interest on the bonds (ranging from a receipt of 1.375% on its euro 2025 notes to 1.875% on its euro 2021 notes) and, in turn, pays either a floating US dollar or sterling variable rates of GBP LIBOR + 0.81% and US Libor + 1.36%.

GBP and USD interest rate swaps are subsequently used to fix an element of the interest charge. The all-in rates (including the spread above LIBOR) that the Group pays are between 1.9% and 3.6%. In addition to this, the Group has executed additional interest rate swaps to offset the floating rate borrowings paying between 0.87% and 2.1%. At 31 December 2020, the Group had interest rate swap contracts to fix £550m of debt and a further £595m of outstanding fixed rate bonds, bringing the total fixed rate debt to £1,145m. These fixed interest rate derivatives are not designated in hedging relationships. Additionally, the Group uses FX derivatives including forwards, collars and cross currency swaps to create synthetic USD debt as a hedge of its USD assets and to achieve certainty of USD currency conversion rates, in line with the Group's FX hedging policy. Outstanding contracts as at 31 December 2020 were held at an average GBP/USD rate of 1.36. The Group also uses FX derivatives to create synthetic BRL debt as a hedge of BRL assets, these are held at an average GBP/BRL rate of 7.53. These derivatives are in designated net investment hedging relationships. The weighted average rate achieved for the bonds in a net investment hedge relationship was GBP/USD 1.59 for the USD bonds and EUR/GBP 0.86 for the euro bonds. Outstanding contracts on the cross currency swaps at 31 December 2020 were held at an average EUR/GBP rate of 0.79. These derivatives are in designated fair value hedging relationships.

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.

Fair value hedges

The Group uses interest rate swaps and cross currency swaps as fair value hedges of the Group's euro issued debt.

Interest rate exposure arises from movements in the fair value of the Group's euro debt attributable to movements in euro interest rates. The hedged risk is the change in the euro bonds fair value attributable to interest rate movements. The hedged items are the Group's euro bonds which are issued at a fixed rate. The hedging instruments are fixed to floating euro interest rate swaps where the Group receives fixed interest payments and pays three month Euribor.

As the critical terms of the interest rate swaps match the bonds, there is an expectation that the value of the hedging instrument and the value of the hedged item will move in the opposite direction as a result of movements in the zero coupon Euribor curve. The hedge ratio is therefore expected to be 100%. Potential sources of hedge ineffectiveness are a reduction or modification in the hedged item or a material change in the credit risk of swap counterparties.

A foreign currency exposure arises from foreign exchange fluctuations on translation of the Group's euro debt into GBP. The hedged risk is the risk of changes in the GBPEUR spot rate that will result in changes in the value of the euro debt when translated into GBP. The hedged items are a portion of the Group's euro bonds. The hedging instruments are floating to floating cross currency swaps which mitigates an exposure to the effect of euro strengthening against GBP within the hedge item. The final exchange on the cross currency swap creates an exposure to euro weakening against GBP.

As the critical terms of the cross-currency swap match the bonds there is an expectation that the value of the hedging instrument and the value of the hedged item move in the opposite direction as a result of movements in the EURGBP exchange rate. The hedge ratio is 100%. Potential sources of hedge ineffectiveness are a reduction or modification in the hedged item or a material change in the credit risk of swap counterparties.

The Group held the following instruments to hedge exposures to changes in interest rates and foreign currency risk associated with borrowings:

16. Derivative financial instruments and hedge accounting continued

			2020
All figures in £ millions	Carrying amount of hedging instruments	Change in fair value of hedging instrument used to determine hedge ineffectiveness	Nominal amounts of hedging instruments
Derivative financial instruments for interest rate risk	**12**	**–**	**354**
Derivative financial instruments for currency risk	**44**	**19**	**354**

			2019
All figures in £ millions	Carrying amount of hedging instruments	Change in fair value of hedging instrument used to determine hedge ineffectiveness	Nominal amounts of hedging instruments
Derivative financial instruments for interest rate risk	13	–	336
Derivative financial instruments for currency risk	25	(21)	336

The amounts at the reporting date relating to items designated as hedge items were as follows:

					2020
All figures in £ millions	Carrying amount of hedged items	Accumulated amount of fair value hedge adjustments on the hedged item included in the carrying amount	Change in fair value of hedged item used to determine hedge ineffectiveness	Hedge ineffectiveness	Line item in profit or loss that includes hedge ineffectiveness
Interest rate risk					
Financial liabilities – borrowings	**(367)**	**(9)**	**–**	**–**	**n/a**
Currency risk					
Financial liabilities – borrowings	**(367)**	**n/a**	**(19)**	**–**	**n/a**

					2019
All figures in £ millions	Carrying amount of hedged items	Accumulated amount of fair value hedge adjustments on the hedged item included in the carrying amount	Change in fair value of hedged item used to determine hedge ineffectiveness	Hedge ineffectiveness	Line item in profit or loss that includes hedge ineffectiveness
Interest rate risk					
Financial liabilities – borrowings	(347)	(9)	–	–	n/a
Currency risk					
Financial liabilities – borrowings	(347)	n/a	21	–	n/a

Hedge of net investment in a foreign operation

A foreign currency exposure arises from the translation of the Group's net investments in its subsidiaries which have USD, EUR and BRL functional currencies. The hedged risk is the risk of changes in the GBPUSD, GBPEUR and GBPBRL spot rates that will result in changes in the value of the Group's net investment in its USD, EUR and BRL assets when translated into GBP. The hedged items are a portion of the Group's assets which are denominated in USD, EUR and BRL. The hedging instruments are debt and derivative financial instruments, including Cross Currency Swaps, FX forwards (including non-deliverable forwards) and FX collars which mitigates an exposure to the effect of a weakening USD, EUR or BRL on the hedged item against GBP.

It is expected that the change in value of each of these items will mirror each other as there is a clear and direct economic relationship between the hedging instrument and the hedged item in the hedge relationship.

Hedge ineffectiveness would arise if the value of the hedged items fell below the value of the hedging instruments, however, this is unlikely as the value of the Group's assets denominated in USD, EUR and BRL are significantly greater than the proposed net investment programme.

Notes to the consolidated financial statements

16. Derivative financial instruments and hedge accounting continued

The amounts related to items designated as hedging instruments were as follows:

					2020
All figures in £ millions	Carrying amount of hedging instruments	Change in value of hedging instrument used to determine hedge ineffectiveness	Nominal amounts of hedging instruments	Hedging gains/(losses) recognised in OCI	Hedge ineffectiveness recognised in profit or loss
Derivative financial instruments	(17)	3	(355)	3	–
Financial liabilities – borrowings	(246)	1	(246)	1	–

					2019
All figures in £ millions	Carrying amount of hedging instruments	Change in value of hedging instrument used to determine hedge ineffectiveness	Nominal amounts of hedging instruments	Hedging gains/(losses) recognised in OCI	Hedge ineffectiveness recognised in profit or loss
Derivative financial instruments	(21)	13	(722)	13	–
Financial liabilities – borrowings	(246)	10	(246)	10	–

In addition to the above, £15m (2019: £3m) of hedging gains were recognised in OCI in relation to derivative financial instruments that matured during the year. A total of £14m (2019: £nil) of losses accumulated in translation reserve are reclassified to profit and loss as a result of the disposal of Penguin Random House in April 2020. Included in the translation reserve is a cost of hedging reserve relating to the time value of FX collars which is not separately disclosed due to materiality. Value of that reserve will decrease over the life of the hedge transaction. Balance as at 1 January and 31 December 2020 was £2m.

Offsetting arrangements with derivative counterparties

All of the Group's derivative financial instruments are subject to enforceable netting arrangements with individual counterparties, allowing net settlement in the event of default of either party. Derivative financial assets and liabilities subject to offsetting arrangements are as follows:

			2020			2019
All figures in £ millions	Gross derivative assets	Gross derivative liabilities	Net derivative assets/ liabilities	Gross derivative assets	Gross derivative liabilities	Net derivative assets/ liabilities
Counterparties in an asset position	35	(10)	25	52	(34)	18
Counterparties in a liability position	28	(42)	(14)	2	(5)	(3)
Total as presented in the balance sheet	63	(52)	11	54	(39)	15

All of the Group's derivative financial instruments are subject to enforceable netting arrangements with individual counterparties, allowing net settlement in the event of default of either party. Offset arrangements in respect of cash balances are described in note 17.

Counterparty exposure from all derivatives is managed, together with that from deposits and bank account balances, within credit limits that reflect published credit ratings and by reference to other market measures (e.g. market prices for credit default swaps) to ensure that there is no significant exposure to any one counterparty's credit risk.

The Group has no material embedded derivatives that are required to be separately accounted for in accordance with IFRS 9 'Financial Instruments'.

17. Cash and cash equivalents (excluding overdrafts)

All figures in £ millions	2020	2019
Cash at bank and in hand	599	401
Short-term bank deposits	498	36
	1,097	437

Short-term bank deposits are invested with banks and earn interest at the prevailing short-term deposit rates.

At the end of 2020, the currency split of cash and cash equivalents was US dollar 14% (2019: 30%), sterling 64% (2019: 12%), and other 22% (2019: 58%).

Cash and cash equivalents have fair values that approximate to their carrying value due to their short-term nature.

17. Cash and cash equivalents (excluding overdrafts) continued

Cash and cash equivalents include the following for the purpose of the cash flow statement:

All figures in £ millions	2020	2019
Cash and cash equivalents	**1,116**	437
Bank overdrafts	**(3)**	(3)
	1,113	434

The cash and cash equivalents balance of £1,116m includes £19m (2019: nil) classified as held for sale. The Group has certain cash pooling arrangements in US dollars, Sterling, Euro and Canadian dollars where both the company and the bank have a legal right of offset. Offsetting amounts are presented gross in the balance sheet. Offset arrangements in respect of derivatives are shown in note 16.

18. Financial liabilities – borrowings

The Group's current and non-current borrowings are as follows:

All figures in £ millions	2020	2019
Non-current		
1.875% euro notes 2021 (nominal amount €195m)	**–**	170
3.75% US dollar notes 2022 (nominal amount $117m)	**86**	89
3.25% US dollar notes 2023 (nominal amount $94m)	**69**	72
1.375% euro notes 2025 (nominal amount €300m)	**279**	262
3.75% gbp notes 2030 (nominal amount £350m)	**353**	–
Revolving credit facility	**–**	230
Lease liabilities (see note 35)	**610**	749
	1,397	1,572
Current (due within one year or on demand)		
Bank loans and overdrafts	**3**	3
1.875% euro notes 2021 (nominal amount €195m)	**178**	–
Lease liabilities (see note 35)	**73**	89
	254	92
Total borrowings	**1,651**	1,664

Included in the non-current borrowings above is £11m of accrued interest (2019: £5m). Included in the current borrowings above is £2m of accrued interest (2019: £nil). In addition to the above, there are non-current borrowings of £66m (2019: £nil) and current borrowings of £3m (2019: £nil) classified as held for sale (see note 32). The maturities of the Group's non-current borrowings are as follows:

All figures in £ millions	2020	2019
Between one and two years	**160**	251
Between two and five years	**531**	609
Over five years	**706**	712
	1,397	1,572

The carrying amounts and market values of borrowings are as follows:

			2020			2019
All figures in £ millions	Effective interest rate	Carrying value	Market value	Effective interest rate	Carrying value	Market value
Bank loans and overdrafts	**n/a**	**3**	**3**	n/a	3	3
1.875% euro notes 2021	**2.04%**	**178**	**176**	2.04%	170	170
3.75% US dollar notes 2022	**3.94%**	**86**	**88**	3.94%	89	90
3.25% US dollar notes 2023	**3.36%**	**69**	**71**	3.36%	72	72
1.375% euro notes 2025	**1.44%**	**279**	**278**	1.44%	262	263
3.75% gbp notes 2030	**3.93%**	**353**	**404**	–	–	–
Revolving credit facility	**n/a**	**–**	**–**	1.075%	230	230
		968	**1,020**		826	828

Notes to the consolidated financial statements

18. Financial liabilities – borrowings continued

The market values stated above are based on clean market prices at the year end or, where these are not available, on the quoted market prices of comparable debt issued by other companies. The effective interest rates above relate to the underlying debt instruments.

The carrying amounts of the Group's borrowings before the effect of derivatives (see notes 16 and 19 for further information on the impact of derivatives) are denominated in the following currencies:

All figures in £ millions	2020	2019
US dollar	**458**	539
Sterling	**686**	576
Euro	**472**	442
Other	**35**	107
	1,651	1,664

The Group has $1.19bn (£0.9bn) of undrawn capacity on its committed borrowing facilities as at 31 December 2020 (2019: $0.9bn (£0.7bn) undrawn). In addition, 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 lease obligations, the rights to the leased asset revert to the lessor in the event of default.

19. Financial risk management

The Group's approach to the management of financial risks together with sensitivity analyses of its financial instruments is set out below.

Treasury policy

Pearson's treasury policies set out the Group's principles for addressing key financial risks including capital risk, liquidity risk, foreign exchange risk and interest rate risk, and sets out measurable targets for each. The Audit Committee receives quarterly reports incorporating compliance with measurable targets and review, and approve, any changes to treasury policies annually.

The treasury function is permitted to use derivatives where their use reduces a risk or allows a transaction to be undertaken more cost effectively. Derivatives permitted include swaps, forwards and collars to manage foreign exchange and interest rate risk, with foreign exchange swap and forward contracts the most commonly executed. Speculative transactions are not permitted.

Capital risk

The Group's objectives when managing capital are:

- To maintain a strong balance sheet and a solid investment grade rating;
- To continue to invest in the business organically and through acquisitions;
- To have a sustainable and progressive dividend policy; and
- To return surplus cash to our shareholders where appropriate. In response to the COVID-19 outbreak, the Group took a decision to suspend the share buyback programme, which helped to preserve liquidity and maintain the Group's credit metrics. In May 2020 Standard and Poor's downgraded the Group to BBB- (stable) (2019: BBB (negative outlook)) and in August 2020 Moody's downgraded the Group to Baa3 (stable) (2019: Baa2 (stable outlook)), reflecting weaker anticipated results for 2020 as a result of COVID-19. It is anticipated that sales and profit growth will improve the Group's credit position following the end of widespread social distancing and lockdown measures in the Group's major markets.

The Group aimed to maintain net debt at a level less than 1.5 times adjusted EBITDA before the adoption of IFRS 16 and less than 2.2 times adjusted EBITDA after the adoption of IFRS 16. This is consistent with a solid investment-grade rating (assuming no material deterioration in trading performance) and provides comfortable headroom against covenants.

Net debt

The Group's net debt position is set out below:

All figures in £ millions	2020	2019
Cash and cash equivalents	**1,116**	437
Derivative financial instruments	**11**	15
Bank loans and overdrafts	**(3)**	(3)
Bonds	**(965)**	(593)
Revolving credit facility	**–**	(230)
Investment in finance lease receivable	**130**	196
Lease liabilities	**(752)**	(838)
Net debt	**(463)**	(1,016)

Net debt presented above includes borrowings of £69m (2019: nil) and cash and cash equivalents of £19m (2019: nil) which are included in assets and liabilities held for sale.

19. Financial risk management continued

Interest and foreign exchange rate management

The Group's principal currency exposure is to the US dollar which represents more than 60% of the Group's sales.

The Group's long-term debt is primarily held in US dollars to provide a natural hedge of this exposure, which is achieved through issued US dollar debt or converting euro debt to US dollars using cross-currency swaps, forwards and collars. As at 31 December 2020, the Group's debt of £1,651m is all held at fixed rates (2019: fixed rates: £1,641m, floating rates: £23m).

See note 16 for details of the Group's hedging programme which addresses interest rate risk and foreign currency risk.

Overseas profits are converted to sterling to satisfy sterling cash outflows such as dividends at the prevailing spot rate at the time of the transaction. To the extent the Group has sufficient sterling, US dollars may be held as dollar cash to provide a natural offset to the Group's debt or to satisfy future US dollar cash outflows.

The Group does not have significant cross-border foreign exchange transactional exposures.

As at 31 December 2020, the sensitivity of the carrying value of the Group's financial instruments to fluctuations in interest rates and exchange rates is as follows:

					2020
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	**138**	**–**	**–**	**(11)**	**13**
Other receivable	**96**	**–**	**–**	**(9)**	**11**
Cash and cash equivalents	**1,097**	**–**	**–**	**(55)**	**25**
Derivative financial instruments	**11**	**17**	**(19)**	**3**	**1**
Bonds	**(965)**	**9**	**(9)**	**54**	**(67)**
Other borrowings	**(686)**	**–**	**–**	**62**	**(76)**
Investment in finance lease receivable	**130**	**–**	**–**	**(12)**	**14**
Other net financial assets	**463**	**–**	**–**	**(44)**	**40**
Total financial instruments	**284**	**26**	**(28)**	**(12)**	**(39)**

					2019
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	122	–	–	(9)	11
Other receivable	182	–	–	(17)	20
Cash and cash equivalents	437	–	–	(32)	39
Derivative financial instruments	15	16	(18)	22	(23)
Bonds	(593)	11	(12)	53	(64)
Other borrowings	(1,071)	2	(2)	46	(56)
Investment in finance lease receivable	196	–	–	(18)	22
Other net financial assets	560	–	–	(43)	52
Total financial instruments	(152)	29	(32)	2	1

The table above shows the sensitivities of the fair values of each class of financial instrument to an isolated change in either interest rates or foreign exchange rates. Other net financial assets comprises trade receivables less trade payables. A significant proportion of the movements shown above would impact equity rather than the income statement due to the location and functional currency of the entities in which they arise and the availability of net investment hedging.

The Group's income statement is reported at average rates for the year while the balance sheet is translated at the year-end closing rate. Differences between these rates can distort ratio calculations such as debt to EBITDA and interest cover. Adjusted operating profit translated at year-end closing rates would be £25m lower than the reported figure of £313m at £288m. Adjusted EBITDA translated at year-end closing rates would be £38m lower than the reported figure of £550m at £512m.

Liquidity and re-financing risk management

The Group regularly reviews the level of cash and debt facilities required to fund its activities. This involves preparing a prudent cash flow forecast for the next three to five years, determining the level of debt facilities required to fund the business, planning for shareholder returns and repayments of maturing debt, and identifying an appropriate amount of headroom to provide a reserve against unexpected outflows.

At 31 December 2020, the Group had cash of £1.1bn and an outstanding drawing of £nil on the US dollar denominated revolving credit facility due 2024 of $1.19bn (£0.9bn).

The $1.19bn facility contains interest cover and leverage covenants which the Group has complied with for the year ended 31 December 2020. The maturity of the carrying values of the Group's borrowings and trade payables are set out in notes 18 and 24 respectively.

Notes to the consolidated financial statements

19. Financial risk management continued

At the end of 2020, the currency split of the Group's trade payables was US dollar £195m, sterling £76m and other currencies £69m (2019: US dollar £214m, sterling £57m and other currencies £87m). Trade payables are all due within one year (2019: all due within one year).

The table below analyses the Group's bonds and derivative assets and liabilities into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. Short dated derivative instruments have not been included in this table. The amounts disclosed in the table are the contractual undiscounted cash flows (including interest) and as such may differ from the amounts disclosed on the balance sheet.

Financial counterparty and credit risk management

Financial counterparty and credit risk arises from cash and cash equivalents, favourable derivative financial instruments and deposits with banks and financial institutions, as well as credit exposures to customers, including outstanding receivables. Counterparty credit limits, which take published credit rating and other factors into account, are set to cover the Group's total aggregate exposure to a single financial institution. The limits applicable to published credit rating 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.

	Analysed by maturity				Analysed by currency			
All figures in £ millions	Greater than one month and less than one year	Later than one year but less than five years	Five years or more	Total	USD	GBP	Other	Total
At 31 December 2020								
Bonds	**200**	**497**	**416**	**1,113**	**166**	**481**	**466**	**1,113**
Rate derivatives – inflows	**(186)**	**(350)**	**(1)**	**(537)**	**(12)**	**(152)**	**(373)**	**(537)**
Rate derivatives – outflows	**180**	**350**	**12**	**542**	**209**	**330**	**3**	**542**
FX forwards – inflows	**(68)**	**–**	**–**	**(68)**	**–**	**(68)**	**–**	**(68)**
FX forwards – outflows	**68**	**–**	**–**	**68**	**36**	**–**	**32**	**68**
Total	**194**	**497**	**427**	**1,118**	**399**	**591**	**128**	**1,118**
At 31 December 2019								
Bonds	12	354	259	625	177	–	448	625
Rate derivatives – inflows	(19)	(223)	(332)	(574)	(41)	(172)	(361)	(574)
Rate derivatives – outflows	23	237	331	591	242	344	5	591
FX forwards – inflows	(186)	(24)	–	(210)	–	(210)	–	(210)
FX forwards – outflows	186	23	–	209	209	–	–	209
Total	16	367	258	641	587	(38)	92	641

Cash deposits and derivative transactions are made with approved counterparties up to pre-agreed limits. To manage counterparty risk associated with cash and cash equivalents, the Group uses a mixture of money market funds as well as bank deposits. As at 31 December 2020, 88% of cash and cash equivalents was held with investment grade bank counterparties, 9% with AAA money market funds and 3% held with non-investment grade bank counterparties.

For trade receivables and contract assets the Group's exposure to credit risk is influenced mainly by the individual characteristics of each customer. However, risk associated with the industry and country in which customers operate may also influence the credit risk. The credit quality of customers is assessed by taking into account financial position, past experience and other relevant factors. Individual credit limits are set for each customer based on internal ratings. The compliance with credit limits is regularly monitored by the Group. A default on a trade receivable is when the counterparty fails to make contractual payments within the stated payment terms. Trade receivables and contract assets are written off when there is no reasonable expectation of recovery. The carrying amounts of financial assets, trade receivables and contract assets represent the maximum credit exposure.

Trade receivables and contract assets are subject to impairment using the expected credit loss model. The Group applies the IFRS 9 simplified approach to measuring expected credit losses which uses a lifetime expected credit loss allowance for all trade receivables and contract assets. To measure the expected credit losses, trade receivables and contract assets have been grouped based on shared credit risk characteristics and the days past due. See note 22 for further details about trade receivables and contract assets including movements in provisions for bad and doubtful debts.

Amendments to IFRS 9 and IFRS 7 Interest Rate Benchmark Reform

In light of Interest Rate Benchmark Reform and amendments to IFRS 9 and IFRS 7 which Pearson early adopted in 2019, the Group has considered the impact of IBOR reform on Pearson's hedge accounting. In accordance with the transition provisions, the amendments have been adopted retrospectively to hedging relationships that existed at the start of 2019 reporting period or were designated thereafter. The amendments provide temporary relief from applying specific hedge accounting requirements to hedging relationships directly affected by IBOR reform.

The reliefs have the effect that IBOR reform should not generally cause hedge accounting to terminate. However, any hedge ineffectiveness continue should be recorded in the income statement. Furthermore, the amendments set out triggers for when the reliefs will end, which include the uncertainty arising from interest rate benchmark reform no longer being present.

19. Financial risk management continued

Pearson has a limited exposure to changes in the EUR IBOR benchmark. The Group has €395m (£355m) of Interest Rate Swaps which are in fair value hedge relationships. Pearson has considered a IBOR transition plan. Pearson currently anticipates that the areas of greatest change will be amendments to the contractual terms of EUR-IBOR-referenced floating-rate swaps and updating hedge designations.

In summary, the reliefs provided by the amendments that apply to the Group are:

› In assessing whether the hedge is expected to be highly effective on a forward-looking basis, the Group has assumed that the Euribor interest rate on which the cash flows of the interest rate swap that hedges fixed-rate Euro bonds is not altered by IBOR reform;

› The Group will not discontinue hedge accounting during the period of IBOR-related uncertainty solely because the retrospective effectiveness demonstrates ineffectiveness due to IBOR reform. The Group has assessed whether the hedged Euribor risk component is a separately identifiable risk only when it first designates the hedge and not on an ongoing basis.

20. Intangible assets – pre-publication

All figures in £ millions	2020	2019
Cost		
At beginning of year	**2,275**	2,096
Exchange differences	**(48)**	(66)
Additions	**323**	306
Disposals	**(31)**	(82)
Transfer from property, plant and equipment	**–**	9
Transfer (to)/from intangible assets	**(5)**	12
At end of year	**2,514**	2,275
Amortisation		
At beginning of year	**(1,405)**	(1,279)
Exchange differences	**45**	53
Charge for the year	**(280)**	(261)
Disposals	**31**	82
At end of year	**(1,609)**	(1,405)
Carrying amounts at end of year	**905**	870

Included in the above are pre-publication assets amounting to £607m (2019: £585m) which will be realised in more than one year. Amortisation is included in the income statement in cost of goods sold. In addition to the above, in 2019 there was a £10m charge and additions of £13m relating to assets and liabilities held for sale (see note 32).

KE Key areas of estimation

› The recoverability of prepublication assets and in particular the assessment of the useful economic lives of pre-publication assets. The key assumption is the estimate of future potential sales.

Pre-publication assets are assessed for impairment triggers on an annual basis or when triggering events occur. In 2020, the impact of COVID-19 resulted in a full impairment analysis being undertaken on pre-publication assets. The impairment test showed that there is adequate headroom across all pre-publication assets and accordingly no impairment charges were recognised.

21. Inventories

All figures in £ millions	2020	2019
Raw materials	**5**	5
Work in progress	**2**	2
Finished goods	**116**	155
Returns asset	**6**	7
	129	169

The cost of inventories recognised as an expense and included in the income statement in cost of goods sold amounted to £219m (2019: £231m) including £41m (2019: £33m) of inventory provisions. None of the inventory is pledged as security.

Included within the inventory balance is the estimation of the right to receive goods from contracts with customers via returns. The value of the returns asset is measured at the carrying amount of the assets at the time of sale aligned to the Group's normal inventory valuation methodology less any expected costs to recover the asset and any expected reduction in value. Impairment charges against the inventory returns asset are £nil in 2020 (2019: £nil). The returns asset all relates to finished goods.

The year on year reduction in inventories is due to increased provisions for obsolescence and a reduction in the production of inventory due to the Group's digital first strategy.

Notes to the consolidated financial statements

22. Trade and other receivables

All figures in £ millions	2020	2019
Current		
Trade receivables	**795**	903
Royalty advances	**2**	4
Prepayments	**189**	138
Investment in finance lease receivable	**18**	25
Accrued income	**12**	11
Other receivables	**102**	194
	1,118	1,275
Non-current		
Trade receivables	**8**	15
Royalty advances	**3**	–
Prepayments	**13**	7
Investment in finance lease receivable	**112**	171
Accrued income	**1**	5
Other receivables	**86**	115
	223	313

Accrued income represents contract assets which are unbilled amounts generally resulting from assessments and services revenue streams where revenue to be recognised over time has been recognised in excess of customer billings to date. Impairment charges on accrued income assets are £nil (2019: £nil). The carrying value of the Group's trade and other receivables approximates its fair value. Trade receivables are stated net of provisions for bad and doubtful debts. In addition to the above, there are trade receivables of £6m (2019: £nil) classified as held for sale (see note 32).

The movements in the provision for bad and doubtful debts are as follows:

All figures in £ millions	2020	2019
At beginning of year	**(92)**	(96)
Exchange differences	**6**	3
Income statement movements	**(26)**	(35)
Utilised	**32**	36
Transfer to assets classified as held for sale	**6**	–
At end of year	**(74)**	(92)

Concentrations of credit risk with respect to trade receivables are limited due to the Group's large number of customers, who are internationally dispersed.

The ageing of the Group's trade receivables is as follows:

All figures in £ millions	2020	2019
Within due date	**668**	654
Up to three months past due date	**70**	155
Three to six months past due date	**11**	35
Six to nine months past due date	**23**	9
Nine to 12 months past due date	**7**	14
More than 12 months past due date	**24**	51
Net trade receivables	**803**	918

The Group reviews its bad debt provision at least twice a year following a detailed review of receivable balances and historical payment profiles, and assessment of forward looking risk factors. In 2020, this assessment included factors specifically related to the COVID-19 pandemic which resulted in a proportionate increase in the bad debt provision. A significant portion of the trade debtors are covered by insurance contracts. Management believes all the remaining receivable balances are fully recoverable.

The year on year reduction in trade and other receivables is primarily driven by reduced sales, a proportionate increase in provisions for bad debts, the receipt of deferred proceeds in relation to the US K-12 disposal and the disposal of a lease held as an investment in finance lease receivable. This is partially offset by an increase in prepayments due to timing differences on certain significant payments.

23. Provisions for other liabilities and charges

All figures in £ millions	Property	Disposals and closures	Legal and other	Total
At 1 January 2020	16	–	49	65
Exchange differences	–	–	(3)	(3)
Charged to income statement	1	4	11	16
Released to income statement	(2)	–	(5)	(7)
Utilised	(7)	–	(36)	(43)
Transfer from trade and other liabilities	–	–	5	5
At 31 December 2020	8	4	21	33

Analysis of provisions:

All figures in £ millions	Property	Disposals and closures	Legal and other	Total
				2020
Current	2	4	19	25
Non-current	6	–	2	8
	8	4	21	33
				2019
Current	9	–	43	52
Non-current	7	–	6	13
	16	–	49	65

Property provisions in 2020 relate primarily to dilapidations and in 2019 relate to restructuring and dilapidation provisions. Disposals and closures relate to the disposal of Pearson Institute of Higher Education.

Legal and other includes legal claims, contract disputes and potential contract losses with the provisions utilised as the cases are settled. Also included in legal and other are other restructuring provisions that are generally utilised within one year.

The year on year reduction in provisions is mainly due to utilisation of provisions related to the 2017-2019 major restructuring programme.

24. Trade and other liabilities

All figures in £ millions	2020	2019
Trade payables	340	358
Sales return liability	86	122
Social security and other taxes	17	13
Accruals	290	295
Deferred income	356	360
Interest payable	30	28
Other liabilities	157	188
	1,276	1,364
Less: non-current portion		
Deferred income	52	55
Other liabilities	28	31
	80	86
Current portion	1,196	1,278

The carrying value of the Group's trade and other liabilities approximates its fair value. The deferred income balance comprises contract liabilities in respect of advance payments in assessment, testing and training businesses; subscription income in school and college businesses; and obligations to deliver digital content in future periods.

In addition to the above, there are accruals of £2m (2019: £nil) and deferred income of £3m (2019: £nil) classified as held for sale (see note 32).

The decrease in the sales return liability is largely due to the reduction in sales of physical products. Other reductions in trade and other liabilities are primarily due to favourable foreign exchange movements.

Notes to the consolidated financial statements

25. Retirement benefit and other post-retirement obligations

Background

The Group operates a number of defined benefit and defined contribution retirement plans throughout the world.

The largest plan is The Pearson Pension Plan (UK Group plan) in the UK, which is sectionalised to provide both defined benefit and defined contribution pension benefits. The defined benefit section was closed to new members from 1 November 2006. The defined contribution section, opened in 2003, is open to new and existing employees. Finally, there is a separate section within the UK Group plan set up for auto-enrolment. The defined benefit section of the UK Group plan is a final salary pension plan which provides benefits to members in the form of a guaranteed level of pension payable for life. The level of benefits depends on the length of service and final pensionable pay. The UK Group plan is funded with benefit payments from trustee-administered funds. The UK Group plan is administered in accordance with the Trust Deed and Rules in the interests of its beneficiaries by Pearson Group Pension Trustee Limited.

At 31 December 2020, the UK Group plan had approximately 26,500 members, analysed in the following table:

All figures in %	Active	Deferred	Pensioners	Total
Defined benefit	–	19	33	52
Defined contribution	12	36	–	48
Total	12	55	33	100

The other major defined benefit plans are based in the US. These are also final salary pension plans which provide benefits to members in the form of a guaranteed pension payable for life, with the level of benefits dependent on length of service and final pensionable pay. The majority of the US plans are funded.

The Group also has several post-retirement medical benefit plans (PRMBs), principally in the US. PRMBs are unfunded but are accounted for and valued similarly to defined benefit pension plans.

In 2020, due to the November court judgement on GMP equalisation, there is a past service cost recognised in the income statement in respect of the UK Group Plan of £1m.

The defined benefit schemes expose the Group to actuarial risks, such as life expectancy, inflation risks and investment risk including asset volatility and changes in bond yields. The Group is not exposed to any unusual, entity-specific or plan-specific risks.

The defined contribution section of the UK Group plan operates a Reference Scheme Test (RST) pension underpin for its members. Where a member's fund value is insufficient to purchase the RST pension upon retirement, the UK Group plan is liable for the shortfall to cover the member's RST pension. A liability of £67m (2019: £33m) is included in the UK Group plan's defined benefit obligation, representing the net cost of the shortfall to cover RST pensions and fund values being converted to a pension in the UK Group plan. This is calculated as the present value of projected payments less the fund value. From 1 January 2018, members who have sufficient funds to purchase an RST pension are able to convert their fund value into a pension in the UK Group plan as an alternative to purchasing an annuity with an insurer. The Group does not recognise the assets and liabilities for members of the defined contribution section of the UK Group plan whose fund values are expected to be sufficient to purchase an RST pension without assistance from the UK Group plan. Based on experience, an assumption has been made about the proportion of members who will choose to convert their fund value into a pension in the UK Group Plan and this has been taken into account in the calculation of the UK Group Plan's defined benefit obligation. The defined contribution section of the UK Group plan had gross assets of £545m at 31 December 2020 (2019: £512m).

KJ Key judgements

› Whether the Group will be eligible to receive the surplus associated with the UK Group Pension Plan in recognising a pension asset.

KE Key areas of estimation

› The determination of the pension cost and defined benefit obligation of the Group's defined benefit pension schemes depends on the selection of certain assumptions, which include the discount rate, inflation rate, salary growth and longevity.

25. Retirement benefit and other post-retirement obligations continued

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.

			2020			2019
All figures in %	**UK Group plan**	**Other plans**	**PRMB**	**UK Group plan**	**Other plans**	**PRMB**
Inflation	**2.9**	**0.6**	**–**	3.0	1.7	1.5
Rate used to discount plan liabilities	**1.4**	**2.2**	**2.1**	2.0	3.0	3.1
Expected rate of increase in salaries	**3.4**	**2.2**	**3.0**	3.5	2.9	3.0
Expected rate of increase for pensions in payment and deferred pensions	**2.05 to 5.05**	**–**	**–**	1.85 to 5.05	–	–
Initial rate of increase in healthcare rate	**–**	**–**	**6.5**	–	–	6.8
Ultimate rate of increase in healthcare rate	**–**	**–**	**5.0**	–	–	5.0

The UK discount rate is based on corporate bond yields adjusted to reflect the duration of liabilities.

The inflation rate for the UK Group plan of 2.9% reflects the RPI rate. In line with changes to legislation in 2010, certain benefits have been calculated with reference to CPI as the inflationary measure and in these instances a rate of 2.2% has been used. The CPI rate is determined as a weighted average deduction from the RPI rate, and allows for the expected change to the formula for calculating RPI to be in line with CPIH from 2030 onwards.

The expected rate of increase in salaries has been set at 3.4% for 2020.

For the UK Group plan, the mortality base table assumptions have been updated and are derived from the SAPS S2 for males and females, adjusted to reflect the observed experience of the plan, with CMI model improvement factors. A 1.5% long-term rate improvement on the CMI 2019 model is applied for both males and females. The analysis of experience, and standard tables, do not reflect the impact of the ongoing COVID-19 pandemic, the ultimate impact of which remains uncertain.

For the US plans, the mortality table (Pri – 2012) and 2020 improvement scale (MP – 2020) with generational projection for male and female annuitants has been adopted.

Using the above tables, the remaining average life expectancy in years of a pensioner retiring at age 65 on the balance sheet date for the UK Group plan and US plans is as follows:

		UK		US
All figures in years	**2020**	**2019**	**2020**	**2019**
Male	**24.0**	24.0	**20.4**	20.6
Female	**24.3**	24.3	**22.4**	22.6

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
All figures in years	**2020**	**2019**	**2020**	**2019**
Male	**25.6**	25.5	**21.9**	22.2
Female	**26.1**	26.1	**23.8**	24.1

Although the Group anticipates that plan surpluses will be utilised during the life of the plan to address member benefits, the Group recognises its pension surplus in full in respect of the UK Group plan on the basis that it is management's judgement that there are no substantive restrictions on the return of residual plan assets in the event of a winding up of the plan after all member obligations have been met.

Notes to the consolidated financial statements

25. Retirement benefit and other post-retirement obligations continued

Financial statement information

The amounts recognised in the income statement are as follows:

All figures in £ millions	UK Group plan	Defined benefit other	Sub-total	Defined contribution	PRMB	Total
						2020
Current service cost	6	2	8	47	–	55
Past service cost	1	–	1	–	–	1
Curtailments	–	(1)	(1)	–	–	(1)
Administration expenses	5	–	5	–	–	5
Total operating expense	12	1	13	47	–	60
Interest on plan assets	(66)	(3)	(69)	–	–	(69)
Interest on plan liabilities	57	5	62	–	1	63
Net finance (income)/expense	(9)	2	(7)	–	1	(6)
Net income statement charge	3	3	6	47	1	54

All figures in £ millions	UK Group plan	Defined benefit other	Sub-total	Defined contribution	PRMB	Total
						2019
Current service cost	6	3	9	57	–	66
Past service cost	–	–	–	–	–	–
Curtailments	(2)	–	(2)	–	(1)	(3)
Administration expenses	6	–	6	–	–	6
Total operating expense	10	3	13	57	(1)	69
Interest on plan assets	(89)	(5)	(94)	–	–	(94)
Interest on plan liabilities	73	6	79	–	2	81
Net finance (income)/expense	(16)	1	(15)	–	2	(13)
Net income statement charge	(6)	4	(2)	57	1	56

The amounts recognised in the balance sheet are as follows:

All figures in £ millions	UK Group plan	Other funded plans	Other unfunded plans	Total	UK Group plan	Other funded plans	Other unfunded plans	Total
				2020				**2019**
Fair value of plan assets	3,588	119	–	3,707	3,341	120	–	3,461
Present value of defined benefit obligation	(3,178)	(135)	(21)	(3,334)	(2,912)	(138)	(19)	(3,069)
Net pension asset/(liability)	410	(16)	(21)	373	429	(18)	(19)	392
Other post-retirement medical benefit obligation				(39)				(43)
Other pension accruals				(9)				(12)
Net retirement benefit asset				325				337
Analysed as:								
Retirement benefit assets				410				429
Retirement benefit obligations				(85)				(92)

The following gains/(losses) have been recognised in other comprehensive income:

All figures in £ millions	2020	2019
Amounts recognised for defined benefit plans	(24)	(148)
Amounts recognised for post-retirement medical benefit plans	1	3
Total recognised in year	(23)	(145)

25. Retirement benefit and other post-retirement obligations continued

Financial statement information continued

The fair value of plan assets comprises the following:

	2020			2019		
All figures in %	UK Group plan	Other funded plans	Total	UK Group plan	Other funded plans	Total
Insurance	**42**	**–**	**42**	43	–	43
Equities	**1**	**1**	**2**	1	1	2
Bonds	**5**	**1**	**6**	5	2	7
Property	**5**	**–**	**5**	5	–	5
Pooled asset investment funds	**33**	**–**	**33**	30	–	30
Other	**12**	**–**	**12**	13	–	13

The plan assets do not include any of the Group's own financial instruments, or any property occupied by the Group. The table below further disaggregates the plan assets into additional categories and those assets which have a quoted market price in an active market and those that do not:

	2020		2019	
All figures in %	Quoted market price	No quoted market price	Quoted market price	No quoted market price
Insurance	**42**	**–**	43	–
Non-UK equities	**–**	**2**	–	2
Fixed-interest securities	**6**	**–**	7	–
Property	**–**	**5**	–	5
Pooled asset investment funds	**34**	**–**	30	–
Other	**–**	**11**	–	13
Total	**82**	**18**	80	20

The liquidity profile of the UK Group plan assets is as follows:

All figures in %	2020	2019
Liquid – call <1 month	**39**	37
Less liquid – call 1–3 months	**–**	–
Illiquid – call >3 months	**61**	63

Notes to the consolidated financial statements

25. Retirement benefit and other post-retirement obligations continued

Financial statement information continued

Changes in the values of plan assets and liabilities of the retirement benefit plans are as follows:

All figures in £ millions	2020 UK Group plan	2020 Other plans	2020 Total	2019 UK Group plan	2019 Other plans	2019 Total
Fair value of plan assets						
Opening fair value of plan assets	3,341	120	3,461	3,240	141	3,381
Exchange differences	–	(3)	(3)	–	(5)	(5)
Interest on plan assets	66	3	69	89	5	94
Return on plan assets excluding interest	297	8	305	133	13	146
Contributions by employer	3	5	8	3	2	5
Benefits paid	(119)	(14)	(133)	(124)	(16)	(140)
Other	–	–	–	–	(20)	(20)
Closing fair value of plan assets	3,588	119	3,707	3,341	120	3,461
Present value of defined benefit obligation						
Opening defined benefit obligation	(2,912)	(157)	(3,069)	(2,671)	(177)	(2,848)
Exchange differences	–	3	3	–	5	5
Current service cost	(6)	(2)	(8)	(6)	(3)	(9)
Past service cost	(1)	–	(1)	–	–	–
Curtailments	–	1	1	2	–	2
Administration expenses	(5)	–	(5)	(6)	–	(6)
Interest on plan liabilities	(57)	(5)	(62)	(73)	(6)	(79)
Actuarial losses – experience	(18)	(2)	(20)	(6)	(1)	(7)
Actuarial gains – demographic	1	1	2	18	1	19
Actuarial losses – financial	(299)	(11)	(310)	(294)	(12)	(306)
Contributions by employee	–	2	2	–	–	–
Other	–	–	–	–	20	20
Benefits paid	119	14	133	124	16	140
Closing defined benefit obligation	(3,178)	(156)	(3,334)	(2,912)	(157)	(3,069)

The weighted average duration of the defined benefit obligation is 17 years for the UK and eight years for the US.

Changes in the value of the US PRMB are as follows:

All figures in £ millions	2020	2019
Opening defined benefit obligation	(43)	(49)
Exchange differences	1	1
Current service cost	–	–
Curtailments	–	1
Interest on plan liabilities	(1)	(2)
Actuarial gains – experience	3	4
Actuarial gains – demographic	1	1
Actuarial losses – financial	(3)	(2)
Benefits paid	3	3
Closing defined benefit obligation	(39)	(43)

25. Retirement benefit and other post-retirement obligations continued

Funding

The UK Group plan is self-administered with the plan's assets being held independently of the Group in trust. The trustee of the UK Group plan is required to act in the best interest of the plan's beneficiaries. The most recent triennial actuarial valuation for funding purposes was completed as at 1 January 2018 and this valuation revealed a technical provisions funding surplus of £163m. The UK Group plan expects to be able to provide benefits (in accordance with the plan rules) with a very low level of reliance on future funding from the Group.

Assets of the UK Group plan are divided into two elements: matching assets, which are assets that produce cash flows that can be expected to match the cash flows for a proportion of the membership, and include a liability-driven investment mandate (UK bonds, interest rate/inflation swaps and other derivative instruments), pensioner buy-in insurance policies, inflation-linked property and infrastructure, and return seeking assets, which are assets invested with a longer-term horizon to generate the returns needed to provide the remaining expected cash flows for the beneficiaries, and include diversified growth funds, property and alternative asset classes. The UK Group plan's long-term investment strategy allocates 95% to matching assets and 5% to return-seeking assets.

Following the purchase of buy-in policies with Legal & General and Aviva in 2017 and 2019, 95% of the UK Group plan's pensioner liabilities are now matched with buy-in policies. These transfer significant longevity risk to Aviva and Legal & General, reducing the pension risks being underwritten by the Group and providing additional security for members.

Regular employer contributions to the UK Group plan in respect of the defined benefit sections are estimated to be £2m for 2021.

Sensitivities

The effect of a one percentage point increase and decrease in the discount rate on the defined benefit obligation and the total pension expense is as follows:

	2020	
All figures in £ millions	**1% increase**	**1% decrease**
Effect:		
(Decrease)/increase in defined benefit obligation – UK Group plan	(522)	723
(Decrease)/increase in defined benefit obligation – US plan	(11)	13

The effect of members living one year more or one year less on the defined benefit obligation is as follows:

	2020	
All figures in £ millions	**One year increase**	**One year decrease**
Effect:		
Increase/(decrease) in defined benefit obligation – UK Group plan	144	(143)
Increase/(decrease) in defined benefit obligation – US plan	8	(9)

The effect of a half percentage point increase and decrease in the inflation rate is as follows:

	2020	
All figures in £ millions	**0.5% increase**	**0.5% decrease**
Effect:		
Increase/(decrease) in defined benefit obligation – UK Group plan	191	(173)
Increase/(decrease) in defined benefit obligation – US plan	–	–

The above sensitivity analyses are based on a change in an assumption while holding all other assumptions constant, although in practice this is unlikely to occur and changes in some assumptions may be correlated. When calculating these sensitivities, the same method has been applied to calculate the defined benefit obligation as has been applied when calculating the liability recognised in the balance sheet. This methodology is the same as prior periods.

Notes to the consolidated financial statements

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	2020	2019
Pearson plans	29	25

The Group operates the following equity-settled employee option and share plans:

Worldwide Save for Shares Plan – Since 1994, the Group has operated a Save-As-You-Earn plan for UK employees. In 1998, the Group introduced a Worldwide Save for Shares Plan. Under these plans, employees can save a portion of their monthly salary over periods of three or five years. At the end of this period, the employee has the option to purchase ordinary shares with the accumulated funds at a purchase price equal to 80% of the market price prevailing at the time of the commencement of the employee's participation in the plan. Options that are not exercised within six months of the end of the savings period lapse unconditionally.

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 American Depositary Receipts (ADRs) with their accumulated funds at a purchase price equal to 85% of the lower of the market prices prevailing at the beginning or end of the period.

Long-Term Incentive Plan – The plan was first introduced in 2001, renewed again in 2006 and again in 2011. The plan consists of restricted shares. The vesting of restricted shares is normally dependent on continuing service over a three to five-year period, and in the case of Executive Directors and 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 Executive Directors in May 2020 and May 2019 vest dependent on relative total shareholder return, return on invested capital and adjusted earnings per share growth. These awards are in addition to the one-off co-investment award for the Chief Executive, vesting in three equal tranches based on market and non-market performance criteria. The applicable market condition for the vesting of the final tranche is on total shareholder return. Further details of the award are outlined in the Directors' Remuneration Report. Other restricted shares awarded in 2020 and 2019 vest depending on continuing service over periods of up to three years.

Management Incentive Plan – The plan was introduced in 2017 combining the Group's Annual Incentive Plan and Long-Term Incentive Plan for senior management. The number of shares to be granted to participants is dependent on Group performance in the calendar year preceding the date of grant (on the same basis as the Annual Incentive Plan). Subsequently, the shares vest dependent on continuing service over a three-year period, and additionally, in the case of the Pearson Executive Management team, upon satisfaction of non-market based performance criteria as determined by the Remuneration Committee. Restricted shares awarded as part of the 2019 Management Incentive Plan were granted in April 2020. Restricted shares awarded as part of the 2020 Management Incentive Plan will be granted in April 2021.

The following shares were granted under restricted share arrangements:

	2020		2019	
	Number of shares 000s	Weighted average fair value £	Number of shares 000s	Weighted average fair value £
Long-Term Incentive Plan	5,598	4.94	2,785	8.09
Management Incentive Plan	696	5.29	1,435	8.49

The fair value of shares granted under the Long-Term Incentive Plan and the Management Incentive Plan that vest unconditionally is determined using the share price at the date of grant. The number of shares expected to vest is adjusted, based on historical experience, to account for potential forfeitures. Participants under the plans are entitled to dividends during the vesting period and therefore the share price is not discounted.

Restricted shares with a market performance condition were valued by an independent actuary using a Monte Carlo model. Restricted shares with a non-market performance condition were fair valued based on the share price at the date of grant. Non-market performance conditions are taken into consideration by adjusting the number of shares expected to vest based on the most likely outcome of the relevant performance criteria.

27. Share capital and share premium

	Number of shares 000s	Share capital £m	Share premium £m
At 1 January 2019	781,078	195	2,607
Issue of ordinary shares – share option schemes	1,021	–	7
Purchase of own shares	–	–	–
At 31 December 2019	782,099	195	2,614
Issue of ordinary shares – share option schemes	**1,236**	**–**	**6**
Purchase of own shares	**(30,077)**	**(7)**	**–**
At 31 December 2020	**753,258**	**188**	**2,620**

The ordinary shares have a par value of 25p per share (2019: 25p per share). All issued shares are fully paid. All shares have the same rights.

A £350m share buyback programme was announced January 2020, the programme was later paused due to the impact of COVID-19. The original intention was to buyback approximately £350m of shares and at the date of pausing the programme approximately 30m shares had been bought back and cancelled at a cost of £176m. There are currently no plans to resume the share buyback programme. The shares bought back have been cancelled and the nominal value of these shares transferred to a capital redemption reserve. The nominal value of shares cancelled at 31 December 2020 was £18m (2019: £11m).

The Group manages its capital to ensure that entities in the Group will be able to continue as a going concern while maximising the return to shareholders through the optimisation of the debt and equity balance.

The capital structure of the Group consists of debt (see note 18), cash and cash equivalents (see note 17) and equity attributable to equity holders of the parent, comprising issued capital, reserves and retained earnings.

The Group reviews its capital structure on a regular basis and will balance its overall capital structure through payments of dividends, new share issues as well as the issue of new debt or the redemption of existing debt in line with the financial risk policies outlined in note 19.

28. Treasury shares

	Number of shares 000s	£m
At 1 January 2019	3,225	33
Purchase of treasury shares	6,100	52
Release of treasury shares	(6,067)	(61)
At 31 December 2019	3,258	24
Purchase of treasury shares	**1,105**	**6**
Release of treasury shares	**(3,460)**	**(23)**
At 31 December 2020	**903**	**7**

The Group holds Pearson plc shares in trust to satisfy its obligations under its restricted share plans (see note 26). These shares, representing 0.1% (2019: 0.4%) of called-up share capital, are treated as treasury shares for accounting purposes and have a par value of 25p per share.

The nominal value of Pearson plc treasury shares amounts to £0.2m (2019: £0.8m). Dividends on treasury shares are waived.

At 31 December 2020, the market value of Pearson plc treasury shares was £6m (2019: £21m).

Notes to the consolidated financial statements

29. Other comprehensive income

All figures in £ millions	Attributable to equity holders of the company				Non-controlling interest	Total
2020	Fair value reserve	Translation reserve	Retained earnings	Total		
Items that may be reclassified to the income statement						
Net exchange differences on translation of foreign operations – Group	–	(109)	–	(109)	–	(109)
Net exchange differences on translation of foreign operations – associates	–	–	–	–	–	–
Currency translation adjustment disposed	–	(70)	–	(70)	–	(70)
Attributable tax	–	–	(13)	(13)	–	(13)
Items that are not reclassified to the income statement						
Fair value gain on other financial assets	14	–	–	14	–	14
Attributable tax	–	–	(6)	(6)	–	(6)
Remeasurement of retirement benefit obligations – Group	–	–	(23)	(23)	–	(23)
Remeasurement of retirement benefit obligations – associates	–	–	–	–	–	–
Attributable tax	–	–	2	2	–	2
Other comprehensive (expense)/income for the year	14	(179)	(40)	(205)	–	(205)

All figures in £ millions	Attributable to equity holders of the company				Non-controlling interest	Total
2019	Fair value reserve	Translation reserve	Retained earnings	Total		
Items that may be reclassified to the income statement						
Net exchange differences on translation of foreign operations – Group	–	(113)	–	(113)	–	(113)
Net exchange differences on translation of foreign operations – associates	–	(2)	–	(2)	–	(2)
Currency translation adjustment disposed	–	4	–	4	–	4
Attributable tax	–	–	5	5	–	5
Items that are not reclassified to the income statement						
Fair value gain on other financial assets	20	–	–	20	–	20
Attributable tax	–	–	(4)	(4)	–	(4)
Remeasurement of retirement benefit obligations – Group	–	–	(145)	(145)	–	(145)
Remeasurement of retirement benefit obligations – associates	–	–	(4)	(4)	–	(4)
Attributable tax	–	–	22	22	–	22
Other comprehensive (expense)/income for the year	20	(111)	(126)	(217)	–	(217)

30. Business combinations

There were no significant acquisitions in 2020. In 2019, the Group made some small acquisitions for total consideration of £40m. Details of the assets acquired and the associated consideration are shown in the table below.

all figures in £ millions	2020	2019
Intangible assets	–	23
Trade and other receivables	–	1
Trade and other liabilities	–	(2)
Net assets acquired	–	22
Goodwill	–	18
Total	–	40
Satisfied by:		
Cash	–	40
Total consideration	–	40

There were no material adjustments to prior year acquisitions in 2019. The net cash outflow on acquisition of subsidiaries in 2020 relates to deferred payments for prior year acquisitions.

All figures in £ millions	2020	2019
Cash flow on acquisitions		
Cash – current year acquisitions	–	(40)
Deferred payments for prior year acquisitions and other items	**(6)**	(5)
Net cash outflow	**(6)**	(45)

Notes to the consolidated financial statements

31. Disposals

In April 2020, the Group completed the sale of the remaining 25% interest in Penguin Random House resulting in a pre-tax profit of £180m. There were no other disposals in 2020 and additional gains of £4m relate to adjustments to prior year disposal costs. In 2019, the only material disposal was the sale of the US K-12 business in March 2019. Deferred proceeds relating to the K-12 sale were received in 2020 (see note 14 for further details).

All figures in £ millions	Notes	2020 Total	2019 Total
Disposal of subsidiaries and associates			
Intangible assets		–	(101)
Investments in joint ventures and associates		(418)	–
Intangible assets – pre-publication		–	(238)
Inventories		–	(64)
Trade and other receivables		–	(70)
Cash and cash equivalents (excluding overdrafts)		–	(104)
Net deferred income tax assets		–	(100)
Trade and other liabilities		–	520
Cumulative currency translation adjustment	29	70	(4)
Net assets disposed		(348)	(161)
Cash received		531	20
Deferred proceeds		–	180
Costs of disposal		1	(23)
Gain on disposal		184	16

All figures in £ millions	2020	2019
Cash flow from disposals		
Proceeds – current year disposals	531	20
Proceeds – prior year disposals	105	–
Cash and cash equivalents disposed	–	(104)
Costs and other disposal liabilities paid	(5)	(17)
Net cash inflow/(outflow)	631	(101)
Analysed as:		
Cash inflow/(outflow) from sale of subsidiaries	100	(101)
Cash inflow from disposal of joint ventures and associates	531	–

32. Held for sale

The held for sale assets and liabilities in 2020 are the Group's interests in Pearson Institute of Higher Education (PIHE) in South Africa following announcement of the sale in November 2020. The sale of PIHE was completed on 5 February 2021 (see note 37). A charge of £8m has been recognised in other net gains and losses in relation to the disposal of PIHE. The charge reduces the carrying value of the assets and liabilities held for sale to their fair value based on expected disposal proceeds net of costs to sell. Held for sale assets in 2019 relate to the 25% holding in Penguin Random House prior to its disposal in April 2020. The held for sale balances are analysed as follows:

	2020	2019
All figures in £ millions	**Total**	**Total**
Non-current assets		
Property, plant and equipment	**48**	–
Investments in joint ventures and associates	**–**	397
	48	397
Current assets		
Trade and other receivables	**6**	–
Cash and cash equivalents	**19**	–
	25	–
Assets classified as held for sale	**73**	397
Non-current liabilities		
Financial liabilities – borrowings	**(66)**	–
	(66)	–
Current liabilities		
Trade and other liabilities	**(5)**	–
Financial liabilities – borrowings	**(3)**	
	(8)	–
Liabilities classified as held for sale	**(74)**	–
Net (liabilities)/assets classified as held for sale	**(1)**	397

Goodwill is allocated to the held for sale businesses on a relative fair value basis where these businesses form part of a larger cash generating unit (CGU).

The Group has historically presented the results of Penguin Random House separately within segment information (see note 2) to provide further information about the composition of the Group outside of the primary segments. The Group has not viewed Penguin Random House as comprising a separate major line of business since the sale of 22% of the Group's stake in Penguin Random House to Bertelsmann in 2017. On this basis, the Group did not classify Penguin Random House as a discontinued operation.

Notes to the consolidated financial statements

33. Cash generated from operations

All figures in £ millions	Notes	2020	2019
Profit		**310**	266
Adjustments for:			
Income tax		**44**	(34)
Depreciation	10	**125**	123
Amortisation and impairment of acquired intangibles and goodwill	11	**80**	151
Amortisation of software	11	**112**	115
Net finance costs	6	**57**	43
Share of results of joint ventures and associates	12	**(5)**	(54)
Profit on disposal of subsidiaries, associates, investments and fixed assets		**(182)**	(9)
Other net gains and losses		**6**	–
Net profit on disposal of right-of-use assets including transfers to investment in finance lease receivable		**(6)**	(4)
Net foreign exchange adjustment from transactions		**(34)**	(21)
Investment income		**–**	(2)
Share-based payment costs	26	**29**	25
Pre-publication		**(56)**	(55)
Inventories		**35**	(20)
Trade and other receivables		**(1)**	59
Trade and other liabilities		**(26)**	(157)
Retirement benefit obligations		**(1)**	5
Provisions for other liabilities and charges		**(37)**	49
Net cash generated from operations		**450**	480
Dividends from joint ventures and associates		**4**	64
Purchase of property, plant and equipment		**(53)**	(55)
Addition of new right-of-use lease assets		**(61)**	(64)
Purchase of intangible assets		**(81)**	(138)
Proceeds from sale of property, plant and equipment		**–**	1
Net disposal of right-of-use lease assets including transfers to/from investment in finance lease receivable		**18**	17
Investment income		**–**	2
Net costs paid for major restructuring		**38**	111
Operating cash flow		**315**	418
Operating tax paid		**(10)**	(9)
Net operating finance costs paid		**(50)**	(64)
Operating free cash flow		**255**	345
Non-operating tax received/(paid)		**12**	(21)
Net costs paid for major restructuring		**(38)**	(111)
Free cash flow		**229**	213
Dividends paid (including to non-controlling interests)		**(147)**	(148)
Net movement of funds from operations		**82**	65
Acquisitions and disposals		**619**	(193)
Loans repaid/(advanced)		**48**	(49)
New equity		**6**	7
Buyback of equity		**(176)**	–
Purchase of treasury shares		**(6)**	(52)
Other movements on financial instruments		**(29)**	(9)
Net movement of funds		**544**	(231)
Exchange movements on net debt		**9**	24
Movement in net debt		**553**	(207)
Opening net debt		**(1,016)**	(143)
Adjustment on initial application of IFRS 16		**–**	(666)
Closing net debt		**(463)**	(1,016)

33. Cash generated from operations continued

Net cash generated from operations is translated at an exchange rate approximating the rate at the date of cash flow. The difference between this rate and the average rate used to translate profit gives rise to a currency adjustment in the reconciliation between net profit and net cash generated from operations. This adjustment reflects the timing difference between recognition of profit and the related cash receipts or payments.

Operating cash flow, operating free cash flow and total free cash flow are non-GAAP (non-statutory) measures and have been disclosed and reconciled in the above table as they are commonly used by investors to measure the cash performance of the Group. In the cash flow statement, proceeds from sale of property, plant and equipment comprise:

All figures in £ millions	2020	2019
Net book amount	**2**	3
Loss on sale of property, plant and equipment	**(2)**	(2)
Proceeds from sale of property, plant and equipment	**–**	1

The movements in the Group's current and non-current borrowings are as follows:

All figures in £ millions	2019	New leases/ disposal of leases	Transfer from non-current to current	Financing cash flows	Foreign exchange movements	Fair value and other movements	2020
Financial liabilities							
Non-current borrowings	1,567	30	(260)	116	(22)	27	**1,458**
Current borrowings	79	(6)	260	(92)	5	2	**248**
Total	1,646	24	–	24	(17)	29	**1,706**

Non-current borrowings include bonds, derivative financial instruments and leases. Current borrowings include loans repayable within one year, derivative financial instruments and leases, but exclude overdrafts classified within cash and cash equivalents.

34. Contingencies and commitments

KJ Key judgements

› The application of tax legislation in relation to provisions for uncertain tax positions.

KE Key areas of estimation

› The level of provisions required in relation to uncertain tax positions is complex and each matter is separately assessed. The estimation of future settlement amounts is based on a number of factors including the status of the unresolved matter, clarity of legislation, range of possible outcomes and the statute of limitations.

There are contingent Group liabilities that arise in the normal course of business in respect of indemnities, warranties and guarantees in relation to former subsidiaries and in respect of guarantees in relation to subsidiaries, joint ventures and associates. In addition, there are contingent liabilities of the Group in respect of unsettled or disputed tax liabilities, legal claims, contract disputes, royalties, copyright fees, permissions and other rights. None of these claims are expected to result in a material gain or loss to the Group.

On 25 April 2019, the European Commission published the full decision that the United Kingdom controlled foreign company group financing partial exemption (FCPE) partially constitutes State Aid. The Group has lodged an appeal. The Group has benefited from the FCPE in 2018 and prior years by approximately £116m (which does not include additional interest that would be due if this amount had to be repaid). Post year end Pearson received Charging Notices requiring a payment on account of materially all of the alleged State Aid to be made. The Group continues to be of the view that no provision is required in respect of this issue.

The Group is under assessment from the tax authorities in Brazil challenging the deduction for tax purposes of goodwill amortisation for the years 2012 to 2017. Similar assessments may be raised for other years. Potential total exposure (including possible interest and penalties) could be up to BRL 754m (£106m) up to 31 December 2020, with additional potential exposure of BRL 142m (£20m) in relation to deductions expected to be taken in future periods. Such assessments are common in Brazil. The Group believes that the likelihood that the tax authorities will ultimately prevail is low and that the Group's position is strong. At present, the Group believes no provision is required.

Pearson is one of several defendants named in 14 US lawsuits and one Canadian antitrust lawsuit related to the Group's Inclusive Access programmes. These lawsuits, purporting to be class actions, have been brought on behalf of students and off campus retailers alleging, among other things, that Pearson's Inclusive Access programmes violate US and Canadian antitrust laws and state or provincial laws by reducing competition from the secondary market and off campus retailers. Motions to dismiss have been filed by all defendants in the US lawsuits and a ruling is expected later in 2021. At present, the Group believes no provision is required in relation to these matters.

At the balance sheet date there were no commitments for capital expenditure contracted for but not yet incurred. Commitments in respect of leases are shown in note 35.

Notes to the consolidated financial statements

35. Leases

The Group's lease portfolio consists of approximately 740 property leases, mainly offices and test centres, together with a number of vehicle and equipment leases. The Group adopted IFRS 16 'Leases' at 1 January 2019 and applied the modified retrospective approach. The Group has elected not to recognise right-of-use assets and lease liabilities for short-term leases that have a lease term of 12 months or less and leases of low value assets. The Group recognises the lease payments associated with these leases as an expense on a straight-line basis over the lease term.

As a lessee:

The amounts recognised in the income statement are as follows:

All figures in £ millions	Note	2020	2019
Interest on lease liabilities		**(41)**	(45)
Expenses relating to short-term leases		**(1)**	(2)
Depreciation of right-of-use assets	10	**(68)**	(64)

Lease liabilities are included within financial liabilities – borrowings in the balance sheet, see note 18. The maturities of the Group's lease liabilities are as follows:

All figures in £ millions	2020	2019
Less than one year	**100**	123
One to five years	**333**	420
More than five years	**441**	622
Total undiscounted lease liabilities	**874**	1,165
Lease liabilities included in the balance sheet	**683**	838
Analysed as:		
Current	**73**	89
Non-current	**610**	749

In addition to the above, there are current lease liabilities of £3m (2019: £nil) and non-current lease liabilities of £66m classified as held for sale (see note 32).

The amounts recognised in the cash flow statement are as follows:

All figures in £ millions	2020	2019
Total cash outflow for leases as a lessee	**133**	136

At the balance sheet date commitments for capital leases contracted for but not yet incurred were £3m. Extension and termination options and variable lease payments are not significant within the lease portfolio. Short-term leases to which the Group is committed at the balance sheet date are similar to the portfolio of short-term leases to which the short-term lease expense is disclosed above.

As a lessor:

In the event that the Group has excess capacity in its leased offices and warehouses, the Group sub-leases some of its properties under operating and finance leases.

The amounts recognised in the income statement are as follows:

All figures in £ millions	2020	2019
Interest on lease receivables	**9**	11
Income from sub-leasing right-of-use assets (within other income)	**7**	17

The amounts recognised in the cash flow statement are as follows:

All figures in £ millions	2020	2019
Total cash inflow for leases as a lessor	**50**	37

35. Leases continued

The following table sets out the maturity analysis of lease payments receivable for sub-leases classified as operating leases, showing the undiscounted lease payments to be received after the reporting date, and sub-leases classified as finance leases showing the undiscounted lease payments to be received after the reporting date and the net investment in the finance lease receivable. During the year the investment in finance lease receivable decreased by £66m (2019: decreased £19m) due to payments received and the disposal of a lease.

All figures in £ millions	Operating leases	Finance leases	2020 Total	2019 Total
Less than one year	1	23	**24**	46
One to two years	–	24	**24**	44
Two to three years	–	18	**18**	37
Three to four years	–	18	**18**	33
Four to five years	–	18	**18**	34
More than five years	3	53	**56**	87
Total undiscounted lease payments receivable	4	154	**158**	281
Unearned finance income		(24)		
Net investment in finance lease receivable		130		

36. Related party transactions

Joint ventures and associates

In 2020, the Group disposed of its interests in Penguin Random House and therefore Penguin Random House is no longer a related party. Prior to the completion of the sale of Penguin Random House, the Group received dividends of £1m (2019: £64m) from Penguin Random House. Loans to Penguin Random House of £49m which were outstanding at 31 December 2019 were repaid at the point of disposal.

Key management personnel

Key management personnel are deemed to be the members of the Pearson Executive Management team (see p72). It is this Committee which had responsibility for planning, directing and controlling the activities of the Group in 2020. Key management personnel compensation is disclosed below:

All figures in £millions	2020	2019
Short-term employee benefits	**6**	5
Retirement benefits	**1**	1
Share-based payment costs	**6**	4
Total	**13**	10

There were no other material related party transactions. No guarantees have been provided to related parties.

37. Events after the balance sheet date

On 5 February 2021, the Group completed the sale of its interests in Pearson Institute of Higher Education in South Africa. Consideration received was nominal.

In February 2021, the Group received charging notices requiring payment of materially all of the alleged State Aid (see note 34 for further details). A payment of £100m was made on 8 March 2021. The Group expects to recover the funds in due course.

In February 2021, the Group renegotiated its revolving credit facility, extending the maturity of $1bn of the facility by one year to 2025.

On 5 March 2021, the Group agreed the disposal of its K-12 Sistemas – COC and Dom Bosco – in Brazil, subject to securing regulatory approval and closing.

On 8 March 2021, the Group announced a new strategy including a new divisional structure. Going forward the new structure will impact segmental reporting and may impact the Group's cash generating units.

Notes to the consolidated financial statements

38. Accounts and audit exemptions

The Pearson plc subsidiary companies listed below are exempt from the requirements of the Companies Act 2006 relating to the audit of individual accounts by virtue of section 479A.

	Company number
Aldwych Finance Limited	04720439
Edexcel Limited	04496750
Education Development International plc	03914767
Longman Group (Overseas Holdings) Limited	00690236
Major123 Limited	05333023
Pearson Australia Finance Unlimited	05578463
Pearson Books Limited	02512075
Pearson Brazil Finance Limited	08848874
Pearson Canada Finance Unlimited	05578491
Pearson Dollar Finance plc	05111013
Pearson Dollar Finance Two Limited	06507766
Pearson Education Holdings Limited	00210859
Pearson Education Investments Limited	08444933
Pearson Education Limited	00872828
Pearson Funding Four Limited	07970304
Pearson International Finance Limited	02496206
Pearson Loan Finance No. 3 Limited	05052661

	Company number
Pearson Loan Finance No. 4 Limited	02635107
Pearson Loan Finance No. 5 Limited	12017252
Pearson Loan Finance No. 6 Limited	12030662
Pearson Loan Finance Unlimited	05144467
Pearson Management Services Limited	00096263
Pearson Overseas Holdings Limited	00145205
Pearson Pension Trustee Services Limited	10803853
Pearson Strand Limited	08561316
Pearson Real Estate Holdings Limited	09768242
Pearson Services Limited	01341060
Pearson Shared Services Limited	04623186
Pearson Strand Finance Limited	11091691
PVNT Limited	08038068
TQ Catalis Limited	07307943
TQ Clapham Limited	07307925
TQ Global Limited	07802458

Company balance sheet

As at 31 December 2020

All figures in £ millions	Notes	2020	2019
Assets			
Non-current assets			
Investments in subsidiaries	2	**6,619**	6,664
Amounts due from subsidiaries		**2,164**	2,122
Deferred income tax assets		**11**	21
Financial assets – derivative financial instruments	6	**45**	29
		8,839	8,836
Current assets			
Amounts due from subsidiaries		**676**	827
Amounts due from related parties	11	**–**	48
Current income tax assets		**18**	2
Cash and cash equivalents (excluding overdrafts)	4	**541**	18
Financial assets – derivative financial instruments	6	**18**	25
Other assets		**3**	2
		1,256	922
Total assets		**10,095**	9,758
Liabilities			
Non-current liabilities			
Amounts due to subsidiaries		**(4,104)**	(2,740)
Financial liabilities – borrowings	5	**–**	(230)
Financial liabilities – derivative financial instruments	6	**(40)**	(24)
		(4,144)	(2,994)
Current liabilities			
Amounts due to subsidiaries		**(1,382)**	(1,800)
Other liabilities		**(1)**	(5)
Financial liabilities – derivative financial instruments	6	**(12)**	(15)
		(1,395)	(1,820)
Total liabilities		**(5,539)**	(4,814)
Net assets		**4,556**	4,944
Equity			
Share capital	7	**188**	195
Share premium	7	**2,620**	2,614
Treasury shares	8	**(7)**	21
Capital redemption reserve		**18**	11
Special reserve		**447**	447
Retained earnings – including loss for the year of £95m (2019: profit of £764m)		**1,290**	1,656
Total equity attributable to equity holders of the company		**4,556**	4,944

These financial statements have been approved for issue by the Board of Directors on 15 March 2021 and signed on its behalf by

Sally Johnson
Chief Financial Officer

Company statement of changes in equity

Year ended 31 December 2020

	Equity attributable to equity holders of the company						
All figures in £ millions	**Share capital**	**Share premium**	**Treasury shares**	**Capital redemption reserve**	**Special reserve**	**Retained earnings**	**Total**
At 1 January 2020	**195**	**2,614**	**21**	**11**	**447**	**1,656**	**4,944**
Loss for the year	**–**	**–**	**–**	**–**	**–**	**(95)**	**(95)**
Equity-settled transactions[1]	**–**	**–**	**–**	**–**	**–**	**29**	**29**
Issue of ordinary shares under share option schemes[1]	**–**	**6**	**–**	**–**	**–**	**–**	**6**
Buyback of equity	**(7)**	**–**	**–**	**7**	**–**	**(176)**	**(176)**
Purchase of treasury shares	**–**	**–**	**(6)**	**–**	**–**	**–**	**(6)**
Release of treasury shares	**–**	**–**	**23**	**–**	**–**	**(23)**	**–**
Transfer of contributions from subsidiaries	**–**	**–**	**(45)**	**–**	**–**	**45**	**–**
Capital reduction	**–**	**–**	**–**	**–**	**–**	**–**	**–**
Dividends	**–**	**–**	**–**	**–**	**–**	**(146)**	**(146)**
At 31 December 2020	**188**	**2,620**	**(7)**	**18**	**447**	**1,290**	**4,556**

	Equity attributable to equity holders of the company						
All figures in £ millions	**Share capital**	**Share premium**	**Treasury shares**	**Capital redemption reserve**	**Special reserve**	**Retained earnings**	**Total**
At 1 January 2019	195	2,607	12	11	447	1,185	4,457
Profit for the year	–	–	–	–	–	764	764
Equity-settled transactions[1]	–	–	–	–	–	25	25
Issue of ordinary shares under share option schemes[1]	–	7	–	–	–	–	7
Buyback of equity	–	–	–	–	–	–	–
Purchase of treasury shares	–	–	(52)	–	–	–	(52)
Release of treasury shares	–	–	61	–	–	(61)	–
Capital reduction	–	–	–	–	–	(110)	(110)
Dividends	–	–	–	–	–	(147)	(147)
At 31 December 2019	195	2,614	21	11	447	1,656	4,944

The capital redemption reserve reflects the nominal value of shares cancelled in the Group's share buyback programme. The special reserve represents the cumulative effect of cancellation of the company's share premium account.

1 Full details of the share-based payment plans are disclosed in note 26 to the consolidated financial statements.

Company cash flow statement

Year ended 31 December 2020

All figures in £ millions	Notes	2020	2019
Cash flows from operating activities			
Net (loss)/profit		**(95)**	764
Adjustments for:			
Income tax		**(20)**	–
Net finance costs		**95**	29
Share-based payment costs		**29**	25
Amounts due from/(to) subsidiaries		**1,061**	(818)
Net cash generated from operations		**1,070**	–
Interest paid		**(56)**	(26)
Tax received		**15**	7
Net cash generated from/(used in) operating activities		**1,029**	(19)
Cash flows from investing activities			
Loans repaid by/(advanced to) related parties		**48**	(49)
Net cash generated from/(used in) investing activities		**48**	(49)
Cash flows from financing activities			
Proceeds from issue of ordinary shares	7	**6**	7
Buyback of equity		**(182)**	(52)
Repayment of borrowings		**(230)**	–
Proceeds from borrowings		**–**	230
Dividends paid to company's shareholders		**(146)**	(147)
Net cash (used in)/generated from financing activities		**(552)**	38
Effects of exchange rate changes on cash and cash equivalents		**(2)**	9
Net increase/(decrease) in cash and cash equivalents		**523**	(21)
Cash and cash equivalents at beginning of year		**18**	39
Cash and cash equivalents at end of year	4	**541**	18

Notes to the company financial statements

1. Accounting policies

The financial statements on pp199-209 comprise the separate financial statements of Pearson plc.

As permitted by section 408 of the Companies Act 2006, only the consolidated income statement and statement of comprehensive income have been presented.

The company has no employees (2019: nil).

The basis of preparation and accounting policies applied in the preparation of these company financial statements are the same as those set out in note 1a to the consolidated 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.

Lending to/from subsidiaries is considered to be an operating activity and any movements are classified as cash flows from operating activities in the cash flow statement.

Amounts owed by subsidiaries

Amounts owed by subsidiaries generally mature within five years, but can be called upon on short notice, or are repayable on demand. Amounts owed by subsidiaries are classified as current if they mature within one year of the balance sheet date or if the company intends to call the loan within one year of the balance sheet date. All other amounts are classified as non-current. The company has assessed and concluded that these loans will be fully recovered. Therefore credit losses are considered to be immaterial.

New accounting standards

No new standards were adopted in 2020.

A number of other new pronouncements are effective from 1 January 2020 but they do not have a material impact on the company financial statements.

2. Investments in subsidiaries

All figures in £ millions	2020	2019
At beginning of year	**6,664**	6,710
Currency revaluations	**(45)**	(46)
At end of year	**6,619**	6,664

There were no impairments in 2020 or 2019.

The recoverability of investments is tested annually for impairment in accordance with IAS 36 'Impairment of Assets'. The carrying value is compared to the asset's recoverable amount which is generally assessed on a value in use basis. Significant estimation is required to determine the recoverable amount. The value in use of the assets is calculated using a discounted cash flow methodology using financial information related to the subsidiaries including cash flow projections in conjunction with the goodwill impairment analysis performed by the Group. The key assumptions used in the cash flow projections are discount rates, perpetuity growth rates, forecast sales growth rates and forecast operating profits. See note 11 of the consolidated financial statements for further details.

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 borrowings. Derivative financial instruments are held at fair value, with all other financial instruments held at amortised cost, which approximates fair value. 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 consolidated financial statements. The company believes the value of its financial assets to be fully recoverable.

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 £17m increase in the carrying value of its financial instruments, with a 1% decrease in interest rates resulting in a £19m decrease in their carrying value. The company also estimates that a 10% strengthening in sterling would decrease the carrying value of its financial instruments by £123m, while a 10% weakening in the value of sterling would increase the carrying value by £146m. 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%.

3. Financial risk management continued

The following table analyses the company's derivative assets and liabilities into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows (including interest) and as such may differ from the amounts disclosed on the balance sheet.

	Analysed by maturity				Analysed by currency			
All figures in £ millions	Greater than one month and less than one year	Later than one year but less than five years	Five years or more	Total	USD	GBP	Other	Total
At 31 December 2020								
Rate derivatives – inflows	**(186)**	**(350)**	**(1)**	**(537)**	**(12)**	**(152)**	**(373)**	**(537)**
Rate derivatives – outflows	**180**	**350**	**12**	**542**	**209**	**330**	**3**	**542**
FX forwards – inflows	**(68)**	**–**	**–**	**(68)**	**–**	**(68)**	**–**	**(68)**
FX forwards – outflows	**68**	**–**	**–**	**68**	**36**	**–**	**32**	**68**
Total	**(6)**	**–**	**11**	**5**	**233**	**110**	**(338)**	**5**
At 31 December 2019								
Rate derivatives – inflows	(19)	(223)	(332)	(574)	(41)	(172)	(361)	(574)
Rate derivatives – outflows	23	237	331	591	242	344	5	591
FX forwards – inflows	(186)	(24)	–	(210)	–	(210)	–	(210)
FX forwards – outflows	186	23	–	209	209	–	–	209
Total	4	13	(1)	16	410	(38)	(356)	16

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.

Fair value hedge accounting

A foreign currency exposure arises from foreign exchange fluctuations on translation of the company's investments in subsidiaries denominated in USD into GBP. The hedged risk is the risk of changes in the GBPUSD spot rate that will result in changes in the value of the USD investments when translated into GBP. The hedged items are a portion of the company's equity investment in subsidiaries denominated in USD. The hedging instruments are a portion of the company's intercompany loans due from subsidiaries which are denominated in USD.

It is expected that the change in value of each of these items will mirror each other as there is a clear and direct economic relationship between the hedge and the hedged item in the hedge relationship. The hedge ratio is 100%. Hedge ineffectiveness would arise if the value of the hedged items fell below the value of the hedging instruments however this is unlikely as the value of the company's investments denominated in USD are significantly greater than the proposed fair value hedge programme.

The value of the hedged items and the hedging instruments are £1.3bn (2019: £1.3bn) and the change in value during the year which was used to assess hedge ineffectiveness was £45m (2019: £46m). There was no hedge ineffectiveness.

Credit risk management

The company's main exposure to credit risk relates to lending to subsidiaries. Amounts due from subsidiaries are stated net of provisions for bad and doubtful debts. The credit risk of each subsidiary is influenced by the industry and country in which they operate, however, the company considers the credit risk of subsidiaries to be low as it has visibility of, and the ability to influence, their cash flows.

4. Cash and cash equivalents (excluding overdrafts)

All figures in £ millions	2020	2019
Cash at bank and in hand	**541**	18
	541	18

At the end of 2020 the currency split of cash and cash equivalents was US dollar 21% (2019: 2%), sterling 76% (2019: 59%) and other 3% (2019: 39%).

Cash and cash equivalents have fair values that approximate 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	2020	2019
Cash and cash equivalents	**541**	18
Bank overdrafts	**–**	–
	541	18

Notes to the company financial statements

5. Financial liabilities – borrowings

All figures in £ millions	2020	2019
Non-current		
Revolving credit facility	–	230
	–	230
Total borrowings	–	230

Current borrowings are classified within cash and cash equivalents and do not give rise to financing cash flows. The carrying amounts of the company's borrowings is equal to, or approximately equal to, the market value.

6. Derivative financial instruments

The company's outstanding derivative financial instruments are as follows:

			2020			2019
All figures in £ millions	Gross notional amounts	Assets	Liabilities	Gross notional amounts	Assets	Liabilities
Interest rate derivatives	**904**	**12**	**(27)**	893	15	(6)
Cross-currency rate derivatives	**516**	**44**	**(20)**	502	29	(31)
FX derivatives	**554**	**7**	**(5)**	941	10	(2)
Total	**1,974**	**63**	**(52)**	2,336	54	(39)
Analysed as expiring:						
In less than one year	**1,238**	**18**	**(12)**	1,167	25	(15)
Later than one year and not later than five years	**663**	**45**	**(32)**	694	13	(6)
Later than five years	**73**	**–**	**(8)**	475	16	(18)
Total	**1,974**	**63**	**(52)**	2,336	54	(39)

The carrying value of the above derivative financial instruments equals their fair value. Derivatives are categorised as level 2 on the fair value hierarchy. 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	Share capital £m	Share premium £m
At 1 January 2019	781,078	195	2,607
Issue of ordinary shares – share option schemes	1,021	–	7
Purchase of own shares	–	–	–
At 31 December 2019	782,099	195	2,614
Issue of ordinary shares – share option schemes	**1,236**	**–**	**6**
Purchase of own shares	**(30,077)**	**(7)**	**–**
At 31 December 2020	**753,258**	**188**	**2,620**

The ordinary shares have a par value of 25p per share (2019: 25p per share). All issued shares are fully paid. All shares have the same rights.

A £350m share buyback programme was announced January 2020, the programme was later paused due to the impact of COVID-19. The original intention was to buyback approximately £350m of shares and at the date of pausing the programme approximately 30m shares had been bought back and cancelled at a cost of £176m. There are currently no plans to resume the share buyback programme. The shares bought back have been cancelled and the nominal value of these shares transferred to a capital redemption reserve. The nominal value of shares cancelled at 31 December 2020 was £18m (2019: £11m).

8. Treasury shares

	Number of shares 000s	£m
At 1 January 2019	3,225	(12)
Purchase of treasury shares	6,100	52
Release of treasury shares	(6,067)	(61)
At 31 December 2019	3,258	(21)
Purchase of treasury shares	**1,105**	**6**
Release of treasury shares	**(3,460)**	**(23)**
Transfer of contributions from subsidiaries	**–**	**45**
At 31 December 2020	**903**	**7**

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 £0.2m (2019: £0.8m). Dividends on treasury shares are waived.

At 31 December 2020, the market value of the company's treasury shares was £6m (2019: £21m). The gross book value of the shares at 31 December 2020 amounts to £7m. In 2020, historical contributions of £45m received from operating companies have been transferred from the treasury shares reserve to retained earnings.

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 (2019: £35,000).

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 £97m (2019: £104m) and interest and guarantee fees receivable from subsidiaries for the year of £46m (2019: £91m). Management fees payable to subsidiaries in respect of centrally provided services amounted to £21m (2019: £45m). Management fees receivable from subsidiaries in respect of centrally provided services amounted to £31m (2019: £35m). Dividends received from subsidiaries were £nil (2019: £803m).

Associates

In 2019, amounts due from related parties, disclosed on the face of the company balance sheet, relate to loans to Penguin Random House, a previous associate of the Group. The amounts outstanding were repaid at the point of disposal of Penguin Random House in April 2020.

Key management personnel

Key management personnel are deemed to be the members of the Pearson Executive Management team.

It is this Committee which had responsibility for planning, directing and controlling the activities of the company in 2020. Key management personnel compensation is disclosed in note 36 to the consolidated financial statements.

Notes to the company financial statements

12. Group companies

In accordance with section 409 of the Companies Act 2006 a full list of subsidiaries, partnerships, associates, joint ventures and joint arrangements, the country of incorporation, the registered address and the effective percentage of equity owned, as at 31 December 2020, is disclosed below. Unless otherwise stated, the shares are all indirectly held by Pearson plc. Unless otherwise stated, all wholly-owned and partly-owned subsidiaries are included in the consolidation and all associated undertakings are included in the Group's financial statements using the equity method of accounting. Principal Group companies are identified in **bold**.

Wholly-owned subsidiaries

Registered company name	Country of Incorp.	Reg office
Addison Wesley Longman, Inc.	US	3
Addison-Wesley Educational Publishers Inc.	US	4
AEL (S) PTE Limited	SG	5
Aldwych Finance Limited	UK	1
ATI Professional Development LLC	US	4
Atkey Finance Limited	IE	7
Axis Finance Inc.	US	4
Camsaw, Inc.	US	4
CAMSAWUSA, Inc.	US	29
Centro Cultural Americano Franquias e Comércio Ltda.	BR	15
Century Consultants Ltd.	US	13
Certiport China Holding, LLC	US	4
Certiport, Inc.	US	4
Cogmed Systems AB	SE	14
Connections Academy of Florida, LLC	US	20
Connections Academy of Iowa, LLC	US	24
Connections Academy of Maine, LLC	US	28
Connections Academy of Maryland, LLC	US	29
Connections Academy of Nevada, LLC	US	31
Connections Academy of New Mexico, LLC	US	32
Connections Academy of Oregon, LLC	US	37
Connections Academy of Pennsylvania LLC	US	38
Connections Academy of Tennessee, LLC	US	40
Connections Academy of Texas LLC	US	41
Connections Education LLC	US	4
Connections Education of Florida, LLC	US	20
Connections Education, Inc.	US	4
CTI Education Group (Pty) Limited	ZA	47
Dominie Press, Inc.	US	17
Dorian Finance Limited	IE	7
Dorling Kindersley Australasia Pty Limited	AU	48
EBNT Canada Holdings ULC	CA	58
EBNT Holdings Limited	CA	57
EBNT USA Holdings Inc.	US	4
eCollege.com	US	4
Edexcel Limited†	UK	49
Éditions Du Renouveau Pédagogique Inc.	CA	50
Education Development International Plc†	UK	1
Education Resources (Cyprus) Limited	CY	51
Educational Management Group, Inc.	US	52
Embanet ULC	CA	44
Embanet-Compass Knowledge Group Inc.	US	20
English Language Learning and Instruction System, Inc.	US	54
Escape Studios Limited*	UK	6
Falstaff Holdco Inc.	US	4
Falstaff Inc.	US	55
FBH, Inc.	US	4
George (Shanghai) Commercial Information Consulting Co., Ltd	CN	21
Global George II limited*	HK	53
Globe Fearon Inc.	US	17
Guangzhou Crescent Software Co., Ltd*	CN	61

Registered company name	Country of Incorp.	Reg office
Heinemann Education Botswana (Publishers) (Proprietary) Limited	BW	8
IndiaCan Education Private Limited	IN	2
Integral 7, Inc.	US	4
INTELLIPRO, INC.	US	13
Kagiso Education Pty Ltd	ZA	47
Knowledge Analysis Technologies, LLC	US	18
LCCIEB Training Consultancy., Ltd	CN	64
LessonLab, Inc.	US	17
Lignum Oil Company	US	4
LION SG PTE. LTD	SG	5
Longman (Malawi) Limited	MW	65
Longman Australasia Pty Ltd	AU	48
Longman Group(Overseas Holdings) Limited	UK	1
Longman Indochina Acquisition, L.L.C.	US	4
Longman Kenya Limited	KE	66
Longman Mocambique Ltda	MZ	42
Longman Swaziland (Pty) Limited	SZ	67
Longman Tanzania Limited*	TZ	68
Longman Zambia Educational Publishers Pty Ltd	ZM	69
Longman Zambia Limited	ZM	69
Longman Zimbabwe (Private) Ltd	ZW	70
Longmaned Ecuador S.A.	EC	71
Lumerit Education, LLC	US	41
Major123 Limited	UK	1
MeasureUp of Delaware, LLC	US	4
Modern Curriculum Inc.	US	17
Multi Treinamento e Editora Ltda	BR	15
National Computer Systems Japan Co. Ltd	JP	74
NCS Information Services Technology (Beijing) Co Ltd	CN	75
NCS Pearson Pty Ltd	AU	48
NCS Pearson Puerto Rico, Inc.	PR	76
NCS Pearson, Inc.	US	30
Ordinate Corporation	US	17
Pearson (Beijing) Management Consulting Co., Ltd.	CN	77
Pearson (Guizhou) Education Technology Co., Ltd.*	CN	78
Pearson America LLC	US	4
Pearson Amsterdam B.V.	NL	79
Pearson Australia Finance Unlimited	UK	1
Pearson Australia Group Pty Ltd	AU	48
Pearson Australia Holdings Pty Ltd	AU	48
Pearson Australia Pty Ltd	AU	48
Pearson Benelux B.V.	NL	79
Pearson Books Limited†	UK	1
Pearson Brazil Finance Limited	UK	1
Pearson Business Services Inc.	US	4
Pearson Canada Assessment Inc	CA	80
Pearson Canada Finance Unlimited	UK	1
Pearson Canada Holdings Inc	CA	80
Pearson Canada Inc.	CA	80

Registered company name	Country of Incorp.	Reg office
Pearson Central Europe Spółka z ograniczoną odpowiedzialnością	PL	41
Pearson College Limited	UK	1
Pearson DBC Holdings Inc.	US	4
Pearson Desarrollo y Capacitación Profesional Chile Limitada	CL	81
Pearson Deutschland GmbH	DE	82
Pearson Digital Learning Puerto Rico, Inc.	PR	76
Pearson Dollar Finance plc†	UK	1
Pearson Dollar Finance Two Limited	UK	1
Pearson Educacion de Chile Limitada	CL	81
Pearson Educacion de Colombia S A S	CO	84
Pearson Educacion de Mexico, S.A. de C.V.	MX	85
Pearson Educacion de Panama SA	PA	86
Pearson Educacion de Peru S.A.	PE	87
Pearson Educacion SA	ES	88
Pearson Education (Singapore) Pte Ltd*	SG	5
Pearson Education Africa (Pty) Ltd	ZA	47
Pearson Education Asia Limited	HK	53
Pearson Education Botswana (Proprietary) Limited	BW	8
Pearson Education do Brasil Ltda	BR	60
Pearson Education Hellas SA	GR	26
Pearson Education Holdings Limited†	UK	1
Pearson Education Indochina Limited	TH	89
Pearson Education Investments Limited	UK	1
Pearson Education Korea Limited	KR	90
Pearson Education Limited	UK	1
Pearson Education Namibia (Pty) Limited	NA	91
Pearson Education Publishing Limited	NG	92
Pearson Education S.A.	UY	93
Pearson Education SA	AR	94
Pearson Education South Africa (Pty) Ltd	ZA	47
Pearson Education South Asia Pte. Ltd.	SG	5

12. Group companies continued

Wholly-owned subsidiaries continued

Registered company name	Country of Incorp.	Reg office
Pearson Education Taiwan Ltd	TW	96
Pearson Education, Inc.	US	4
Pearson Educational Measurement Canada, Inc.	CA	36
Pearson Educational Publishers, LLC	US	4
Pearson Egitim Cozumleri Tikaret Limited Sirketi	TR	100
Pearson Falstaff (Holdings) Inc.	US	4
Pearson Falstaff Holdco LLC	US	4
Pearson France	FR	97
Pearson Funding Four Limited†	UK	1
Pearson Funding plc†	UK	1
Pearson Holdings Inc.	US	4
Pearson Holdings Southern Africa (Pty) Limited	ZA	47
Pearson Hungary LLC	HU	25
Pearson India Education Services Private Limited	IN	2
Pearson India Support Services Private Limited*	IN	16
Pearson Institute of Higher Education	ZA	47
Pearson International Finance Limited†	UK	1
Pearson Investment Holdings, Inc.	US	4
Pearson IOKI Spółka z ograniczoną odpowiedzialnością	PL	98
Pearson Italia S.p.A	IT	99
Pearson Japan KK	JP	101
Pearson Lanka (Private) Limited	LK	63
Pearson Lanka Support Services (Private) Limited	LK	12
Pearson Lesotho (Pty) Ltd	LS	62
Pearson Loan Finance No. 3 Limited	UK	1
Pearson Loan Finance No. 4 Limited	UK	1
Pearson Loan Finance No.5 Limited	UK	1
Pearson Loan Finance No. 6 Limited	UK	1
Pearson Loan Finance Unlimited	UK	1
Pearson Longman Uganda Limited	UG	43
Pearson Malaysia Sdn. Bhd.	MY	59
Pearson Management Services Limited†	UK	1
Pearson Management Services Philippines Inc.	PH	33
Pearson Maryland Inc.	US	11
Pearson Netherlands B.V.	NL	79
Pearson Netherlands Holdings B.V.	NL	79
Pearson Nominees Limited†	UK	1
Pearson Online Tutoring LLC	US	4
Pearson Overseas Holdings Limited†	UK	1
Pearson PEM P.R., Inc.	PR	19
Pearson Pension Nominees Limited	UK	1
Pearson Pension Property Fund Limited	UK	1
Pearson Pension Trustee Services Limited†	UK	1
Pearson Phoenix Pty Ltd	AU	48
Pearson Professional Assessments Limited	UK	1
Pearson Real Estate Holdings Inc.	US	4
Pearson Real Estate Holdings Limited†	UK	1
Pearson Schweiz AG	CH	34
Pearson Services Limited†	UK	1
Pearson Shared Services Limited†	UK	1
Pearson Strand Finance Limited†	UK	1
Pearson Strand Limited	UK	1

Registered company name	Country of Incorp.	Reg office
Pearson Sweden AB	SE	14
Pearson VUE Philippines, Inc.	PH	27
Penguin Capital, LLC	US	4
Phumelela Publishers (Pty) Ltd*	ZA	47
PN Holdings Inc.	US	4
ProctorCam, Inc.	US	4
PT Efficient English Services	ID	83
PVNT Limited	UK	1
Reading Property Holdings LLC	US	73
Rebus Planning Associates, Inc.	US	10
Reston Publishing Company, Inc.	US	4
Rycade Capital Corporation	US	4
Shanghai AWL Education Software Ltd*	CN	72
Silver Burdett Ginn Inc.	US	4
Skylight Training and Publishing Inc.	US	52
Smarthinking, Inc.	US	4
Sound Holdings Inc.	US	4
Sparrow Phoenix Pty Ltd	AU	23
Spear Insurance Company Limited†	BM	45
Stark Verlag GmbH	DE	82
The Financial Times (I) Pvt Ltd	IN	22
The Learning Edge International pty Ltd	AU	48
The Waite Group Inc	US	17
TQ Catalis Limited	UK	1
TQ Clapham Limited	UK	1
TQ Education and Training Limited	UK	1
TQ Education and Training Limited	SA	56
TQ Global Limited	UK	1
TQ Group Limited	UK	1
TQ Holdings Limited	UK	1
Trio Parent Holdings LLC	US	4
Vue Testing Services Israel Ltd	IL	46
Vue Testing Services Korea Limited	KR	35
Williams Education GmbH	DE	82

* In liquidation.
† Directly owned by Pearson plc.

Subsidiary addresses

The following list includes all Pearson registered offices worldwide. See wholly-owned subsidiaries list opposite for each subsidiary's registered office code.

	Registered office address
1	80 Strand, London, WC2R 0RL, England
2	The HIVE, 3rd Floor, No 44, Pilliayar Koil Street, Jawaharlal Nehru Road, Anna Nagar, Chennai, TN 600040, India
3	C T Corporation System, 155 Federal St., Suite 700, Boston, MA, 02110, United States
4	The Corporation Trust Company, Corporation Trust Center, 1209 Orange Street, Wilmington, New Castle, DE, 19801, United States
5	9, #13-05/06, North Buona Vista Drive, The Metropolis Tower One, 138588, Singapore
6	Evergreen House North, Grafton Place, London, NW1 32DX England
7	1st Floor The Liffey Trust Centre, 117-126 Sheriff Street Upper, Dublin 1, Ireland
8	Plot 50371, Fairground Office Park, Gaborone, Botswana
9	3F, Building R2 China Merchants Tower, No.118 Jianguo Road, Chaoyang District, Beijing, China
10	The Corporation Company, 40600 Ann Arbor Rd E Suite 201, Plymouth, MI, 48170, United States
11	The Corporation Trust Company, 2405 York Road, Suite 201, Lutherville Timonium, MD, 21093-2264, United States
12	#1, 3, 5th Floor, East Tower, World Trade Centre, Echelon Square, Colombo, O1, Sri Lanka
13	820, Bear Tavern Road, West Trenton, Mercer, NJ, 08628, United States
14	Gustavslundsvägen 137, 167 51 Bromma, Stockholm, Sweden
15	Comendador Aladino Selmi Avenue, 4630, Galpão 1, Sala 3, Parque Cidade Campinas, City of Campinas, São Paulo 13069-036, Brazil
16	7th Floor, SDB2, ODC 7, 8 & 9, Survey No.01 ELCOT IT/ ITES-SEZ, Shollinganallur, Chennai, TN, TN 600119, India
17	C T Corporation System, 818 West Seventh Street, Suite 930, Los Angeles, CA, 90017, United States
18	The Corporation Company, 7700 E Arapahoe Rd Suite 220, Centennial, CO, 80112-1268, United States
19	500, 401, Calle de la Tanca Edificio Ochoa, San Juan, 00901-1969, Puerto Rico
20	1200, South Pine Island Road, Plantation, FL, 33324, United States
21	Suite A7b, 3/F, No. 586 Longchang Road, Yangpu District, Shanghai, China
22	N-94, S-2 Outer Ring Road Panchsheel Park, Panchsheel Club, New Delhi, South Delhi, DL 110017, India
23	Suite 201, 25 Cooper Street, Surry Hills, NSW, 2010, Australia
24	C T Corporation System, 400 E Court Ave, Des Moines, IA, 50309, United States
25	22 B, 13 em, Népfürdő utca, Budapest
26	4 Zalogou Str., 15343 Agia Paraskevi, Athens, Greece
27	27/F Trident Tower, 312 Sen. Gil Puyat Avenue, Makati City, Metro Manila, Philippines
28	C T Corporation System, 128 State St #3, Augusta, ME, 04330, United States
29	7 St. Paul Street, Suite 1660, Baltimore, MD, 21202, United States
30	C T Corporation System Inc., 1010 Dale Street North, St Paul, MN, 55117-5603, United States
31	The Corporation Trust Company of Nevada, 701 S Carson St, Suite 200, Carson City, NV, 89701, United States

Notes to the company financial statements

12. Group companies continued

Subsidiary addresses continued

	Registered office address
32	C T Corporation System, 206 S Coronado Ave, Espanola, NM, 87532-2792, United States
33	7/F North Tower, Rockwell Business Center COR. Sheridan & United Street, Brgy. Highway Hills, Mandaluyong, Philippines
34	10 Gewerbestrasse, Cham, 6330, Switzerland
35	21, Mugyo-ro Jung-gu, Seoul, Republic of Korea
36	199 Bay Street, Commerce Court West, Suite 2800, Toronto, ON, M5L1A9, Canada
37	C T Corporation System, 780 Commercial Street SE, STE 100, Salem, OR, OR 97301, United States
38	C T Corporation System, 600 N. 2nd Street, Suite 401, Harrisburg, PA, 17101-1071, United States
39	Ulica Szamocka 8 01-748, Warszawa, Poland
40	C T Corporation System, 300 Montvue Rd, Knoxville, TN, 37919-5546, United States
41	CT Corporation System, 1999 Bryan Street, Suite 900, Dallas, TX, 75201, United States
42	Numero 776, Avenida 24 de Julho, Maputo, Mozambique
43	Plot 8, Berkley Road, Old Kampala, Uganda
44	3500, 855 – 2nd Street, S.W., Calgary, AB, T2P 4K7, Canada
45	Power House, 7 Par-la-ville Road, PO Box 1826, Hamilton, HM 11, Bermuda
46	Derech Ben Gurion 2, BSR Building 9th Floor, Ramat Gan, 52573, Israel
47	Auto Atlantic, 4th Floor, Corner Hertzog Boulevard and Heerengracht, Cape Town, 8001, South Africa
48	707 Collins Street, Docklands, Melbourne, VIC, 3008, Australia
49	190, High Holborn, London, WC1V 7BH, England
50	1611, Boul. Cremazie Est, 10th Floor, Montréal, PQ, H2M 2P2, Canada
51	195, Archbishop Makarios III Avenue, Neocleous House, Limassol, 3030, Cyprus
52	Illinois Corporation Service Company, 700 S 2nd Street, Springfield, IL, 62703, United States
53	28/F, 1063 King's Road, Quarry Bay, Hong Kong
54	251, Little Falls Drive, Wilmington, DE, 19808, United States
55	28 Liberty Street, New York, NY, 10005, United States
56	King Fahad Road, Olaya, Riyadh, 58774, 11515, Saudi Arabia

	Registered office address
57	44 Chipman Hill, Suite 1000, Saint Jon, NB, E2L 4S6, Canada
58	Suite 2600, Three Bentall Centre, P.O. Box 49314, 595 Burrard Street, Vancouver, BC, V7X 1L3, Canada
59	Unit 30-01, Level 30, Tower A, Vertical Business Suite, Avenue 3, Bangsar South, No 8, Jalan Kerinchi, 59200 Kuala Lumpur, Malaysia
60	Comendador Aladino Selmi Avenue, 4630, Galpão 1, Mezanino, Sala 5, Parque Cidade Campinas, City of Campinas,São Paulo, 13069-036, Brazil
61	Suite 1201 (site: self-made No. 1219), No. 85 Huacheng Avenue, Tianhe District, Guangzhou, China
62	C/o Du Preez, Llebetrau & Co, 252 Kingsway, Next to USA Embassy, Maseru, Lesotho
63	MAGA ONE-Level 22, No. 200, Nawala Road, Narahenpita, Colombo 05, 11222, Sri Lanka
64	Room 305, Building 2, 6555 Shangchuan Road, Pudong District, Shanghai, China
65	Parkway House, Hannover Avenue, Blantyre, Malawi
66	Queensway House, Kaunda Street, Nairobi, Kenya
67	Robinson Bertram, 3rd Floor, Sokhzmlilio Bldg, Mbabane, Swaziland
68	P O Box 45, IPS Building, Maktaba Street, Dar es Salaam, Tanzania
69	Mlungushi Conference Centre, Centre Annex, Great East Road, Lusaka, Zambia
70	Stand 1515, Cnr Tourle Road/Harare Drive, Ardbennie, Harare, Zimbabwe
71	Andalucía y cordero E12-35. Edificio CYEDE piso 1, Oficina 11, Sector "La Floresta", Quito, Pichincha, Ecuador
72	Suite 302-9,Block 3, No. 333 Weining Road, Changning District, Shanghai, China
73	C/O Pearson Education, 501 Boylston St, Boston, MA, 02116, United States
74	Teikoku Hotel Tower 18F, 1-1-1 Uchi Saiwai-Cho, Chiyoda-ku, Tokyo, Japan
75	Suite 1201, Tower 2, No. 36 North Third Ring East Road, Dongcheng District, Beijing, China
76	268 Munoz Rivera Avenue, Suite 1400, San Juan, 00918, Puerto Rico
77	Suite 1208, 12/F, Tower 2, No. 36 North Third Ring East Road, Dongcheng District, Beijing, China
78	Suites 3-28 (2:3), Shi Guang Jun Yuan, No. 89 Hubin Road, Goden Sun Technology Industrial Park, High Technical & Industrial Development District, Guiyang City, Guizhou Province, China

	Registered office address
79	Kabelweg 37, Amsterdam, 1014 BA, Netherlands
80	26 Prince Andrew Place, Don Mills, Toronto, ON, M3C 2T8, Canada
81	Oficina N°117, edificio Casa Colorada, calle Merced N°838-A Santiago Centro, Santiago, Chile
82	c/o Pearson Deutschland GmbH, St.-Martin-Str. 82, Munich, 81541, Germany
83	30th Floor, Ratu Plaza Office Tower, Jl. Jend. Sudirman Kav 9, Jakarta, 10270, Indonesia
84	Carrera 7 Nro 156 – 68, Piso 26, Bogota, Colombia
85	Calle Antonio Dovali jaime #70, Torre B, Piso 6, Col. Zedec ed Plaza Santa Fe, del. Álvaro Obregon, Ciudad de Mexico, CP 01210, Mexico
86	Punta Pacifica, Torres de las Americas, Torre A Piso 15 Ofic. 1517, Panama, 0832-0588, Panama
87	Cal. Los Halcones, no. 275, Urb. Limatombo, Lima, Perú
88	16, Ribera del Loira, Madrid, 28042, Spain
89	87/1 Capital Tower Building, All Seasons Place unit 1604 – 6 16th floor, Wireless Road, Lumpini, Pathumwan, Bangkok, Thailand
90	6F Kwanjeong Building, 35, Cheonggyecheon-Ro, Jongno-gu, Seoul, 03188, Republic of Korea
91	Unit 7 Kingland Park, 98 Nickel Street, Prosperita, Windhoek, Namibia
92	8, Secretariat Road, Obafemi Awolowo Way, Alausa, Ikeja, Lagos State, Nigeria
93	Juan Benito Blanco 780 – Plaza Business Center Montevideo, Uruguay
94	498, Libertador Ave, City of Buenos Aires. 3rd floor, Buenos Aires, Argentina
95	No 219, Room D, 11F, Sec 3, Beixin Road, New Taipei City, Xindian District, 23143, Taiwan
96	11F, No 209, Sec. 1, Civic Blvd., Datong District, Taipei City, 10351, Taiwan (Province of China)
97	3-15, Immeuble Terra Nova II, Rue Henri Rol Tanguy, Montreuil, 93100, France
98	Ulica Jana Henryka Dąbrowskiego 77A 60-529, Poznań, Poland
99	16, Corso Trapani, Turin, 10100, Italy
100	Nida Kule Kozyatagi, Kozyatagi Mahallesi, Degirmen Sokak No:18 Kat:6 D:15, Kadikoy, Istanbul, 34742, Turkey
101	1-5-15 Kanda-Sarugakucho, Chiyoda-ku, Tokyo, Japan

12. Group companies continued

Partly-owned subsidiaries

Registered company Name	Country of Incorp.	% Owned	Reg office
Certiport China Co Ltd	CN	50.69	1
Educational Publishers LLP	UK	85	2
GED Domains LLC	US	70	3
GED Testing Service LLC	US	70	4
Heinemann Publishers (Pty) Ltd	ZA	75	5
LRTE Voxy, LLC	US	50	4
LRTE Voxy, L.P	US	83.3	4
Maskew Miller Longman (Pty) Limited	ZA	75	5
Pearson Education Achievement Solutions (RF) (Pty) Limited	ZA	97.3	5
Pearson Pension Trustee Limited	UK	50	2
Pearson South Africa (Pty) Ltd	ZA	75	5

Associated undertakings

Registered company Name	Country of Incorp.	% Owned	Reg office
Avanti Learning Centres Private Limited‡	IN	23.47	6
Karadi Path learning Company Private Limited‡	IN	24.96	8
Learn Capital Special Opportunities Fund I, L.P.‡	US	99.59	11
Learn Capital Venture Partners II, L.P.‡	US	72.93	11
Learn Capital Venture Partners IIIA, L.P.‡	KY	99.00	7
Learn Capital Venture Partners, L.P.‡	US	99.15	11
Peking University Pearson (Beijing) Cultural Development Co., Ltd	CN	45	9
Tenyi Education Company Limited*	CN	49	12
The Egyptian International Publishing Company-Longman	EG	49	10

* In liquidation.
‡ Accounted for as an 'Other financial asset' within non-current assets.

Partly-owned subsidiaries and associated undertakings company addresses

	Registered office address
1	Suite 1804, No.99 Huichuan Road, Changning District, Shanghai City, China
2	80 Strand, London, WC2R 0RL, England
3	C T Corporation System, 4701 Cox Road, Suite 285, Glen Allen, Henrico, VA, 23060-0000, United States
4	The Corporation Trust Company, Corporation Trust Center, 1209 Orange Street, Wilmington, New Castle, DE, 19801, United States
5	Auto Atlantic, 4th Floor, Corner Hertzog Boulevard and Heerengracht, Cape Town, 8001, South Africa
6	16 Paschimi Marg, Vasant Vihar, New Delhi, DL, India
7	Campbells Corporate Services Limited, Floor 4, Willow House, Cricket Square, Grand Cayman, KY1-9010, Cayman Islands
8	3A Dev Regency II, First Main Road, Gandhinagar, Adyar, Chennai, TN, India
9	Suite 216, No. 127-1 Zhongguancun North Street, Haidian District, Beijing, China
10	10a Hussein Wassef St, Midan Missaha, Dokki Giza, 12311, Egypt
11	Incorporating Services, Ltd. 3500 S Dupont Way, Dover, Kent, DE, United States
12	28/F, 1063 King's Road, Quarry Bay, Hong Kong

Five-year summary

All figures in £ millions	2016	2017	2018	2019	2020
Sales: By operating segment					
Global Online Learning			521	586	**697**
Global Assessment			955	1,031	**892**
North American Courseware			1,461	1,091	**894**
International			1,192	1,161	**914**
Continuing	4,552	4,513	4,129	3,869	**3,397**
Discontinued	–	–	–	–	**–**
Total sales	4,552	4,513	4,129	3,869	**3,397**
Adjusted operating profit: By operating segment					
Global Online Learning			99	84	**99**
Global Assessment			304	351	**245**
North American Courseware			297	231	**190**
International			305	299	**182**
Enabling Functions			(527)	(449)	**(404)**
Penguin Random House			68	65	**1**
Continuing	635	576	546	581	**313**
Discontinued	–	–	–	–	**–**
Total adjusted operating profit	635	576	546	581	**313**

All figures in £ millions	2016	2017	2018	2019	2020
Operating margin – continuing	13.9%	12.8%	13.2%	15.0%	**9.2%**
Adjusted earnings					
Total adjusted operating profit	635	576	546	581	**313**
Net finance costs	(59)	(79)	(24)	(41)	**(61)**
Income tax	(95)	(55)	27	(89)	**(35)**
Non-controlling interest	(2)	(2)	(2)	(2)	**–**
Adjusted earnings	479	440	547	449	**217**
Weighted average number of shares (millions)	814.8	813.4	778.1	777.0	**755.4**
Adjusted earnings per share	58.8p	54.1p	70.3p	57.8p	**28.7p**

Prior periods have not been restated to reflect the adoption of IFRS 15 and IFRS 9 in 2018 and IFRS 16 in 2019.

Periods prior to 2018 have not been restated to reflect the new organisation structure as there is no appropriate basis for restatement of those periods.

All figures in £ millions	2016	2017	2018	2019	2020
Cash flow					
Operating cash flow	663	669	513	418	**315**
Operating cash conversion	104%	116%	94%	72%	**101%**
Operating free cash flow	549	525	448	345	**255**
Operating free cash flow per share	67.4p	64.5p	57.6p	44.4p	**33.8p**
Free cash flow	310	227	473	213	**229**
Free cash flow per share	38.0p	27.9p	60.8p	27.4p	**30.3p**
Net assets	4,348	4,021	4,525	4,323	**4,134**
Net debt	1,092	432	143	1,016	**463**
Return on invested capital					
Total adjusted operating profit	635	576	546	581	**313**
Operating tax paid	(63)	(75)	(43)	(9)	**(10)**
Return	572	501	503	572	**303**
Gross basis:					
Average invested capital	11,464	11,568	10,672	11,096	**10,625**
Return on invested capital	5.0%	4.3%	4.7%	5.2%	**2.9%**
Net basis:					
Average invested capital	7,906	8,126	7,544	8,097	**7,708**
Return on invested capital	7.2%	6.2%	6.7%	7.1%	**3.9%**
Dividend per share	52.0p	17.0p	18.5p	19.5p	**19.5p**

Financial key performance indicators

The following tables and narrative provide further analysis of the financial key performance indicators which are described in the financial review of the annual report on pages 29-34, shown within the key performance indicators on page 2 of the annual report and shown in notes 2 and 8 of the notes to the consolidated financial statements.

Adjusted performance measures

The annual report and accounts reports results and performance on a headline basis which compares the reported results both on a statutory and on a non-GAAP (non-statutory) basis. The Group's adjusted performance measures are non-GAAP (non-statutory) financial measures and are also included in the annual report as they are key financial measures used by management to evaluate performance and allocate resources to business segments. The measures also enable investors to more easily, and consistently, track the underlying operational performance of the Group and its business segments by separating out those items of income and expenditure relating to acquisition and disposal transactions, major restructuring programmes and certain other items that are also not representative of underlying performance.

The Group's definition of adjusted performance measures may not be comparable to other similarly titled measures reported by other companies. A reconciliation of the adjusted measures to their corresponding statutory measures is shown below.

Sales

Underlying sales movements exclude the effect of exchange, the impact of portfolio changes arising from acquisitions and disposals and the impact of adopting new accounting standards that are not retrospectively applied. Portfolio changes are calculated by taking account of the additional sales (at constant exchange rates) from acquisitions made in both the current year and the prior year. For acquisitions made in the prior year the additional sales excluded is calculated as the sales made in the period of the current year that corresponds to the pre-acquisition period in the prior year. Sales made by businesses disposed in either the current year or the prior year are also excluded. Constant exchange rates are calculated by assuming the average exchange rates in the prior year prevailed throughout the current year. These non-GAAP measures enable management and investors to track more easily, and consistently, the underlying sales performance of the Group.

All figures in £ millions	Global Online Learning	Global Assessment	North American Courseware	International	Total
Statutory sales 2020	697	892	894	914	**3,397**
Statutory sales 2019	586	1,031	1,091	1,161	**3,869**
Statutory sales (decrease)/increase	111	(139)	(197)	(247)	**(472)**
Comprising:					
Underlying (decrease)/increase	106	(141)	(133)	(218)	**(386)**
Portfolio changes	4	–	(65)	6	**(55)**
Exchange differences	1	2	1	(35)	**(31)**
Statutory sales (decrease)/increase	111	(139)	(197)	(247)	**(472)**
Statutory (decrease)/increase	19%	(13)%	(18)%	(21)%	**(12)%**
Constant exchange rate (decrease)/increase	19%	(14)%	(18)%	(18)%	**(11)%**
Underlying (decrease)/increase	18%	(14)%	(13)%	(19)%	**(10)%**

Adjusted operating profit

Adjusted operating profit excludes the cost of major restructuring; other net gains and losses on the sale of subsidiaries, joint ventures, associates and other financial assets; and intangible charges, including impairment, relating only to goodwill and intangible assets acquired through business combinations and the direct costs of acquiring those businesses. Further details are given below under 'Adjusted earnings per share'. Underlying adjusted operating profit movements exclude the effect of exchange, the impact of portfolio changes arising from acquisitions and disposals and the impact of adopting new accounting standards that are not retrospectively applied. Portfolio changes are calculated by taking account of the additional contribution (at constant exchange rates) from acquisitions made in both the current year and the prior year.

For acquisitions made in the prior year the additional contribution excluded is calculated as the operating profit made in the period of the current year that corresponds to the pre-acquisition period in the prior year. Operating profit made by businesses disposed in either the current year or the prior year is also excluded. Constant exchange rates are calculated by assuming the average exchange rates in the prior year prevailed throughout the current year. This non-GAAP measure enables management and investors to track more easily, and consistently, the underlying operating profit performance of the Group.

All figures in £ millions	2020	2019
Operating profit	**411**	275
Cost of major restructuring	**–**	159
Other net gains and losses	**(178)**	(16)
Intangible charges	**80**	163
Adjusted operating profit	**313**	581

All figures in £ millions	Global Online Learning	Global Assessment	North American Courseware	International	Enabling Functions	Penguin Random House	Total
Adjusted operating profit (decrease)/increase	15	(106)	(41)	(117)	45	(64)	**(268)**
Comprising:							
Underlying (decrease)/increase	19	(107)	(48)	(116)	42	–	**(210)**
Portfolio changes	(3)	–	6	2	–	(64)	**(59)**
Exchange differences	(1)	1	1	(3)	3	–	**1**
Adjusted operating profit (decrease)/increase	15	(106)	(41)	(117)	45	(64)	**(268)**
Constant exchange rate (decrease)/increase	19%	(30)%	(18)%	(38)%	9%	–	**(46)%**
Underlying (decrease)/increase	23%	(30)%	(20)%	(39)%	9%	–	**(40)%**

Adjusted earnings per share

Adjusted earnings includes adjusted operating profit and adjusted finance and tax charges. Adjusted earnings is included as a non-GAAP measure as it is used by management to evaluate performance and allocate resources to business segments and by investors to more easily, and consistently, track the underlying operational performance of the Group over time. Adjusted earnings per share is calculated as adjusted earnings divided by the weighted average number of shares in issue on an undiluted basis.

The following items are excluded from adjusted earnings:

Cost of major restructuring – In May 2017, the Group announced a restructuring programme to run between 2017 and 2019 to drive significant cost savings. The costs of this restructuring programme are significant enough to exclude from the adjusted operating profit measure so as to better highlight the underlying performance (see note 4).

Other net gains and losses – These represent profits and losses on the sale of subsidiaries, joint ventures, associates and other financial assets and are excluded from adjusted earnings as they distort the performance of the Group as reported on a statutory basis.

Intangible charges – These represent charges in respect of intangible assets acquired through business combinations and the direct costs of acquiring those businesses. These charges are excluded as they reflect past acquisition activity and do not necessarily reflect the current year performance of the Group.

Financial key performance indicators

Other net finance income/costs – These include finance costs in respect of retirement benefits, finance costs of deferred consideration and foreign exchange and other gains and losses. Finance income relating to retirement benefits are excluded as management does not believe that the consolidated income statement presentation under IAS 19 reflects the economic substance of the underlying assets and liabilities. Finance costs relating to acquisition transactions are excluded as these relate to future earn outs or acquisition expenses and are not part of the underlying financing. Foreign exchange and other gains and losses are excluded as they represent short-term fluctuations in market value and are subject to significant volatility. Other gains and losses may not be realised in due course as it is normally the intention to hold the related instruments to maturity.

Tax – Tax on the above items is excluded from adjusted earnings. Where relevant the Group also excludes the benefit from recognising previously unrecognised pre-acquisition and capital losses. The tax benefit from tax deductible goodwill and intangibles is added to the adjusted income tax charge as this benefit more accurately aligns the adjusted tax charge with the expected rate of cash tax payments.

All figures in £ millions	2020	2019
Profit for the year	**310**	266
Non-controlling interest	**–**	(2)
Cost of major restructuring	**–**	159
Other net gains and losses	**(178)**	(16)
Intangible charges	**80**	163
Other net finance income	**(4)**	2
Tax	**9**	(123)
Adjusted earnings	**217**	449
Weighted average number of shares (millions)	**755.4**	777.0
Adjusted earnings per share	**28.7p**	57.8p

Return on invested capital

Return on invested capital (ROIC) is included as a non-GAAP measure as it is used by management to help inform capital allocation decisions within the business. ROIC is calculated as adjusted operating profit less operating cash tax paid expressed as a percentage of average invested capital. Invested capital includes the original unamortised goodwill and intangibles. Average values for total invested capital are calculated as the average monthly balance for the year. ROIC is also presented on a net basis after removing impaired goodwill from the invested capital balance. The net approach assumes that goodwill which has been impaired is treated consistently to goodwill disposed as it is no longer being used to generate returns. The adoption of IFRS 16 has impacted adjusted operating profit and average tangible fixed assets in 2019, however, the overall impact on ROIC is not material.

All figures in £ millions	2020 Gross	2019 Gross	2020 Net	2019 Net
Adjusted operating profit	**313**	581	**313**	581
Operating tax paid	**(10)**	(9)	**(10)**	(9)
Return	**303**	572	**303**	572
Average goodwill	**6,199**	6,645	**3,282**	3,646
Average other non-current intangibles	**2,186**	2,394	**2,186**	2,394
Average intangible assets – pre-publication	**906**	889	**906**	889
Average tangible fixed assets and working capital	**1,334**	1,168	**1,334**	1,168
Average invested capital	**10,625**	11,096	**7,708**	8,097
Return on invested capital	**2.9%**	5.2%	**3.9%**	7.1%

Return on capital

Return on capital (ROC) is included as a non-GAAP measure of how efficiently we are generating returns from our asset base. ROC is calculated as adjusted operating profit less adjusted income tax as a proportion of capital, where capital adjusts net statutory assets for net debt, retirement benefit assets, other post-retirement medical obligations and other non-operating items. These adjustments to net statutory assets have been made to better reflect the asset base that generates returns.

All figures in £ millions	2020	2019
Adjusted operating profit	**313**	581
Adjusted income tax charge	**(35)**	(89)
Return	**278**	492
Net statutory assets	**4,134**	4,323
Adjustments for:		
Net debt	**463**	1,016
Retirement benefit assets	**(410)**	(429)
Other post-retirement medical benefit obligation	**39**	43
Other non-operating assets	**(30)**	(150)
Capital	**4,196**	4,803
Return on capital	**6.6%**	10.2%

Operating cash flow

Operating cash flow is calculated as net cash generated from operations before the impact of items excluded from the adjusted income statement plus dividends from joint ventures and associates (less the re-capitalisation dividends from Penguin Random House); less capital expenditure on property, plant and equipment (including additions to right of use assets) and intangible software assets; plus proceeds from the sale of property, plant and equipment (including the impacts of transfers to/from investment in finance lease receivable) and intangible software assets; plus special pension contributions paid; and plus cost of major restructuring paid. Operating cash flow is included as a non-GAAP measure in order to align the cash flows with the corresponding adjusted operating profit measures.

All figures in £ millions	2020	2019
Net cash generated from operations	**450**	480
Dividends from joint ventures and associates	**4**	64
Purchase of property, plant and equipment	**(53)**	(55)
Addition of new right-of-use lease assets	**(61)**	(64)
Purchase of intangible software assets	**(81)**	(138)
Proceeds from sale of property, plant and equipment and intangible assets	**–**	1
Net disposal of right-of-use lease assets including transfers to/from investment in finance lease receivable	**18**	17
Investment income	**–**	2
Net costs paid for major restructuring	**38**	111
Operating cash flow	**315**	418

Cash conversion, calculated as operating cash flow as a percentage of adjusted operating profit, is also shown as a non-GAAP measure as this is used by management and investors to measure cash generation by the Group.

All figures in £ millions	2020	2019
Adjusted operating profit	**313**	581
Operating cash flow	**315**	418
Cash conversion	**101%**	72%

Operating cash flow, operating free cash flow and total free cash flow, which are non-GAAP measures, are disclosed and reconciled in note 33 of the notes to the consolidated financial statements as they are commonly used by investors to measure the cash performance of the Group.

Financial key performance indicators

Net debt and adjusted earnings before interest, tax, depreciation and amortisation (EBITDA)

For information, the net debt/adjusted EBITDA ratio is shown as a non-GAAP measure as it is commonly used by investors to measure balance sheet strength. Adjusted EBITDA is calculated as adjusted operating profit less depreciation on property, plant and equipment, right-of-use assets and less amortisation on intangible software assets.

All figures in £ millions	2020	2019
Adjusted operating profit	**313**	581
Depreciation (excluding items included in 'cost of major restructuring')	**125**	122
Amortisation on intangible software assets (excluding items included in 'cost of major restructuring')	**112**	101
Adjusted EBITDA	**550**	804
Cash and cash equivalents	**1,116**	437
Investment in finance lease receivable	**130**	196
Derivative financial instruments	**11**	15
Bank loans and overdrafts	**(3)**	(3)
Revolving credit facility	**–**	(230)
Bonds	**(965)**	(593)
Lease liabilities	**(752)**	(838)
Net debt	**(463)**	(1,016)
Net debt/adjusted EBITDA ratio	**0.8x**	1.3x

Glossary of major products and services

Accelerated pathways: a corporate education benefit, where Pearson partners with companies to improve employee development by focusing on the educational needs of a specific business and its people, helping to strategically align educational assistance spending to the talent objectives of the organisation.

Artificial intelligence (AI): describes machines that can sense and interact with environments in a perception-planning-action cycle, or with other machines, without explicit programming. This is typically accomplished through Machine Learning (ML) which is the development, and application of algorithms that improve their performance (inference) at some task based on experience (training). Pearson takes a human-centric perspective of AI that considers the entire learning ecosystem when developing AI capabilities including ethics, privacy, appropriate uses and user needs.

BTEC: taught in colleges, schools and university throughout the world, a BTEC gives learners of all levels and ages the knowledge and skills they need for career success, now and into the future. The unique experience BTEC learners get of having to apply the knowledge and skills they've learned to real-life scenarios means more employers and learners are choosing BTEC.

- BTEC Level 1/Level 2 Firsts: BTEC Firsts allow level 2 learners to develop knowledge and understanding by applying their learning and skills in real-life scenarios. Combined with other qualifications, they enable learners to progress to further study, an apprenticeship, or into employment
- BTEC Level 1/Level 2 Tech Awards: studied alongside GCSE, BTEC Tech Awards provide a great introduction to a professional sector where students learn transferable skills they'll use if they progress to further study, and in their future career
- BTEC Level 2 Technicals: designed in collaboration with employers and industry professionals, BTEC Level 2 Technicals provide career-focused, applied courses for post-16 level 2 learners in a specialist occupational area. They support progression to an apprenticeship, to further technical study, or into the workplace
- BTEC Level 3 Nationals: allow level 3 learners to apply their learning in real-life scenarios to develop the specialist knowledge and skills they need to progress towards their chosen career path, whether that is through further or higher education, an apprenticeship or directly into the workplace
- BTEC Higher Nationals: available at levels 4 and 5, BTEC Higher Nationals are internationally recognised, career-focused higher education courses which are the same level as the first and second years of a degree course. Co-designed with employers and representing the most up-to-date professional standards, they support learners to develop the real-world knowledge, skills and behaviours needed to succeed, allowing them to move on to complete degree and progress in their chosen career path.

Clinical Assessment: our Clinical Assessment business provides assessments to help professionals improve lives by providing valuable information that can identify and manage an individual learner's strengths and weaknesses and learning barriers. The Clinical Assessment portfolio offers a range of assessments serving a diverse audience of professionals including Psychologists, Speech Language Pathologists, Occupational Therapists and more. These professionals rely on leading measures like the Wechsler Scales of Intelligence, which assess an individual's cognitive strengths and weaknesses or the Minnesota Multiphasic Personality Inventory (MMPI), a world-renowned measure of psychopathology and personality.

Other examples of our Clinical products include:

- Behavior Assessment System for Children-Third Edition (BASC-3): a comprehensive set of rating scales and forms to help children thrive in their school and home environments through effective behaviour assessment. BASC provides a complete picture of child and adolescent behaviour. School and clinical psychologists have depended on BASC for more than 20 years.
- Goldman-Fristoe Test of Articulation-Third Edition (GFTA-3): a systematic means of assessing an individual's ability to pronounce different speech sounds of Standard American English in order to diagnose different disorders which can inhibit an individual's articulation. It provides information about an individual's speech sound ability by sampling both spontaneous and imitative sound production in single words and connected speech.
- Q-interactive: a digital system for administering and scoring tests in a one-on-one setting between an examiner and examinee. Testing takes place on two iPads with an app called Assess. The simplicity of the system improves accuracy and speed in providing real-time scoring and allows for greater flexibility.

Connections Academy: The Connections Academy online school programme for grades K-12 is a comprehensive collection of online learning products and school support services for online public schools across the US, most of which carry the Connections Academy name. In addition, Pearson Online Academy is a private online school for grades K-12 and serves students worldwide.

Digitally–enabled learning: learning that is enabled through digital media, tools or technology.

GED: GED Testing Service is a joint venture between Pearson and the American Council on Education, and is part of a programme which measures proficiency in language arts, maths, science and social studies. It enables learners to obtain their high school equivalency credential, be placed in college courses, and even earn college credit. In addition to the actual GED test, GED also offers a suite of products and services delivered through Pearson VUE to help people prepare for their assessments, including GED Ready, a predictive practice test that provides learners with a detailed score report, which outlines areas of mastery and areas requiring more attention, giving learners the tools they need to be successful.

Inclusive Access: provides all US college students with equal and affordable access to course materials by their first day of class eliminating key hurdles to their academic success. Inclusive Access can also provide institutions a valuable tool to help increase retention by lowering the withdraw and fail rates caused by the lack of students preparedness. By utilising Inclusive Access institutions can drive down the overall cost of attendance for students by realising savings in using digital course materials rather than new print materials.

Lumerit Education: Acquired by Pearson in 2019, and integrated within Accelerated Pathways, Lumerit helps learners address the issues of college degree completion and affordability in the consumer and corporate markets. Lumerit uses data and analytics to match learner profiles to academic programmes.

MePro: a complete, blended service solution for English Language Learning, which provides a personalised learning experience through courseware and assessment linked to the Global Scale of English (GSE), remediation and stretch content for personalised learning, professional development for teachers and a parent app.

Glossary of major products and services

Online proctoring: Pearson's OnVUE online proctoring enables test takers to take certification exams securely from their home or office via a highly secure, online platform. The test involves a simple check-in process, with ID verification, face-matching technology and a live greeter. In 2020 Pearson saw a 10-fold increase in remote and online proctoring services as a result of the pandemic – that's 2.1m assessments.

Online Program Management (OPM): a market in which Pearson is a provider by partnering with colleges and universities around the world to bring their degrees and short courses online, helping students gain skills for the changing world of work. Pearson provides the upfront capital and infrastructure that institutions need, as well as providing services such as student enrolment and retention, course design and development, and market research and insights.

Pearson Advance: Pearson launched Pearson Advance offering learners an affordable, accessible catalogue of flexible, short, online courses from leading experts and universities. A partnership with edX provides access to Professional Certificates, MicroMasters, as well as Pearson's IT-related courses, while employers find solutions to help fill skill gaps and deliver upskilling opportunities for existing employees.

Pearson Institute of Higher Education (PIHE): Pearson Institute of Higher Education (Pty) Ltd. is in South Africa and is registered with the Department of Higher Education and Training as a private higher education institution under the Higher Education Act, 101, of 1997. We have 12 campuses across South Africa. Our campuses engage in a range of employability initiatives in order to enhance students success in the workplace. We have over 31 qualifications and programmes across a range of faculties, all equipping students with the skills they need in the workplace. We use an optimal combination of technology-enhanced and traditional learning methods, as well as practical application, to prepare students for the technology-driven and fast-changing work environment of the 21st century. Producing employable graduates is a priority for Pearson Institute.

Pearson Learning Platform (PLP): ultimately Pearson's single product platform that leverages best-in-class technology to deliver the future generation of global digital learning experiences. The PLP is not a product, but it will change the way we design and deliver products, providing a modern, reliable consumer grade experience across all devices in all geographies. Products built on PLP will deliver improved outcomes and provide a user-centered, globally consistent, locally optimised, learning experience for our customers.

Pearson Pathways: Designed to uncomplicate the education decision process, Pathways is Pearson's direct to consumer online marketplace for online learning programs that matches people to online degree programs, bootcamps, credentials. Users can research and compare programs, review tuition rates, get real human help, and apply to programs with a single application, free of charge.

Pearson Prep: provides customised study sessions to help students revise and prioritise their time to helps them decide when they are ready for their exams. Students can practice with online flashcards created from their own notes or written by experts to help them prepare more effectively.

Pearson Writer: provides support to help students with writing essays, citing references, and managing projects.

PTE Academic (Pearson Test of English Academic): the fast and fair computerised English proficiency test that is trusted and used by institutions and governments around the world. It is now accepted by the UK Government, alongside the Australian and New Zealand governments and thousands of colleges and universities. A PTE Academic test can be booked up to 24 hours in advance, with 84% of test results delivered within 48 hours, PTE Academic is the convenient and efficient choice for study and work.

To note: PTE Academic UKVI is the name for those taking the test for UK Visa and Immigration purposes

PTE Home (Pearson Test of English Home): approved by the UK Home Office for all family visas, as well as for settlement and citizenship, PTE Home offers a fast and reliable service to help make immigration to the UK as straightforward as possible. Developed to test candidates speaking and listening skills, there are three test levels to choose from. Fast, reliable and convenient: PTE Home tests can be booked up to 24 hours in advance and with a simple pass or fail result, most test-takers will receive their results within just 48 hours.

Pearson VUE: Pearson Virtual University Enterprises (VUE) is a comprehensive computer-based testing company that develops and delivers millions of high-stakes certification and licensure exams for professionals around the globe each year. Pearson VUE clients include many of the most highly regarded and highly respected high-stakes exam owners in every industry from academia and admissions to IT and healthcare. Pearson VUE is the global leader in exam development and psychometric services, programme management tools and services, diverse exam delivery options including online proctored and client proctored, and boasts the most expansive and highly secure network of 20,000 global test centres in nearly 200 countries.

Remote proctoring: in our Pearson VUE business, remote proctoring is when a proctor and a test-taker are not physically located in the same room. In most cases, the testing candidate takes their entire exam on a computer while the proctor watches through an online video camera. 'Remote proctoring' is often synonymous with 'online proctoring.' Pearson VUE's online proctoring solution is called OnVUE.

Revel: improves results by empowering students to actively participate in learning. More than a digital textbook, Revel delivers an engaging blend of author content, media, and assessment. With Revel, students read and practice in one continuous experience – anytime, anywhere, on any device. With assignment and tracking tools, Revel also enables instructors to gauge student understanding and engagement with the material inside and outside the classroom, empowering them to spend class time on meaningful instruction. For example, each additional five hours a student spent on Revel Psychology readings was associated with an increase of 2.19 (±1.10) percentage points on unit exams.

Sistemas: a complete package of products and services for private and public K-12 schools in Brazil. With a single price per student, we provide courseware, educational assistance, professional development, management consulting, and marketing support, as well as digital content.

Smarthinking: expert online tutoring and writing review that gives students 24x7 access to academic help from live professional educators and uses a proven, problem-solving approach to help students learn, gain confidence, and handle future assignments on their own. Complementing Pearson content and technology solutions, Smarthinking's human delivered services have 20 years of experience improving student performance, course persistence, and overall retention. Karen Reilly, Campus Dean of Learning Support at Valencia College, reports "The results of our analysis show that Smarthinking is an important component in our overall academic support programme; it is essential that students have access to tutoring assistance after hours and on weekends – whenever a learning moment is happening."

The Enabling Programme (TEP): one of Pearson's largest business transformation projects. Its aim is to make us a simpler organisation, with globally consistent ways of working across HR, finance, procurement, supply chain, and rights and royalties.

In the US Higher Education landscape, we partner and provide products and services to a diverse array of educational institutions including:

- Community College: sometimes called junior colleges, are two-year schools that provide affordable postsecondary education as a pathway to a four-year degree
- Private Not For Profit: a private foundation that is engaged in social or public benefit activities and is registered as such with the IRS. It derives its revenue from a small group of donors without any intention of earning income for its owners. All the profits and donations of a not-for-profit organisation are used in operating the organisation as per its objectives (i.e., charity or public service)
- 4 Year Public Universities: a university offering a Bachelor's degree that is predominantly funded by public means through a national or subnational government, as opposed to private universities
- For-Profit Universities: a university that is owned and run by a private organisation or corporation.

US School Assessment Business: helps young children and students reach their educational aspirations through meaningful feedback. Testing plays an integral role in determining educator and student success, and we are the largest provider of educational assessment services in the US. We partner with departments of education and educators to develop customised, effective, and scalable assessments that measure 21st century skills and inform instruction throughout the school year. We also partner with test providers to deliver their paper and/or online assessments. Examples of the tests we support include:

- SAT: an entrance exam used by most colleges and universities to make admissions decisions. It is a multiple-choice, pencil-and-paper test with the purpose to measure a high school student's readiness for college, and provide colleges with one common data point that can be used to compare all applicants
- National Assessment of Educational Progress (NAEP): The National Assessment of Educational Progress (NAEP) is the largest nationally representative and continuing assessment of what America's students know and can do in various subject areas
- ACT: The ACT® test is the nation's most popular college entrance exam accepted and valued by all universities and colleges in the US.

Shareholder information

Pearson ordinary shares are listed on the London Stock Exchange and on the New York Stock Exchange in the form of American Depositary Receipts.

Corporate website

The investors' section of our corporate website plc.pearson.com/investors provides a wealth of information for shareholders. It is also possible to sign up to receive email alerts for reports and press releases relating to Pearson at plc.pearson.com/en-GB/investors/shareholders

Shareholder information online

Shareholder information can be found on our website at plc.pearson.com/investors

Our registrar, Equiniti, also provides a range of shareholder information online. You can check your holding and find practical help on transferring shares or updating your details at www.shareview.co.uk. For more information, please contact our registrar, Equiniti, Aspect House, Spencer Road, Lancing, West Sussex, BN99 6DA. Telephone 0371 384 2043* or, for those shareholders with hearing difficulties, textphone number 0371 384 2255*.

Information about the Pearson share price

The company's share price can be found on our website at plc.pearson.com/investors/performance/share-price-dividend. It also appears in the financial columns of the national press.

2020 dividends

	Payment date	Amount per share
Interim	21 September 2020	6 pence
Final[1]	7 May 2021	13.5 pence

1 Subject to approval by shareholders at the Annual General Meeting.

2021 financial calendar

Ex-dividend date	**25 March 2021**
Record date	**26 March 2021**
Last date for dividend reinvestment election	**15 April 2021**
Annual General Meeting	**30 April 2021**
Payment date for dividend and share purchase date for dividend reinvestment	**7 May 2021**

Payment of dividends to mandated accounts

Should you elect to have your dividends paid through BACS, this can be done directly into a bank or building society account, with the tax voucher sent to the shareholder's registered address. Equiniti can be contacted for information on 0371 384 2043*.

Dividend reinvestment plan (DRIP)

The DRIP gives shareholders the right to buy the company's shares on the London stock market with their cash dividend. For further information, please contact Equiniti on 0371 384 2268*.

Individual Savings Accounts (ISAs)

Equiniti offers ISAs in Pearson shares. For more information, please go to www.shareview.co.uk/dealing or call customer services on 0345 300 0430*.

Share dealing facilities

Equiniti offers telephone and internet services for dealing in Pearson shares. For further information, please contact their telephone dealing helpline on 03456 037 037* or, for online dealing, log on to www.shareview.co.uk/dealing. You will need your shareholder reference number as shown on your share certificate.

A postal dealing service is also available through Equiniti. Please telephone 0371 384 2248* for details or log on to www.shareview.co.uk to download a form.

* Lines open 8.30 am to 5.30 pm Monday to Friday (excluding UK public holidays).

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 ShareGift, PO Box 72253, London, SW1P 9LQ.

American Depositary Receipts (ADRs)

Pearson's ADRs are listed on the New York Stock Exchange and traded under the symbol PSO. Each ADR represents one ordinary share. For enquiries regarding registered ADR holder accounts and dividends, please contact Bank of New York Mellon, Shareholder Correspondence (ADR), PO Box 505000, Louisville, KY 40233-5000, telephone 1 (866) 259 2289 (toll free within the US) or 001 201 680 6825 (outside the US). Alternatively, you may email shrrelations@cpushareownerservices.com

Voting rights for registered ADR holders can be exercised through Bank of New York Mellon, and for beneficial ADR holders (and/or nominee accounts) through your US brokerage institution. Pearson will file with the Securities and Exchange Commission a Form 20-F.

Share register fraud: protecting your investment

Pearson does not contact its shareholders directly to provide recommendations or investment advice and neither does it appoint third parties to do so. As required by law, our shareholder register is available for public inspection but we cannot control the use of information obtained by persons inspecting the register. Please treat any approaches purporting to originate from Pearson with caution.

For more information, please log on to our website at plc.pearson.com/en-GB/investors/shareholders/shares-shareholding

Tips on protecting your shares

- Keep any documentation that contains your shareholder reference number in a safe place and shred any unwanted documentation
- Inform our registrar, Equiniti, promptly when you change address
- Be aware of dividend payment dates and contact the registrar if you do not receive your dividend cheque or, better still, make arrangements to have the dividend paid directly into your bank account
- Consider holding your shares electronically in a CREST account via a nominee.

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Reliance on this document
The intention of this document is to provide information to shareholders and is not designed to be relied upon by any other party or for any other purpose.

Forward-looking statements
This document includes forward-looking statements concerning Pearson's financial condition, business and operations and its strategy, plans and objectives. In particular, all statements that express forecasts, expectations and projections, including trends in results of operations, margins, growth rates, overall market trends, the impact of interest or exchange rates, the availability of financing, anticipated cost savings and synergies and the execution of Pearson's strategy, are forward-looking statements.

By their nature, forward-looking statements involve known and unknown risks and uncertainties because they relate to events and depend on circumstances that may occur in the future. They are based on numerous expectations, assumptions and beliefs regarding Pearson's present and future business strategies and the environment in which it will operate in the future. There are various factors which could cause Pearson's actual financial condition, results and development to differ materially from the plans, goals, objectives and expectations expressed or implied by these forward-looking statements, many of which are outside Pearson's control. These include international, national and local conditions, as well as the impact of competition. They also include other risks detailed from time to time in Pearson's publicly-filed documents and, in particular, the risk factors set out in this document, which you are advised to read. Any forward-looking statements speak only as of the date they are made and, except as required by law, Pearson gives no undertaking to update any forward-looking statements in this document whether as a result of new information, future developments, changes in its expectations or otherwise. Readers are cautioned not to place undue reliance on such forward-looking statements.

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