Board of directors

Pearson's board brings a wide range of experience, skills and backgrounds.

CHAIRMAN

Glen Moreno Chairman
aged 70, appointed 1 October 2005

Chairman of the nomination committee and member of the remuneration committee

Glen has more than four decades of experience in business and finance, and is currently deputy chairman of The Financial Reporting Council Limited in the UK and non-executive director of Fidelity International Limited. Previously, Glen was deputy chairman and senior independent director at Lloyds Banking Group plc, senior independent director of Man Group plc and acting chairman of UK Financial Investments Limited, the company set up by HM Treasury to manage the government's shareholdings in UK banks.

EXECUTIVE DIRECTORS

John Fallon Chief executive
aged 51, appointed 3 October 2012

Member of the nomination committee

John became Pearson's chief executive on 1 January 2013. Since 2008 he had been responsible for the company's education businesses outside North America, and a member of the Pearson management committee. He joined Pearson in 1997 as director of communications and was appointed president of Pearson Inc., a role he combined with his communications responsibilities, in 2000. In 2003, he was appointed CEO of Pearson's educational publishing businesses for Europe, Middle East & Africa (EMA) and gradually took on a broader international education brief. Prior to joining Pearson, John was director of corporate affairs at Powergen plc, where he was also a member of the company's executive committee. Earlier in his career, John held senior public policy and communications roles in UK local government.

Robin Freestone Chief financial officer
aged 55, appointed 12 June 2006

Robin's experience in management and accounting includes a previous role as group financial controller of Amersham plc (now part of General Electric) and senior financial positions with ICI plc, Zeneca and Henkel UK. He joined Pearson in 2004 as deputy chief financial officer and became chief financial officer in June 2006. Robin qualified as a chartered accountant with Touche Ross (now Deloitte), and is currently a non-executive director and founder shareholder of eChem Limited. Robin sits on the Advisory Group of the ICAEW's Financial Reporting Faculty and is chairman of The Hundred Group of Finance Directors. He also sits on the CBI's Economic Growth Board.

Board of directors
continued

NON-EXECUTIVE DIRECTORS

David Arculus Non-executive director
aged 67, appointed 28 February 2006

Chairman of the remuneration committee and member of the audit and nomination committees

David has experience in banking, telecommunications and publishing in a long career in business. Currently he is chairman of Numis Corporation plc and the Advisory Board of the British Library and is a member of council of Cranfield University. David's previous roles include the chairmanship of Aldermore Bank plc, O2 plc, Severn Trent plc and IPC Group, as well as chief operating officer of United Business Media plc, group managing director of EMAP plc and a non-executive director of Telefonica S.A. David served from 2002 to 2006 as chairman of the UK government's Better Regulation Task Force, which worked on reducing burdens on business.

Vivienne Cox Senior independent director
aged 54, appointed 1 January 2012

Member of the audit, remuneration and nomination committees

Vivienne has wide experience in energy, natural resources and business innovation. She worked for BP plc for 28 years, in Britain and Continental Europe, in posts including executive vice president and chief executive of BP's Gas, Power & Renewables business and its Alternative Energy unit. She is non-executive director of mining company Rio Tinto plc and energy company BG Group plc, and chairman of the supervisory board of Vallourec, which supplies tubular systems for the energy industry. She is also lead independent director at the UK Department for International Development. Vivienne is a commissioner of the Airports Commission, which was set up by the UK government to examine any requirements for additional UK airport capacity.

Linda Lorimer Non-executive director
aged 61, appointed 1 July 2013

Member of the audit and nomination committees

Linda has a deep background in education strategy, administration and public affairs. She is vice president for Global & Strategic Initiatives at Yale University in New Haven, Connecticut, where her duties include oversight of Yale's Office of International Affairs and Office of Digital Dissemination. Over a 30-year career in higher education, she has been responsible for many of Yale's administrative services including the university's public communications, alumni relations and Office of Sustainability. Previously, Linda served as president of Randolph-Macon Woman's College in Virginia, and had earlier worked at Yale in several senior roles including associate provost. She is a non-executive director of Save the Children (US) and was chair of the board of the Association of American Colleges and Universities.

Ken Hydon Non-executive director
aged 69, appointed 28 February 2006

Chairman of the audit committee and member of the remuneration and nomination committees

Ken's experience in finance and business includes working in the electronics, retail, consumer products and healthcare sectors. He is a non-executive director of Reckitt Benckiser Group plc, one of the world's leading branded consumer goods companies in health, hygiene and home. He is also a non-executive director of Merlin Entertainments plc, the world's second largest visitor attraction operator. From 2004 to 2013 he was a non-executive director of Tesco plc. Previously, Ken was chief financial officer of Vodafone Group plc, the multinational telecommunications company, and financial director of subsidiaries of Racal Electronics.

Josh Lewis Non-executive director
aged 51, appointed 1 March 2011

Member of the remuneration and nomination committees

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

Harish Manwani Non-executive director
aged 60, appointed 1 October 2013

Member of the nomination committee

Harish has an extensive background in emerging markets and senior experience in a successful global organisation. He is chief operating officer of consumer products company Unilever, and serves on the company's executive board. Harish joined Unilever in 1976 as a marketing management trainee in India, and has held senior management roles around the world, including North America, Latin America, Europe, Africa and Asia. He is non-executive chairman of Hindustan Unilever Limited in India, and serves on the board of Whirlpool Corporation in the US. He is also on the board of the Indian School of Business, the Economic Development Board (EDB) of Singapore, and The Human Capital Leadership Institute in Singapore.

Chairman's letter

Dear shareholders

This year, we are reporting for the first time against the 2012 edition of the UK Corporate Governance Code (the Code).

As has been highlighted elsewhere within this report, 2013 was a period of great change in our organisation, following the appointment of John Fallon as chief executive at the start of the year. I would like to take this opportunity to share with you some insights as to how our board and governance operations have adapted throughout the year to take account of Pearson's focus on becoming one global education company.

The Pearson board consists of senior executive management alongside a strong group of non-executive directors drawn from successful international businesses and education institutions with experience of corporate strategy, education, emerging markets, technology and consumer marketing. We continually assess and refresh the board to ensure we maintain an appropriate balance and diversity of skills and experience.

2013 saw a number of changes in Pearson's boardroom, reflecting both the new strategic direction of the business and our desire to maximise the valuable external experience which non-executive directors bring to the table. Executive directors Rona Fairhead and John Makinson stepped down from the board in April and July respectively, although John remains part of the Pearson family in his new role as chairman of Penguin Random House. In August we said goodbye to Susan Fuhrman, a non-executive director for nine years and, at the end of December, Will Ethridge stepped down from his executive position on the board and from his role as CEO of Pearson North American Education, although he will remain a valued adviser to the company during 2014.

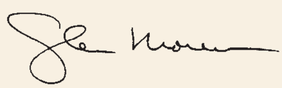
During the year we also welcomed Linda Lorimer and Harish Manwani to the board, as non-executive directors. Linda and Harish bring a wealth of experience in the areas of education, digital initiatives and emerging markets, which reflect precisely those areas on which Pearson is now focused.

With these changes the board now predominantly comprises independent non-executive directors. We believe this re-balancing enables Pearson to benefit from our board's wide range of perspectives and backgrounds, and allows the board to look at the bigger picture of the Group's strategy, performance and value, whilst allowing the executive management to focus on what it does best – driving our company forward.

May 2013 saw the announcement of the new Pearson Executive team. You will have read elsewhere in this report about the new Geographies and Lines of Business along which Pearson is now organised. The presidents of these Geographies and Lines of Business now sit on the Pearson Executive, together with colleagues leading the key enabling functions. The board and I had the pleasure of spending two days discussing strategy with the Pearson Executive in October 2013, of which a little more later in the governance report.

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

We hope this report clearly sets out how your company is run, and how we align governance and our board agenda with the strategic direction of Pearson. We always welcome questions or comments from shareholders, either via our website (www.pearson.com) or in person at our annual shareholders' meeting.



Glen Moreno Chairman

Board governance

Corporate governance

Introduction

The board believes that during 2013 the company was in full compliance with the UK Corporate Governance Code (the Code). A detailed account of the provisions of the Code can be found on the FRC's website at www.frc.org.uk and we encourage readers to view our compliance schedule on the company website at www.pearson.com/investors/shareholder-information/governance

Composition of the board

The board currently consists of the chairman, Glen Moreno, two executive directors including the chief executive, John Fallon, and six independent non-executive directors.

Chairman and chief executive

There is a defined split of responsibilities between the chairman and the chief executive. The chairman is primarily responsible for the leadership of the board and ensuring its effectiveness; 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 the Pearson Executive. The roles and responsibilities of the chairman and chief executive are clearly defined, set out in writing and reviewed and agreed by the board annually.

Chairman

There were no changes to the chairman's significant commitments during the course of 2013.

Senior independent director

Vivienne Cox is the company's senior independent director, having been appointed to the role on 1 January 2013.

Vivienne's role includes meeting regularly with the chairman and chief executive to discuss specific issues, as well as being available to shareholders generally if they should have concerns that have not been addressed through the normal channels.

Following Patrick Cescau's departure in December 2012, he was invited back in February 2013 – in his former role as senior independent director – to conduct a session with the other non-executive directors and the chief executive to appraise the performance of the chairman, including in relation to the effectiveness of the nomination committee as part of the annual board evaluation process.

Vivienne, as incumbent senior independent director, has responsibility for appraising the chairman's performance during 2013 and beyond.

The senior independent director would be expected to chair the nomination committee in the event that it was considering succession to the role of chairman of the board.

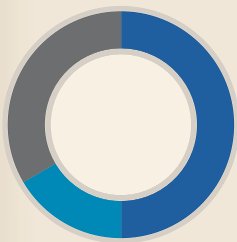
Independence of directors

All of the non-executive directors were considered by the board to be independent for the purposes of the Code during the year ended 31 December 2013.

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 circumstances likely to affect their character or judgement. In addition to this review, each of the non-executive directors is asked annually to complete an independence questionnaire to satisfy requirements arising from Pearson's US listing.

David Arculus and Ken Hydon have each now served on the board for eight years and it is their intention to retire from the board at the 2015 AGM. As chairmen of the remuneration and audit committees respectively, the nomination committee is actively considering options for their successors both in their capacity as non-executive directors and for their chairmanships.

Length of tenure of non-executive directors



Under 3 years	3
3 to 6 years	1
7 years or more	2

Source: Pearson

Conflicts of interest

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

Board meetings

The board held six scheduled meetings in 2013, with some meetings taking place over two or more days. In recent years, we have developed our board meeting agenda to ensure that board discussion and debate is centred on the key strategic issues facing the company. Over the course of 2013, the board maintained a watching brief over the transformation project and received regular formal updates from the chief executive and the transformation team, headed by the director of communications. Other major items covered by the board in the year included:

BUSINESS PERFORMANCE: FEBRUARY 2013, LONDON

- 2012 report and accounts and dividend recommendation
- 2013 operating plan
- Risk assessment and review of mitigating actions
- Annual review of authorised conflicts
- Review of division of responsibilities between chairman and chief executive
- Plans for board effectiveness review
- Discussion of accounting exemption for UK subsidiaries

GOVERNANCE AND SHAREHOLDER MATTERS: APRIL 2013, LONDON

- Focus on forthcoming AGM and review of shareholder issues
- Review of investor relations strategy and share price performance
- Review of corporate social responsibility
- Status update on Penguin Random House transaction and ebook settlement proposal
- Risk assessment and review of mitigating actions
- Governance update

STRATEGY: JUNE 2013, JOHANNESBURG

- Review of Southern African education business including site visits, panel sessions and debates – see case study on page 62 for further information

BUSINESS PERFORMANCE: JULY 2013, LONDON

- Interim results and dividend approval
- Penguin Random House – post-completion update
- Initial review of proposed Multi acquisition
- Consideration of Mergermarket sale

STRATEGY: OCTOBER 2013, LONDON

- Launch of efficacy strategy
- Discussion of New York Attorney General's review of the Pearson Foundation
- Review of standing committee terms of reference
- Workshop with Pearson Executive – see case study on page 61 for further information

STRATEGIC PLAN: DECEMBER 2013, NEW YORK

- Preliminary view of 2014
- Overview of changes to the 2013 year end reporting requirements
- Risk assessment and review of mitigating actions
- Approval of schedule of authority limits

In addition to the six scheduled meetings, the board held one further full meeting in November 2013 to approve the Mergermarket sale and Grupo Multi acquisition and undertook discussions throughout the year, both in formal meetings and as otherwise required, to consider the progress and terms of these and other corporate transactions.

Board governance continued

The following table sets out the attendance of the company's directors at scheduled board meetings during 2013:

	Board meetings attended	Notes
Chairman		
Glen Moreno	6/6	
Executive directors		
John Fallon	6/6	
Will Ethridge	5/6	absent for medical reasons
Rona Fairhead	–	stood down 26 April 2013
Robin Freestone	6/6	
John Makinson	3/3	stood down 1 July 2013
Non-executive directors		
David Arculus	4/6	unable to travel due to injury
Vivienne Cox	6/6	
Susan Fuhrman	3/4	stood down 7 August 2013
Ken Hydon	6/6	
Josh Lewis	6/6	
Linda Lorimer	3/3	appointed 1 July 2013
Harish Manwani	2/2	appointed 1 October 2013

The role and business of the board

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

A schedule of formal matters reserved for the board's decision and approval is available on our website, at www.pearson.com/investors/shareholder-information/governance

A standing committee of the board has been established to approve certain ordinary course of business items such as banking matters, guarantees, intra-group transactions and routine matters relating to employee share plans. The committee has written terms of reference, reviewed and approved each year, which clearly set out its authority and duties. These can be found on the company website at www.pearson.com/investors/shareholder-information/governance

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

Non-executive directors meet with local senior management every time board and committee meetings are held at the locations of operating companies, such as during the board's 2013 trip to South Africa. This allows the non-executive directors to share their experience and expertise with senior managers as well as allowing them to better understand the abilities of senior management, which in turn will help them assess the company's prospects and plans for succession.

Culture and values of the board

During a time of widespread organisational and strategic change at Pearson, the board has had oversight of the plans to embed efficacy firmly into the company's culture.

Since 2012, the board has been kept abreast of the company's intentions through a number of sessions with the chief education advisor. At the most recent such session, in October 2013, the board had the opportunity to discuss building efficacy into all aspects of Pearson's operations, and noted their strong support for Pearson's involvement in the global public dialogue on efficacy and education.

Succession planning

The board considers oversight of succession planning – not only at board and executive management level but for all key positions throughout the business – as one of its prime responsibilities.

2013 has seen a large scale reorganisation of both the company and the structure of its senior management team. Throughout the year, the board received regular updates from the chief executive and the transformation team on the organisational redesign project. This included oversight of the key appointments made to the Pearson Executive and that team's direct reports, the senior leadership group.

CASE STUDY

Board and Pearson Executive

As part of the board's regular programme of updates on the education strategy and organisational design initiatives, a section of the October 2013 board meeting was dedicated to a workshop involving members of the Pearson Executive. Each member of the Pearson Executive discussed with the board their new roles, strategic priorities, and the challenges and opportunities facing their particular business area as they moved towards the new operating structure on 1 January 2014.

The session had benefits for all parties involved – the board was able to learn more about the recently appointed executive team, and to explore with them key issues relating to the geographies, lines of business, products and technologies, whilst demonstrating to the executive its involvement and support during a period of great change.

During the year the board also approved formal contingency plans for temporary absence of the chief executive for health or other reasons.

Board evaluation

The board's review of its effectiveness in 2012 took place during early 2013. A primary focus for the board in 2012 was chief executive succession. On review, the board concluded that the process was structured, detailed and effective.

For 2013, the board identified two key priorities:

- To restructure and strengthen the board through a higher proportion of independent directors with experience and skills relevant to Pearson's strategy, particularly in education and emerging markets. The appointments of Linda Lorimer and Harish Manwani were in line with this objective;
- To keep the board closely informed and involved in Pearson's strategic transformation during the year, including regular detailed briefings on strategy, planned organisational changes and key leadership appointments. The board reviewed plans and actions in considerable detail on six different occasions in 2013, including at the strategy workshop held in October with the Pearson Executive.

The board has also given consideration to the information it receives and how this is reported. As a result, an improved board information system is being designed which will enable the board to more effectively track performance and developments in the business model. As part of this review, in January 2014, we instituted a revised monthly chief executive's letter to the board.

The board also wished to give consideration as to ways in which to maximise the effectiveness of its overseas meetings. In June 2013, the board held a meeting in South Africa, more information on which is set out in the case study on page 62. Following the trip, a short questionnaire was distributed to board members. Particular learning points arising from the board's input related to:

- Continuing to ensure site visits are representative of Pearson's operations in the region;
- The high value placed on meeting the end users of Pearson's products – students and teachers;
- Logistical arrangements both before and during the trip; and
- Ensuring that board presentations are pitched to impart a sufficient level of knowledge for directors to perform their roles.

Board governance continued

It is intended that these learning points will be used to shape future overseas agendas, including potential visits by the board to the US and an emerging market territory during 2014.

During the course of the year the executive directors were also evaluated on their performance against personal objectives. Up to 20% of the executives' total annual incentive opportunity for 2013 was based on functional, operational, strategic and non-financial objectives relevant to their specific area of responsibility. The chairman leads the assessment of the chief executive, and the non-executive directors, led by the senior independent director, conduct a review of the chairman's performance.

In accordance with the Code, the board anticipates undertaking an external evaluation during 2014. The board is currently discussing focus and timing for the process to gain the maximum benefit from the review.

In addition to the review of the board and individual directors, the audit and remuneration committees each undergo an annual evaluation process to review their performance and effectiveness. The process covers areas such as roles and responsibilities, quality and timeliness of meeting materials, opportunity for discussion and debate, dialogue with management and access to independent advice.

CASE STUDY

South Africa

In June 2013, the board visited South Africa for a three-day meeting to understand the economic and political environment, the education landscape and Pearson's South African business, one of the Group's most consistently successful businesses over the last decade.

The board met with a number of Pearson's senior leaders in the region and also took the opportunity to meet with the leader of Pearson's Nigeria business as it learned more about scope for growth in that country and more widely across Africa.

The board spent time visiting local schools as well as reviewing higher education initiatives on the main campus of CTI, Pearson's higher education business in South Africa.

The board also met with Cyril Ramaphosa, the recently elected deputy president of the ANC, at a session involving a range of business leaders, journalists, authors and key opinion leaders in education, exploring how Pearson could do more to tackle problems in education and training in the region.

Finally, outside of the core educational focus of the trip, the board received an update on Penguin in South Africa to learn more about how the merger with Random House is enhancing publishing opportunities.

Directors' training and induction

Directors receive a significant bespoke induction programme and a range of information about Pearson when they join the board. This includes background information on Pearson and details of board procedures, directors' responsibilities and various governance-related issues, including procedures for dealing in Pearson shares and their legal obligations as directors. The induction also includes a series of meetings with members of the board, presentations regarding the business from senior executives and a briefing on Pearson's investor relations programme. The induction programme for Linda Lorimer and Harish Manwani is ongoing and is being tailored to best introduce them to Pearson in a period of organisational change.

The directors' training is supplemented with presentations about the company's operations, by holding board meetings at the locations of operating companies and by encouraging the directors to visit operating companies and local management as and when their schedule allows. The company secretary and general counsel, in conjunction with the Group's advisers, monitor legal and governance developments and update the board on such matters as agreed with the chairman. Directors can also make use of external courses.

Directors' indemnities

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

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

Shareholder engagement

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

In 2013, we continued with our shareholder outreach programme, seeing approximately 780 institutional and private investors at more than 450 different institutions in Australia, Brazil, Canada, China, Continental Europe, India, Japan, Malaysia, Singapore, South Africa, South Korea, the UK and the US.

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

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

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

Private investors represent over 80% of the shareholders on our register and we make a concerted effort to engage with them regularly. Shareholders who cannot attend the AGM are invited to email questions to the chairman in advance at glenmoreno-agm@pearson.com

We encourage our private shareholders to become more informed investors and have provided a wealth of information on our website about managing Pearson shareholdings, see www.pearson.com/investors/shareholder-information for further information, or turn to page 210 of this report. We also encourage all shareholders, who have not already done so, to register their email addresses through our website and with our registrar. This enables them to receive email alerts when trading updates and other important announcements are added to our website.

Board governance continued

We post all company announcements on our website, www.pearson.com, as soon as they are released, and major shareholder presentations are made accessible via webcast or conference call. Our website contains a dedicated investor relations section with an extensive archive of past announcements and presentations, historical financial performance, share price data and a calendar of events. It also includes information about all of our businesses, links to their websites and details of our corporate responsibility policies and activities.

We are committed to ensuring that all our shareholders receive their dividends and encourage the use of our dividend mandate service which enables UK and many overseas shareholders to receive dividends directly into their nominated bank account.

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

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

Our AGM – which will be held on 25 April this year – is an opportunity for all shareholders to meet the board and to hear presentations about Pearson's businesses and results.

Board committees

The board has established three formal committees: the nomination committee, the remuneration committee and the audit committee. The chairmen and members of these committees are appointed by the board on the recommendation (where appropriate) of the nomination committee and in consultation with each relevant committee chairman.

In addition to these board committees, two further committees operate with board input: the standing committee and the reputation and responsibility committee which primarily focuses on reputational risk. More detail on the work of this committee can be found within the principal risks and uncertainties section on pages 41 to 45.

During 2013, the balance of work considered by the board and its formal committees has shifted, so that more time is spent by the committees discussing their areas of expertise, enabling the board meetings to focus on strategy and performance. Reports to the board by each of the committee chairmen continue to form a standing item on each board agenda, ensuring a good communication flow between the bodies.

The following table shows attendance by directors at committee meetings throughout 2013:

	Audit committee meetings	Remuneration committee meetings	Nomination committee meetings
Glen Moreno	–	5/5	5/5
John Fallon	–	–	5/5
David Arculus*	4/5	5/5	3/5
Vivienne Cox	4/5	3/5	5/5
Susan Fuhrman**	3/3	–	3/4
Ken Hydon	5/5	5/5	5/5
Josh Lewis***	5/5	4/4	5/5
Linda Lorimer	–	–	2/2
Harish Manwani	–	–	1/1

* Unable to travel due to injury.

** Stood down on 7 August 2013.

*** Joined remuneration committee on 23 April 2013.

NOMINATION COMMITTEE

Chairman Glen Moreno

Members David Arculus, Vivienne Cox, John Fallon, Ken Hydon, Josh Lewis, Linda Lorimer, Harish Manwani and Glen Moreno

The nomination committee meets at least once a year and at other times as and when required. The committee primarily monitors the composition and balance of the board and its committees, and identifies and recommends to the board the appointment of new directors and/or committee members.

During 2013, the committee met five times with its primary focus being to consider suitable candidates for non-executive positions, culminating in the appointment of Linda Lorimer and Harish Manwani to the board. An external search consultancy, Egon Zehnder, was used during the recruitment process. Egon Zehnder does not have any other connection to Pearson apart from as a search consultancy. Pearson uses a number of leading firms in its board and executive search activities.

During the year, the committee also discussed and approved the appointments of Josh Lewis to the remuneration committee and of Linda Lorimer to the audit committee, in place of Josh Lewis who stepped down at the end of 2013. Linda Lorimer and Harish Manwani also joined the nomination committee following their appointments to the board during the year.

Although the chairman of the board chairs the nomination committee, he is not permitted to chair meetings when the appointment of his successor is being considered or during a discussion regarding his performance. At such times, the senior independent director will chair the meetings.

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

Diversity

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

The committee and the board always take account of diversity in its broadest sense when considering board appointments whilst ensuring that appointments are made based on merit and relevant experience.

Lord Davies' review published in 2011 called for companies to target 25% female representation on boards of FTSE 100 companies by 2015. Pearson is committed to having at least 30% female directors within Lord Davies' 2015 timeframe and currently has two female directors on its board of nine (representing 22%). With the retirement of three female directors over the last year, the committee is actively seeking to recruit at least one additional female board member.

Immediately below board level, the Pearson Executive, not including the chief executive and chief financial officer who are main board directors, has four female members out of a total of 13 (representing 31%).

Pearson considers diversity as an important issue across the Group, not just at board level. One of the key aims of Pearson's diversity policy is to increase the number of leaders coming from a diverse background, including advancing more women into leadership positions. The Responsible business section of this report on pages 47 to 53 contains further information and statistics on diversity throughout the Group.

REMUNERATION COMMITTEE

Chairman David Arculus

Members David Arculus, Vivienne Cox, Ken Hydon, Josh Lewis and Glen Moreno

The remuneration committee reports to the full board and the directors' remuneration report, which has been considered and adopted by the board, is set out on pages 78 to 114.

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

Board governance continued

AUDIT COMMITTEE

Chairman Ken Hydon

Members David Arculus, Vivienne Cox, Ken Hydon and Linda Lorimer

As a committee we welcome the new governance requirements for the financial statements, enshrined in the changes to the Code introduced in 2013, and in particular that the report and accounts need to be fair, balanced and understandable. The production, co-ordination and review of the annual report and accounts is a substantial exercise which needs to be undertaken within a relatively short timeframe, running alongside the formal audit process undertaken by our external auditors. In order to arrive at a position where the audit committee and the board are satisfied with the overall fairness, balance and clarity of the document we discussed the new requirements and agreed with management a robust process of review and approval.

The committee is aware of the recommendations of the Competition Commission and the EU on audit tender and rotation, and currently expects that the tender process will begin no later than 2017 for the 2018 financial year end. The committee reviews the auditor's independence on an annual basis and also monitors on a quarterly basis the nature and level of non-audit fees payable to them. As described later in this report, during 2013 Pearson spent a considerable amount of non-audit fees with PwC. In the main, this expenditure related to specific assurance and tax advisory services associated with the planned creation of the venture between Penguin and Random House, and both management and the audit committee believe that using PwC for these services was the most practical and economical solution for the company. We anticipate that this level of non-audit fee is unusual, and that the balance of audit to non-audit fee paid to PwC will return to more normal levels in 2014.

As I have said in previous years, a key part of the role of the committee is in providing oversight and reassurance to the board with regard to the integrity of the company's financial reporting, internal control policies, and procedures for the identification, assessment and reporting of risk. The latter two have been a particular focus for the Pearson audit committee throughout 2013 as the company embarked on such a wide ranging and significant transformational and organisational change through the launch of its global education strategy. Again, committee meetings are always attended by the chief financial officer and SVP internal audit and compliance and our external auditors, and others often attend by invitation, including the chief executive and chairman.

During the year the audit committee continued to interact with local and business management, and in particular spent time with local management during their visit to South Africa, discussing the implementation of the company's anti-bribery and corruption policy, data protection, disaster recovery planning, risk registers and the Pearson code of conduct. The committee also added an additional fifth meeting to its annual calendar, both to allow an appropriate amount of time be set aside for consideration of all relevant matters, as well as to allow us to focus on a number of risk deep-dives, in particular on data security and privacy, treasury risk and anti-bribery and corruption.

In August 2013, Susan Fuhrman stood down from the board and audit committee, and at the end of 2013, Josh Lewis stood down from the committee and has been replaced by Linda Lorimer. We thank Susan and Josh for their wise counsel over the last few years and welcome Linda.

Ken Hydon

Members

All of the audit committee members are independent non-executive directors and have financial and/or related business experience due to the senior positions they hold or have held in other listed or publicly traded companies and/or similar public organisations. Ken Hydon, chairman of the committee, is the company's designated financial expert. He is a Fellow of the Chartered Institute of Management Accountants, the Association of Chartered Certified Accountants and the Association of Corporate Treasurers. He also serves as audit committee chairman for Reckitt Benckiser Group plc and Merlin Entertainments plc, and until 2012 for Tesco plc and Royal Berkshire NHS Foundation Trust.

The qualifications and relevant experience of the other committee members are detailed on page 56.

Role and responsibilities

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

The committee has been established by the board primarily for the purpose of overseeing the accounting, financial reporting, internal control and risk management processes of the company and the audit of the financial statements of the company.

The committee is responsible for assisting the board's oversight of the quality and integrity of the company's external financial reporting and statements and the company's accounting policies and practices. The group's internal auditor has a dual reporting line to the chief financial officer and chair of the committee and external auditors have direct access to the committee to raise any matter of concern and to report on the results of work directed by the committee. The committee reports to the full board at every board meeting immediately following a committee meeting. It also reviews the independence of the external auditors, including the provision of non-audit services (further details of which can be found on page 73 and note 4 to the financial statements), and ensures that there is an appropriate audit relationship and that auditor objectivity and independence is upheld.

External audit

Based on management's recommendations, the committee reviews the proposal on the appointment of the external auditors. The committee reviewed the effectiveness and independence of the external auditors during 2013 and remains satisfied that the auditors provide effective independent challenge to management.

The review was conducted by distributing a questionnaire to key audit stakeholders including members of the audit committee, the chief executive, chief financial officer, SVP company secretarial, SVP internal audit and compliance, operating company CFOs and heads of corporate functions. In relation to specific comments received, the lead audit partner explained to the committee how PwC were monitoring and reviewing each highlighted area and confirmed that they would consider how to adapt their approach in light of feedback.

In addition, in accordance with our external auditor policy, Group internal audit performs an annual assessment of audit fees, services and independence. This review takes into account internal and external information and benchmarks and forms the basis for a recommendation by the committee to the board in respect of the appointment and compensation of our external auditor.

Recognising the importance of maintaining auditor independence and objectivity, the committee paid particular attention to this matter during 2013. PwC were appointed to provide assurance procedures over the completion balance sheet and tax advice on the Penguin Random House transaction. This decision was made only after careful consideration of the alternatives, as well as ensuring that appropriate safeguards were put in place to maintain independence. As a result of this decision, non-audit fees paid to PwC exceeded Pearson's target proportion of audit fees during the year.

Board governance continued

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

Pearson's last audit tender was in respect of the 1996 year end resulting in the appointment of Price Waterhouse as auditors. Given the recent rotation of lead audit partner ahead of the 2013 reporting period and giving careful consideration to the timing and other practicalities of undertaking a formal audit tendering process, the committee agreed that a tender process would commence no later than 2017 to ensure auditors have been appointed in time for the 2018 year end audit, following the end of the current lead partner's term. The committee is also monitoring developments from the Competition Commission on audit tendering and at EU level regarding mandatory audit rotation for listed companies, and will factor any legislative requirements into its future plans for audit tender.

Significant issues

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

At the July 2013 audit committee meeting, the committee discussed and approved the auditors' Group audit plan and reviewed the key risks of misstatement of the Group's financial statements, which were updated at the December 2013 committee meeting. The table below sets out the significant issues considered by the audit committee together with details of how these items have been addressed.

SIGNIFICANT ISSUES	HOW ISSUES WERE ADDRESSED
Penguin Random House transaction: A number of complex accounting and business model changes including disposal accounting, valuation of the new business and intangibles, associate accounting including harmonisation of accounting policies, changes to existing operating model of shared services, infrastructure and corporate costs such as pensions.	The committee discussed this issue at a number of meetings, including reviewing management's discussion of the significant accounting judgements and estimates and monitoring the views of the external auditors. The committee and management have visibility of Penguin Random House's accounting to ensure that all accounting policies, valuations and adjustments are considered in Pearson's accounts. The committee monitors and, where appropriate, challenges mitigating actions by management. These actions include key Sarbanes-Oxley controls over acquisition and disposal accounting including review by the technical accounting team, use of external valuation experts and use of local management to ensure that policies and operating model are communicated and adjusted as required.
Revenue recognition: This is considered significant in light of a number of products and services sold by Pearson where revenue recognition practices are complex and management assumptions and estimates are necessary.	The committee receives a regular presentation from management on revenue recognition and routinely monitors the views of the external auditors on this issue. The committee has visibility to internal audit findings relating to revenue recognition controls and processes, the related management action plans and timely closure of open issues. The committee monitors and, where appropriate, challenges mitigating actions by management. These actions include key Sarbanes-Oxley controls and identification of significant contracts through the 'large and unusual' process, such that accounting treatment can be agreed by specialists.

SIGNIFICANT ISSUES	HOW ISSUES WERE ADDRESSED
US tax activity: Changes to processes, structure and strategy in 2012 and 2013, and IRS audit activity.	The committee met with the SVP, Tax twice during 2013, discussed the tax strategy and held a risk deep dive into the tax process in October. Key tax accounting matters including judgements and estimates were reported to the committee by management, and the committee monitored the views of the external auditors on the company's tax accounting. The committee monitors and, where appropriate, challenges mitigating actions by management. These actions include key Sarbanes-Oxley controls in place in the US, and improved UK central oversight to ensure critical judgements are appropriately reviewed and understood.
Impairment of goodwill and intangibles: The Group carries significant goodwill and acquired intangible asset balances. There is judgement in the identification and aggregation of cash generating units (CGUs) and in the assumptions used in the annual goodwill impairment review.	The committee considered the results of the Group's annual goodwill impairment review and management's judgements and assumptions used in arriving at a valuation for each of the Group's CGUs. The key assumptions are cash flows derived from strategic plans, long-term growth rates and weighted average cost of capital. The committee also considered sensitivities to changes in assumptions and related disclosures as required by IAS 36 'Impairment of Assets'. The annual impairment review in 2013 showed that there was sufficient headroom in each of the Group's CGUs and based on the sensitivity analysis a reasonably possible change in any of the assumptions is unlikely to cause an impairment in any of the CGUs.

The committee discussed these issues with the auditors at the time of their review of the half year interim financial statements in July 2013 and again at the conclusion of their audit of the financial statements for the year in February 2014. All the significant issues were areas of focus for the auditors, as detailed in their report on pages 116 to 122.

In December 2013, the committee discussed with the auditors the status of their work, focusing in particular on internal controls and covering the significant issues outlined above.

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

- The work they had conducted over revenue, which included targeted procedures and testing of products and services which were considered to have more complex revenue recognition, such as multiple element arrangements (e.g. the provision of supplementary print or digital materials or training with textbooks) and certain long-term contracts in the education businesses;
- Their evaluation of the directors' assessment of the Penguin Random House transaction and assessment of valuations of that business and associate accounting;
- The work they had done to understand the Group's tax strategy and identify business and legislative risks, to challenge key underlying assumptions and assess the recoverability of deferred tax assets;
- Their assessment and evaluation of returns provisions and controls in the shipment and returns processes, particularly in light of the ongoing business transition from print to digital;
- Their evaluation of the recoverability of pre-publication assets and inventories. These are considered to be material and judgement is required to evaluate their valuation, plus estimating recoverability may be more complex during the transition to digital;
- Their focus on goodwill impairment due to the Group's significant goodwill and intangible asset balances, and the work they had done to test management's impairment analysis, underlying assumptions, calculation of discount and growth rates and integrity of the valuation model;
- The results of their controls testing to date for Sarbanes-Oxley Act section 404 reporting purposes and in support of their financial statements audit; and
- The review of the company's 'going concern' reports.

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

Board governance continued

Training

The committee receives regular technical updates as well as specific or personal training as appropriate. During 2013, the committee discussed with PwC at an audit committee meeting the new Code requirement for the annual report and accounts to be 'fair, balanced and understandable', and the disclosure committee undertook a training session on the subject.

Committee members also meet with local management on an ongoing basis in order to gain a better understanding of how Group policies are embedded in operations.

Meetings

The committee met five times during the year with the following in attendance: the chief financial officer; SVP internal audit and compliance; members of the senior management team; and the external auditors. Additionally, the chief executive and chairman periodically attended committee meetings. The committee also met regularly in private with the external auditors and the SVP internal audit and compliance.

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

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

- The 2012 annual report and accounts: preliminary announcement, financial statements and income statement;
- The Group accounting policies;
- Compliance with the Code;
- Form 20-F and related disclosures including the annual Sarbanes-Oxley Act section 404 attestation of financial reporting internal controls;
- Receipt of the external auditors' report on the Form 20-F and on the year end audit;
- Penguin Random House transaction – accounting matters;
- Assessment of the effectiveness of the Group's internal control environment;
- Reappointment, remuneration and engagement letter of the external auditors;
- Provision of non-audit services by PwC;
- Review of the interim financial statements and announcement;
- Review of key findings of over 100 Group internal audits and special projects;
- Annual reapproval of the Group internal audit mandate;
- Compliance with SEC and NYSE requirements including Sarbanes-Oxley Act;
- Reviews of the effectiveness of the audit committee, the external auditors and the Group internal audit function;
- External auditor benchmarking;
- Review of the committee's terms of reference;
- Annual internal audit plan;
- Review of company risk maps and mitigating actions for top risks;
- Risk deep dives – anti-bribery and corruption, data security and privacy, and treasury risk;
- Implementation of new health and safety strategy, policy and reporting of any significant incidents;
- Fraud, whistleblowing and code of conduct matters;
- Review of Group tax strategy, tax risks and tax departmental structure; and
- Annual review of treasury policy and strategy.

At its December meeting, the committee considered the Group's business continuity planning, the latest internal report on which indicated that readiness to withstand significant business interruption does not currently meet Pearson's own stringent standards. It was noted that workable plans generally existed but that, in light of the scale of business transformation, these plans had not been updated or tested within the past year. The committee reported this risk to the board at its December meeting where it was noted that management had in principle accepted the level of risk on the basis that the restructured organisation would change the focus of business continuity plans which would consequently require updating.

In February 2014, the committee also considered the 2013 annual report and accounts, including the preliminary announcement, financial statements, strategic report, directors' report and corporate governance compliance statement.

Internal control and risk management

The directors confirm they have conducted a review of the effectiveness of the Group's systems of risk management and internal controls, including strategic, financial, operational and compliance controls and risk management systems, in accordance with the Code and Turnbull guidance. These systems have been operating throughout the year and to the date of this report.

During 2013, the semi-annual reporting of top risks was reviewed by executive management as well as the board and audit committee. The principal risks are set out on pages 41 to 45, together with mitigating factors. During the year, the audit committee considered the oversight of specific selected principal risks, through a series of risk 'deep dives'. This is covered in more detail in the separate report on the audit committee.

The key elements and procedures that have been established to provide effective risk management and internal control systems are described below. We recognise that during 2014, we will need to align these existing procedures to the new organisation structure.

Control environment

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

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

The identification and mitigation of significant business risks is the responsibility of Group senior management and the management team for each business area – being the heads of the Lines of Business, Geographies and enabling functions. Each business area, including the corporate centre, maintains internal controls and procedures appropriate to its structure, business environment and risk assessment, whilst complying with Group policies, standards and guidelines.

Financial management and reporting

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

We have an ongoing process to monitor the risks and effectiveness of controls in relation to the financial reporting and consolidation process including the related information systems. This includes up-to-date Group financial policies, formal requirements for finance functions, Group consolidation reviews and analysis of material variances, Group finance technical reviews, including the use of technical specialists, and review and sign-off by senior finance managers. These processes are subject to reviews based on Group internal audit's risk based audit programme. The Group finance function also monitors and assesses these processes, through a finance compliance function.

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

The effectiveness of key financial controls is subject to management review and self-certification and independent evaluation by Group internal audit.

Board governance continued

An enterprise risk management (ERM) framework is in place to identify, evaluate and manage risks, including key financial reporting risks. Business areas undertake semi-annual risk reviews to identify new or potentially under-managed risks. Throughout the year, risk discussions are facilitated by the risk assurance team with Group and business area management to identify the key risks the company faces in achieving its objectives, to assess the probability and impact of those risks and to document the actions being taken to manage those risks. The Pearson Executive reviews the output of these sessions, focusing on the key risks facing the business. Management has the responsibility to consider and execute appropriate action to mitigate these risks whenever possible. The results of these reviews are reported to the audit committee and the board in detail.

Group internal audit

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

The SVP internal audit and compliance oversees compliance with our code of conduct and works with senior legal and human resources personnel to investigate any reported incidents including ethical, corruption and fraud allegations. The Pearson anti-bribery and corruption programme provides the framework to support our compliance with various anti-bribery and corruption regulations such as the UK Bribery Act 2010 and the US Foreign Corrupt Practices Act.

Treasury management

The treasury department operates within policies approved by the board and its procedures are reviewed regularly by the audit committee. Major transactions are authorised outside the department at the requisite level, and there is an appropriate segregation of duties. Frequent reports are made to the chief financial officer and regular reports are prepared for the audit committee and the board.

Insurance

Pearson purchases comprehensive insurance coverage where this is available on a cost-effective basis. Pearson's insurance subsidiary, Spear Insurance Company Limited, is used to leverage the risk retention capability of the Group and to achieve a balance between retaining insurance risk and transferring it to external insurers.

Going concern

Having reviewed the Group's liquid resources and borrowing facilities and the Group's 2014 and 2015 cash flow forecasts, the directors believe that the Group has adequate resources to continue as a going concern. For this reason, the financial statements have, as usual, been prepared on that basis. Information regarding the Group's borrowing liabilities and financial risk management can be found in notes 18 and 19 on pages 164 to 172.

Share capital

Details of share issues are given in note 27 to the accounts on page 185. 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 2013, 818,580,447 ordinary shares were in issue. At the AGM held on 26 April 2013, the company was authorised, subject to certain conditions, to acquire up to 81,746,807 ordinary shares by market purchase. Shareholders will be asked to renew this authority at the AGM on 25 April 2014.

Information provided to the company pursuant to the Financial Conduct Authority's Disclosure and Transparency Rules (DTR) is published on a Regulatory Information Service and on the company's website.

As at 4 March 2014, being the latest practicable date before the publication of this report, the company had been notified under DTR5 of the following significant voting rights in its shares:

	Number of voting rights	Percentage as at date of notification
Harbor International Fund	24,598,034	3.01%
Libyan Investment Authority	24,431,000	3.01%

Annual General Meeting (AGM)

The notice convening the AGM, to be held at 12 noon on Friday, 25 April 2014 at 8 Northumberland Avenue, London WC2N 5BY, is contained in a circular to shareholders to be dated 24 March 2014.

Registered auditors

In accordance with section 489 of the Act, a resolution proposing the reappointment of PricewaterhouseCoopers LLP (PwC) as auditors to the company will be proposed at the AGM, at a level of remuneration to be agreed by the directors.

Auditors' independence

In line with best practice, our relationship with PwC is governed by our external auditors policy, which is reviewed and approved annually by the audit committee. The policy establishes procedures to ensure the auditors' independence is not compromised, as well as defining those non-audit services that PwC may or may not provide to Pearson. These allowable services are in accordance with relevant UK and US legislation.

The audit committee approves all audit and non-audit services provided by PwC. Certain categories of allowable non-audit services have been pre-approved by the audit committee subject to the authorities below:

- Pre-approved non-audit services can be authorised by the chief financial officer up to £100,000 per project, subject to a cumulative limit of £500,000 per annum;
- Acquisition or disposal transactions and due diligence up to £100,000 per project may be performed by our external auditors, in light of the need for confidentiality. Any project/transaction generating fees in excess of £100,000 must be specifically approved by the audit committee;
- Tax compliance and related activities up to the greater of £1,000,000 per annum or 50% of the external audit fee; and
- For forward-looking tax advisory services we use the most appropriate adviser, usually after a tender process. Where we decide to use our independent auditors, authority, up to £100,000 per project subject to a cumulative limit of £500,000 per annum, has been delegated by the audit committee to management.

Services provided by PwC above these limits and all other allowable non-audit services, irrespective of value, must be approved by the audit committee. Where appropriate, services will be tendered prior to a decision being made as to whether to award work to the auditors.

The audit committee receives regular reports summarising the amount of fees paid to the auditors. During 2013, Pearson spent a considerable amount of non-audit fees with PwC. In the main, this expenditure related to specific assurance and tax advisory services associated with the planned creation of the venture between Penguin and Random House. PwC were selected only after consideration that it was most practical and economical to utilise PwC for these services. We anticipate that this level of non-audit fee is unusual, and that the balance of audit to non-audit fee paid to PwC will return to more normal levels in 2014. Other significant non-audit work performed by PwC during 2013 was:

- Tax compliance services related to a routine audit by the US Internal Revenue Service;
- Assurance services on a corporate bond issued in May 2013; and
- Other assurance services which were individually less than £100,000 per project.

In each case, PwC was selected as they were best able to provide the services we required at a reasonable fee and within the terms of our external auditors policy. To assist in ensuring that independence and objectivity is maintained, for forward-looking tax advisory and due diligence work PwC assign a different partner from the one leading the external audit.

A full statement of the fees for audit and services is provided in note 4 to the accounts on page 141.

Board governance continued

Fair, balanced and understandable reporting

Pearson is mindful of the Code's revised principle C.1.1 relating to fair, balanced and understandable reporting and has accordingly built in additional steps to its annual report timetable to ensure that the directors are given sufficient opportunity to review, consider and comment on the report.

The disclosure committee and the board each held an additional meeting as part of their review process, and members of the disclosure committee also attended a training session provided by PwC to better understand the requirements. In addition, the audit committee is available to advise the board on certain aspects of the report, to enable the directors to fulfil their responsibility in this regard.

Statement of directors' responsibilities

The directors are responsible for preparing the annual report, the report on directors' remuneration and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the Group and parent company financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and the Group and of the profit or loss of the Group for that period.

In preparing these financial statements, the directors are required to:

› Select suitable accounting policies and then apply them consistently;
› Make judgements and accounting estimates that are reasonable and prudent;
› State whether applicable IFRSs as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements; and
› Prepare the financial statements on a going concern basis, unless it is inappropriate to presume that the company and/or the Group will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and the Group and enable them to ensure that the financial statements and the report on directors' remuneration comply with the Act and, as regards the Group financial statements, Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Each of the directors, whose names and functions are listed on pages 55 and 56, confirm that to the best of their knowledge:

› The Group financial statements, which have been prepared in accordance with IFRSs as adopted by the European Union, give a true and fair view of the assets, liabilities, financial position and profit of the Group and company; and
› The directors' report contained in the annual report includes a fair review of the development and performance of the business and the position of the company and Group, together with a description of the principal risks and uncertainties that they face.

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

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

b) they have taken all the steps that they ought to have taken as directors in order to make themselves aware of any relevant audit information and to establish that the company's auditors are aware of that information.

In addition, the directors as at the date of this report consider that the annual report, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the company's performance, business model and strategy.

Sections one to four of this document contain the information required to be disclosed in the directors' report and were approved by the board on 10 March 2014 and signed on its behalf by

Philip Hoffman Secretary

Additional information for shareholders

Set out below is other statutory and regulatory information that Pearson is required to disclose in its directors' report.

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.

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 for every ordinary share of which they are the registered holder. A resolution put to the vote at a general meeting is decided on a show of hands unless before, or on the declaration of the result of, a vote on a show of hands, a poll is demanded. A poll can be demanded by the chairman of the meeting, or by at least three shareholders (or their representatives) present in person and having the right to vote, or by any shareholders (or their representatives) present in person having at least 10% of the total voting rights of all shareholders, or by any shareholders (or their representatives) present in person holding ordinary shares on which an aggregate sum has been paid up of at least 10% of the total sum paid up on all ordinary shares. At this year's AGM voting will 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.

No shareholder is, unless the board decides otherwise, entitled to attend or vote either personally or by proxy at a general meeting or to exercise any other right conferred by being a shareholder if he/she or any person with an interest in shares has been sent a notice under section 793 of the Act (which confers upon public companies the power to require information with respect to interests in their voting shares) and he/she or any interested person failed to supply the company with the information requested within 14 days after delivery of that notice. The board may also decide, where the relevant shareholding comprises at least 0.25% of the nominal value of the issued shares of that class, that no dividend is payable in respect of those default shares and that no transfer of any default shares shall be registered.

Pearson operates two employee benefit trusts to hold shares, pending employees becoming entitled to them under the company's employee share plans.

Board governance continued

There were 9,282,365 shares so held as at 31 December 2013. Each trust has an independent trustee which has full discretion in relation to the voting of such shares. A dividend waiver operates on the shares held in these trusts.

Pearson also operates a nominee shareholding arrangement known as Sharestore which holds shares on behalf of employees. There were 4,564,039 shares so held as at 31 December 2013. The beneficial owners of shares held through Sharestore are invited to submit voting instructions online at www.shareview.co.uk. If no instructions are given by the beneficial owner, the trustees holding these shares will not exercise the voting rights.

Transfer of shares

The board may refuse to register a transfer of a certificated share which is not fully paid, provided that the refusal does not prevent dealings in shares in the company from taking place on an open and proper basis. The board may also refuse to register a transfer of a certificated share unless (i) the instrument of transfer is lodged, duly stamped (if stampable), at the registered office of the company or any other place decided by the board, and is accompanied by the certificate for the share to which it relates and such other evidence as the board may reasonably require to show the right of the transferor to make the transfer; (ii) it is in respect of only one class of shares; and (iii) it is in favour of not more than four transferees.

Transfers of uncertificated shares must be carried out using CREST and the board can refuse to register a transfer of an uncertificated share in accordance with the regulations governing the operation of CREST.

Variation of rights

If at any time the capital of the company is divided into different classes of shares, the special rights attaching to any class may be varied or revoked either:

(i) with the written consent of the holders of at least 75% in nominal value of the issued shares of the relevant class; or

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

Without prejudice to any special rights previously conferred on the holders of any existing shares or class of shares, any share may be issued with such preferred, deferred, or other special rights, or such restrictions, whether in regard to dividend, voting, return of capital or otherwise as the company may from time to time by ordinary resolution determine.

Appointment and replacement of directors

The Articles contain the following provisions in relation to directors:

Directors shall number no less than two. Directors may be appointed by the company by ordinary resolution or by the board. A director appointed by the board shall hold office only until the next AGM and shall then be eligible for reappointment, but shall not be taken into account in determining the directors or the number of directors who are to retire by rotation at that meeting. The board may from time to time appoint one or more directors to hold executive office with the company for such period (subject to the provisions of the Act) and upon such terms as the board may decide and may revoke or terminate any appointment so made.

The Articles provide that, at every AGM of the company, at least one-third of the directors shall retire by rotation (or, if their number is not a multiple of three, the number nearest to one-third). The first directors to retire by rotation shall be those who wish to retire and not offer themselves for re-election. Any further directors so to retire shall be those of the other directors subject to retirement by rotation who have been longest in office since they were last re-elected but, as between persons who became or were last re-elected on the same day, those to retire shall (unless they otherwise agree among themselves) be determined by lot. In addition, any director who would not otherwise be required to retire shall retire by rotation at the third AGM after they were last re-elected.

Notwithstanding the provisions of the Articles, the board has resolved that all directors should offer themselves for re-election annually, in accordance with the Code.

The company may by ordinary resolution remove any director before the expiration of his/her term of office. In addition, the board may terminate an agreement or arrangement with any director for the provision of his/her services to the company.

Powers of the directors

Subject to the company's Articles, the Act and any directions given by special resolution, the business of the company will be managed by the board who may exercise all the powers of the company, including powers relating to the issue and/or buying back of shares by the company (subject to any statutory restrictions or restrictions imposed by shareholders in general meeting).

Significant agreements

The following significant agreements contain provisions entitling the counterparties to exercise termination or other rights in the event of a change of control of the company:

Under the $1,750,000,000 revolving credit facility agreement dated November 2010 which matures in November 2015 between, amongst others, the company, HSBC Bank plc (as facility agent) and the banks and financial institutions named therein as lenders (the Facility), any such bank may, upon a change of control of the company, require its outstanding advances, together with accrued interest and any other amounts payable in respect of such Facility, and its commitments, to be cancelled, each within 60 days of notification to the banks by the facility agent. For these purposes, a 'change of control' occurs if the company becomes a subsidiary of any other company or one or more persons acting either individually or in concert, obtains control (as defined in section 1124 of the Corporation Tax Act 2010) of the company.

Shares acquired through the company's employee share plans rank *pari passu* with shares in issue and have no special rights. For legal and practical reasons, the rules of these plans set out the consequences of a change of control of the company.

Report on directors' remuneration

Dear shareholders

I am pleased to present our report on directors' remuneration for 2013.

The report and related resolutions will be put forward for your consideration and approval at the annual general meeting on 25 April 2014.

I should like to start by summarising the decisions on, and the changes to, directors' remuneration made during the year and importantly the context in which those changes occurred and decisions have been taken.

Pearson has a unique set of advantages with which to help meet the global demands for better education and skills. And, by being better able to meet some of the biggest challenges in global education, we can build a stronger, more profitable and faster growing company.

To get there Pearson has fundamentally changed the way the company is organised. From January this year, Pearson is being run as one globally-connected education company, working to an operating model designed specifically to support a global education strategy, and a new executive team has been appointed to lead it. The new model ensures that the company will be organised around a smaller number of global products and platforms, built around a single, world-class infrastructure and common systems and processes.

Over time, this will help Pearson to grow more quickly, as it will free up resources to invest in digital transformation, and the new, more service oriented, products that are vital to future growth. It should enable the company to increase the rate of innovation and invention, by focusing on the research and development of the next generation of global products that will have the data to demonstrate their positive impact on learning outcomes.

Pearson's executive remuneration arrangements have been reviewed to align with and better support this strategy. Executive remuneration decisions have been made after careful consideration of the needs of the business, the transformation and reorganisation of the business and the impact on roles and responsibilities, the pay markets in which Pearson operates and changes in pay elsewhere within the company.

This strategy also informs our remuneration philosophy and policy and complements our more traditional financial measures. In financial terms, Pearson's goal is to achieve sustainable growth on three key financial goals (earnings, cash and return on invested capital) and reliable cash returns to our investors through healthy and growing dividends. We believe those are, in concert, good indicators that we are building the long-term value of Pearson. So those measures (or others that contribute to them) form the basis of our annual budgets and strategic plans and the basis for annual and long-term incentives.

The remuneration committee is continually sensitive to the current social and economic environment surrounding executive compensation.

We welcome the UK government's action to improve the clarity and transparency of remuneration disclosure. We welcome the introduction of the new executive remuneration reporting requirements including a new binding vote on policy.

We hope that these changes will continue to demonstrate the link between our remuneration policy and practice and the company's strategy and performance, as well as our commitment to shareholder engagement.

Performance in 2013

In 2013, trading was tough in many of our biggest and most established markets. Overall, we saw:

- sales up 2% on 2012 at constant exchange rates
- adjusted operating profit 6% lower before net restructuring charges
- our dividend raised 7% which was Pearson's 22nd straight year of increasing our dividend above the rate of inflation.

Over the past ten years we have increased our dividend at a compound annual rate of 7%, returning £2.9bn to shareholders. Restructuring is on track to deliver benefits in 2014 and beyond.

Principles of remuneration policy

The remuneration committee believes that the purpose of its remuneration policy is to support the company's strategy and to help deliver sustained performance and consistent long-term value creation in the interests of all stakeholders.

Our reward policy is aligned with the interests of all stakeholders in providing:

- competitive base salaries that reflect the market and individual roles and contribution
- a high proportion of total remuneration being delivered in variable forms that are directly linked to the annual and long-term performance of the company
- annual incentives that reward achievement of strategic goals

- long-term incentives that drive long-term earnings and share price growth and encourage participants in these plans to acquire and hold Pearson shares in line with shareholders' interests
- the opportunity for many people at Pearson to share in the company's success through cash-based annual incentives and bonuses and worldwide participation in share ownership plans, continuing practices first started in 1998.

We continue to keep our remuneration policy under review in light of the prevailing economic conditions and the impact of these on the company's objectives and strategy.

What we did in 2013

Looking back to some specific aspects of policy and practice in 2013:

- we reviewed and established an appropriate starting remuneration package for John Fallon comprising base salary, annual and long-term incentives, allowances and benefits
- we reviewed and amended the service agreements for those executive directors, including the CEO, who continued to serve throughout 2013. The consequence of this review was to remove any entitlement to annual incentive from the calculation of any compensation that might be payable on termination of employment by the company without notice or cause
- we undertook a regular periodic review of base salaries for 2013 taking into account general economic and market conditions, the level of increases made across the company as a whole, the remuneration of executives in similar positions in comparable companies and individual performance
- appointments were made to the new Pearson Executive
- annual incentives paid to executives for 2013 were below target, as they were in 2012, reflecting performance in a tough trading environment
- there was a nil pay-out on long-term incentives based on 2013 performance reflecting below threshold performance against the company's three-year targets for earnings per share growth, return on invested capital and relative total shareholder return.

What we've planned for 2014

Looking forward, for 2014:

- we have undertaken a full review of the company's executive remuneration policy and either confirmed or, where necessary, established maximum opportunities for each of the different elements of remuneration to ensure that this policy fully supports the needs of the business
- we have aligned executive remuneration policy with the new global education strategy and 'one Pearson' organisation
- we have listened to, and sought to address, shareholders' concerns and wishes regarding simplicity and alignment of interests
- we actively consulted with our major shareholders and their representative bodies on the directors' remuneration policy set out in this report.

As a consequence:

- while we have established maximum opportunities for each of the different elements of remuneration, in all cases these represent maximum limits or caps to cover all likely eventualities for the life of the policy and should not be deemed to be a target or an entitlement. For example, for 2014 there will be no increase in maximum annual incentive opportunities and award levels under the long-term incentive plan will be consistent with those seen in recent years and below the policy maximum
- starting in 2014 and onwards, the size of the global annual incentive pool and the funding of all annual incentives across the company will be linked to overall Pearson results
- for performance-related long-term incentive awards for 2014 for members of the Pearson Executive, to emphasise the importance of earnings growth and to reward the delivery of the desired outcomes from the strategic effort, the weighting of the performance metrics within the Pearson long-term incentive plan will be changed from one-third on each measure to half on earnings per share growth, one-third (no change) on return on invested capital and one-sixth on relative total shareholder return
- for performance-related long-term incentive awards for 2015 and onwards, the averaging period for the calculation of relative total shareholder return will be moved to the period running up to the year end and the length of the averaging period will be increased to three months. This is understood to be more in line with institutional investors' preferences
- to promote simplicity, the previous annual bonus share matching plan has ceased to operate with the last awards made in 2013 in respect of annual bonus for 2012. We have not made any compensatory adjustments to annual or long-term incentive opportunities to take this into account

Report on directors' remuneration continued

- for performance-related long-term incentive awards for members of the Pearson Executive, performance will continue to be tested over three years and 75% of the vested shares will continue to be released at that point. However, starting with awards for 2014, there will be a mandatory restriction on participants' ability to dispose of the 75% of the vested shares (other than to meet personal tax liabilities) for a further two years. Furthermore, participants' rights to the release of the 25% of the vested shares will be subject to continued employment over the same period
- we have affirmed our commitment to share ownership and increased our mandatory shareholding guidelines to 300% of salary for the CEO and 200% of salary for other executive directors (compared to 200% and 125% respectively). We will continue to set performance targets for our annual and long-term incentive arrangements that are appropriately stretching
- on incentive pay-outs, we have clarified our arrangements for adjusting for malus and strengthened our provisions for clawback.

We are confident that these changed remuneration arrangements will better suit the needs of Pearson going forward.

Our policy and implementation is summarised in more detail in the remainder of this report.

I look forward to the ongoing support of Pearson shareholders on both the advisory vote on the executive remuneration arrangements as they were operated in the year as well as the forward-looking remuneration policy which is the subject of the binding vote.

I am personally committed to an ongoing dialogue with shareholders regarding executive remuneration and would therefore welcome any observations or questions that individual shareholders may wish to put forward to me. I can be contacted at david.arculus@integral2.com.

Finally, I would like to thank my fellow members of the committee and the people who have assisted us for their contribution over the past year.

Yours sincerely,

David Arculus
Chairman, remuneration committee

Introduction

The rest of this report on directors' remuneration comprises:

- the directors' remuneration policy report – a forward-looking statement on remuneration policy for 2014 and beyond; and
- the annual remuneration report – a report on remuneration practice in 2013.

Together, this report was compiled in accordance with Schedule 8 of the Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2008 and was approved by the board of directors on 10 March 2014.

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

Where required under current regulations, the following tables have been subject to audit:

- single total figure of remuneration and prior year comparison (page 97)
- remuneration paid to the chairman and non-executive directors (page 98)
- retirement benefits (page 101)
- details of long-term share interests including awards made in 2013 (pages 102 to 105)
- payments to former directors (pages 105 and 106)
- payments for loss of office (page 107)
- interests of directors and value of shareholdings (page 108).

Directors’ remuneration policy report

This report outlines the company’s policy on directors’ remuneration that applies to executive directors, the chairman and non-executive directors. Reference is also made to the remuneration policy for other members of the Pearson Executive (currently 13 in number) who are not directors but who fall within the committee’s remit.

The policy is intended to last three years and will take effect, subject to shareholder approval, at the AGM on 25 April 2014.

The policy report is comprised of the following parts:

› future policy table
› selection of performance measures and target setting
› legacy arrangements under the annual bonus share matching plan
› remuneration policy for other employees
› pay and performance scenario analysis
› other policies relating to directors such as recruitment, service contracts and termination provisions, executive directors’ non-executive directorships
› considerations taken into account when determining remuneration policy for directors
› chairman’s and non-executive directors’ remuneration.

The committee considers that a successful remuneration policy needs to be sufficiently flexible to take account of future changes in the company’s business environment and in remuneration practice. Our starting point continues to be that total remuneration should reward both short- and long-term results, delivering competitive rewards for target performance but outstanding rewards for exceptional performance.

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

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

Report on directors' remuneration continued

Future policy table for executive directors

Total remuneration is made up of fixed and performance-linked elements, with each element supporting different strategic objectives. Total remuneration is normally reviewed annually and benchmarked against total remuneration for similar positions in comparable companies.

Base salary

PURPOSE AND LINK TO STRATEGY

- Helps to recruit, reward and retain.
- Reflects competitive market level, role, skills, experience and individual contribution.

OPERATION

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 may be set in sterling or the local currency of the country in which the director is based.

Base salaries are normally reviewed annually for the following year taking 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; and individual performance.

For benchmarking purposes, we review remuneration by reference to different comparator groups. We look at survey data from: FTSE 100 companies with significant international exposure, excluding financial services; the FTSE 20-50, excluding financial services; a broad media industry group of US companies; select UK human capital-intensive businesses; and UK and US so-called media convergence companies with a focus on media, information services and technology. These companies are of a range of sizes relative to Pearson, but the method our independent advisers, Towers Watson, use to make comparisons on remuneration takes this variation in size into account. We also look at publicly disclosed and proxy data for global media convergence comparators with a focus on media and technology. We use these companies because they represent the wider executive talent pool from which we might expect to recruit externally and the pay market to which we might be vulnerable if our remuneration was not competitive.

Base salaries are paid in cash via the regular employee payroll (monthly in the UK and every two weeks in the US) and are subject to all necessary withholdings.

No malus or clawback provisions apply to base salary.

OPPORTUNITY

Base salary increases for executive directors will not ordinarily exceed 10% per annum and will take account of the base salary increases elsewhere within the company.

The committee will retain the discretion to deliver base salary increases in excess of 10% per annum in specific individual situations including internal promotions and material changes to the business or the role.

PERFORMANCE CONDITIONS

None, although performance of both the company and the individual are taken into account when determining an appropriate level of base salary increase each year.

PERFORMANCE PERIOD

None.

Allowances and benefits

PURPOSE AND LINK TO STRATEGY

- Help to recruit and retain.
- Reflect local competitive market.

OPERATION

Allowances and benefits comprise cash allowances and non-cash benefits and *inter alia* include: travel-related benefits (comprising company car, car allowance and private use of a driver); health-related benefits (comprising health care, health assessment and gym subsidy); and risk benefits (comprising additional life cover and long-term disability insurance that are not covered by the company's retirement plans). Allowances may also include, where appropriate, location and market premium and housing allowance although no continuing director is in receipt of such allowances. Allowances and benefits received in 2013 are set out in the annual remuneration report.

Directors are also covered by the company's directors' and officers' liability insurance and an indemnity in respect of certain third-party liabilities.

Other benefits may be offered on the same terms as to other employees.

Allowances and benefits do not form part of pensionable earnings.

No malus or clawback provisions apply to allowances and benefits.

OPPORTUNITY

The provision and level of cash allowances and non-cash benefits are competitive and appropriate in the context of the local market.

The total value of cash allowances and non-cash benefits for executive directors will not ordinarily exceed 15% of base salary in any year. The committee will retain the discretion to deliver a total value of benefits in excess of 15% of base salary in specific individual situations including changes in individual circumstances such as health status, changes in the role such as relocation, increases in the cost of current benefits that are outside company control, and changes in benefits' providers.

Executive directors are also eligible to participate in savings-related share acquisition programmes in the UK, US and rest of world, which are not subject to any performance conditions, on the same terms as other employees.

PERFORMANCE CONDITIONS

None.

PERFORMANCE PERIOD

None.

Retirement benefits

PURPOSE AND LINK TO STRATEGY

- Help to recruit and retain.
- Recognise long-term commitment to the company.

OPERATION

New employees in the UK are eligible to join the Money Purchase 2003 section of the Pearson Group Pension Plan. New employees in the US are eligible to join the 401(k) plan.

Under the Money Purchase 2003 section of the Pearson Group Pension Plan in the UK, normal retirement age is 62, but, subject to company consent, retirement is currently possible from age 55 or earlier in the event of ill-health. During service, the company and the employee make contributions into a pension fund. Account balances are used to provide benefits at retirement. Pensions for a member's spouse, dependent children and/or nominated financial dependants are payable on death.

Under the 401(k) plan in the US, which is a defined contribution plan, account balances will be used to provide benefits at retirement. In the event of death before retirement, the account balances will be used to provide benefits for designated beneficiaries.

Depending on when they joined the company, directors may participate in the Final Pay section of the Pearson Group Pension Plan in the UK or the defined benefit Pearson Inc. Pension Plan in the US, both of which are closed to new members.

Under the Final Pay section of the Pearson Group Pension Plan in the UK, normal retirement age is 62, but, subject to company consent, retirement is currently possible from age 55 or earlier in the event of ill-health. During service, the employee makes a contribution of 5% of pensionable salary and the pension fund builds up based on final pensionable salary and pensionable service. The accrued pension is reduced on retirement prior to age 60. Pensions for a member's spouse, dependent children and/or nominated financial dependants are payable on death.

Report on directors' remuneration continued

Retirement benefits continued

In the US, the defined benefit Pearson Inc. Pension Plan provides a lump sum benefit that is convertible to an annuity on retirement. The lump sum benefit accrued at an age dependent percentage of capped compensation until 31 December 2001 when further benefit accruals ceased for most employees.

Employees who satisfied criteria of age and service as of 30 November 1998 continue to earn benefits under an alternative formula that provides for 1.5% of final average earnings, adjusted for US Social Security. The benefit paid to these employees is the maximum of the lump sum benefit converted to an annuity and the benefit earned under the alternative final average earnings formula.

Executive directors and other executives across the company may be entitled to additional pension benefits to take account of the cap on the amount of benefits that can be provided from the all-employee pension arrangements in the US and the UK.

Members of the Pearson Group Pension Plan who joined after May 1989 are subject to an upper limit of earnings that can be used for pension purposes, known as the earnings cap. This limit, £108,600 as at 6 April 2006, was abolished by the Finance Act 2004. However the Pearson Group Pension Plan has retained its own 'cap', which will increase annually in line with the UK Government's Index of Retail Prices (All Items). The cap was £137,400 as at 6 April 2012. As a result of the UK Government's A-Day changes effective from April 2006, UK executive directors and other members of the Pearson Group Pension Plan who are, or become, affected by the lifetime allowance or new hires who opt out of membership of the Plan may be provided with a cash supplement of normally up to 26% of salary as an alternative to further accrual of pension benefits.

No malus or clawback provisions apply to retirement benefits.

Note Effective from 6 April 2011, the annual allowance (i.e. the maximum amount of pension saving that benefits from tax relief each year) reduced from £255,000 to £50,000 and will further reduce to £40,000 from 6 April 2014. Effective 6 April 2012, the lifetime allowance (i.e. the maximum amount of pension and/or lump sum that can benefit from tax relief) reduced from £1.8m to £1.5m and will further reduce to £1.25m from 6 April 2014.

OPPORTUNITY

In the UK, company contributions for eligible employees to the Money Purchase 2003 section of the Pearson Group Pension Plan amount up to 16% of pensionable salary (double the amount of the employee contribution, which is limited according to certain age bands).

In the US, company contributions to the 401(k) plan amount to 100% of the first 3% of eligible compensation contributed by the employee and 50% of the next 3%, plus a basic annual company contribution of 1.25% of eligible compensation. Pearson Inc. Pension Plan participants who were at least age 40 at 31 December 2001 can receive an additional 0.5% to 1.5% of pay.

John Fallon is a member of the Final Pay section of the Pearson Group Pension Plan. His pension accrual rate is 1/30th of pensionable salary per annum, restricted to the plan earnings cap. Until April 2006, the company also contributed to a Funded Unapproved Retirement Benefits Scheme (FURBS) on his behalf. Since April 2006, he has received a taxable and non-pensionable cash supplement in replacement of the FURBS.

Robin Freestone is a member of the Money Purchase 2003 section of the Pearson Group Pension Plan. Company contributions are 16% of pensionable salary per annum, restricted to the plan earnings cap. Until April 2006, the company also contributed to a Funded Unapproved Retirement Benefits Scheme (FURBS) on his behalf. Since April 2006, he has received a taxable and non-pensionable cash supplement in replacement of the FURBS.

The company has no ongoing financial liabilities in respect of FURBS.

No continuing director is currently a member of the defined benefit Pearson Inc. Pension Plan.

PERFORMANCE CONDITIONS

None.

PERFORMANCE PERIOD

None.

Annual incentives

PURPOSE AND LINK TO STRATEGY

- Motivate the achievement of annual strategic goals and personal objectives.
- Provide a focus on key financial metrics.
- Reward individual contribution to the success of the company.

OPERATION

Annual incentive is delivered entirely in cash and does not form part of pensionable earnings.

Measures and performance targets are set by the committee at the start of the year with payment made after year end following the committee's assessment of performance relative to targets.

The plans are designed to incentivise and reward underlying performance and actual results are adjusted for the effect of foreign exchange and for portfolio changes (acquisitions and disposals) and other factors that the committee considers relevant in the performance year.

Annual incentive plans are discretionary. The committee reserves the right to adjust payments up or down before they are made if it believes exceptional factors warrant doing so. The committee may in exceptional circumstances make a special award where it is satisfied that the normal operation of the annual incentive does not provide an appropriate incentive or reward to participants.

The committee also reserves the right as a form of malus to adjust payments before they are made if special circumstances exist that warrant this, such as financial misstatement, individual misconduct or reputational damage to the company.

The committee also reserves, in the same special circumstances, a right to reclaim or claw back payments or awards that have already been made.

OPPORTUNITY

Annual incentives will not exceed 200% of base salary.

For the chief executive, the individual maximum incentive opportunity that will apply for 2014 is 180% of base salary (which is the same as applied for 2013).

For other executive directors and other members of the Pearson Executive, individual maximum incentive opportunities vary by individual but will be no more than 170% of base salary.

For the chief executive, other executive directors and other members of the Pearson Executive, there is normally no pay-out for performance at threshold.

No adjustment has been made to annual incentive opportunities for the cessation of the annual bonus share matching plan under which the last conditional awards were made in 2013 in respect of 2012 annual incentive.

PERFORMANCE CONDITIONS

The committee has the discretion to select the performance measures, targets and relative weightings from year to year to ensure continuing alignment with strategy and to ensure targets are sufficiently stretching.

The committee establishes a threshold below which no pay-out is achieved and a maximum at or above which the annual incentive pays out in full.

For 2014 and onwards, the funding of annual incentives will normally be related to the performance against targets for Pearson's adjusted earnings per share (or operating profit), sales, and operating cash flow. For 2014, the weightings will be 60% on adjusted earnings per share, 20% on sales and 20% on operating cash flow.

Individual annual incentive pay-outs will also take into account individual performance against personal objectives. Personal objectives are agreed with the chief executive (or, in the case of the chief executive, the chairman) and may be functional, operational, strategic and non-financial and include *inter alia* objectives relating to environmental, social and governance issues.

Details of performance measures, weightings and targets will be disclosed in the annual remuneration report for the relevant financial year if and to the extent that the committee deems them to be no longer commercially sensitive.

PERFORMANCE PERIOD

One year.

Report on directors' remuneration continued

Long-term incentives

PURPOSE AND LINK TO STRATEGY

- Help to recruit, reward and retain.
- Drive long-term earnings, share price growth and value creation.
- Align the interests of executives and shareholders.
- Encourage long-term shareholding and commitment to the company.
- Link management's long-term reward and wealth to corporate performance in a flexible way.

OPERATION

Awards of restricted shares are made on an annual basis.

Awards of restricted shares for executive directors and other members of the Pearson Executive vest on a sliding scale based on performance against stretching corporate performance targets measured at the end of the three-year performance period.

For performance-related awards for members of the Pearson Executive, performance will continue to be tested over three years and 75% of the vested shares will continue to be released at that point. However, starting with awards made in 2014, there will be a mandatory restriction on participants' ability to dispose of the 75% of the vested shares (other than to meet personal tax liabilities) for a further two years. Furthermore, participants' rights to the release of the 25% of the vested shares will be subject to continued employment over the same period.

Where shares vest, participants also receive additional shares representing the gross value of dividends that would have been paid on these shares during the performance period and reinvested.

The plan permits awards of restricted shares to be made that are not subject to performance conditions to satisfy reward and retention objectives. However, other than in exceptional circumstances on recruitment, it is the company's normal policy not to award restricted shares to executive directors and other members of the Pearson Executive without performance conditions.

The long-term incentive plan also provides for the grant of stock options. Whilst it is not the committee's intention to grant stock options in 2014 or the foreseeable future, the committee believes that it should retain the flexibility of granting stock options in addition to, or instead of, restricted stock awards in the right circumstances. Any decision by the committee to grant stock options in the future would take account of best practice prevailing at the time. The committee would consult with shareholders before granting stock options to executive directors.

An option granted under the stock option element may not generally be exercised until a time specified when the option is granted. The date on which options would become exercisable would be set by the committee. Options may not be exercised later than the tenth anniversary of grant. Any options granted to executive directors would vest only if stretching performance conditions are achieved over a three-year minimum vesting period. Any options would vest on a sliding scale based on performance over the period. There will be no re-testing.

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

The committee reserves the right to adjust pay-outs up or down before they are released taking into account exceptional factors that distort underlying business performance or if it believes exceptional factors warrant doing so. In making such adjustments, the committee is guided by the principle of aligning shareholder and management interests.

The committee also reserves the right as a form of malus to adjust pay-outs before they are released if exceptional circumstances exist that warrant this, such as financial misstatement, individual misconduct or reputational damage to the company.

The committee also reserves, in the same special circumstances, a right to reclaim or claw back pay-outs or awards that have already been released.

OPPORTUNITY

We set the level of individual awards by taking into account:

- the face value of individual awards at the time of grant, assuming that performance targets are met in full;
- market practice for comparable companies and market assessments of total remuneration from our independent advisers;
- individual roles and responsibilities; and
- company and individual performance.

Restricted share awards to executive directors may normally be made up to a maximum face value of 400% of base salary. Awards in excess of 400% of base salary may be made in exceptional circumstances, for example, for retention purposes or to reflect particular business situations.

OVERVIEW
OUR PERFORMANCE
RESPONSIBLE BUSINESS
GOVERNANCE
FINANCIAL STATEMENTS

The reasons for any such exceptional awards will be disclosed in the annual report for the year in which they are made.

The value of awards at pay-out is subject to the extent to which performance and any other conditions are met and the share price at the time of vesting. The proportion of the award that vests at threshold level of performance may vary by performance condition.

Whilst it is not the committee's intention to grant stock options in 2014 or the foreseeable future, the maximum value of stock option awards would be the equivalent expected value of the maximum restricted share awards set out above, based on an independent assessment of their net present value taking into account all the conditions.

For 2014, we will set the level of individual restricted share awards consistent with those seen in recent years and within the policy maximum taking into account the factors set out above.

No adjustment has been made to long-term incentive opportunities for the cessation of the annual bonus share matching plan under which the last conditional awards were made in 2013 in respect of 2012 annual incentive.

PERFORMANCE CONDITIONS

The committee will determine the performance measures, weightings and targets governing an award of restricted shares prior to grant to ensure continuing alignment with strategy and to ensure that targets are sufficiently stretching.

The committee establishes a threshold below which no pay-out is achieved and a maximum at or above which the award pays out in full.

For 2014 and onwards, awards will normally be subject to the achievement of targets for growth in earnings per share, return on invested capital and relative total shareholder return. For 2014, to emphasise the importance of earnings growth and to reward the delivery of the desired outcomes from the strategic effort, the weighting of the performance metrics within the Pearson long-term incentive plan will be changed from one-third on each measure to half on earnings per share growth, one-third on return on invested capital (no change) and one-sixth on relative total shareholder return.

We will set targets for the 2014 awards that are consistent with the company's strategic objectives over the period to 2016. Full details of the performance measures, weightings and targets for 2014 and the proportion of the award payable at threshold will be set out in the annual remuneration report for 2014.

As with restricted shares, the committee will determine the performance conditions that apply to any awards of stock options prior to grant. The intention would be that these conditions would be the same as apply to restricted shares.

Total shareholder return (TSR) is the return to shareholders from any growth in Pearson's share price and reinvested dividends over the performance period. For long-term incentive awards, TSR is measured relative to the constituents of the FTSE World Media Index over a three-year period. Companies that drop out of the index are normally excluded i.e. only companies in the index for the entire period are counted. Share price is averaged over three months at the start and end of the performance period. Dividends are treated as reinvested on the ex-dividend date, in line with the *Datastream* methodology. The vesting of shares based on relative TSR is subject to the committee satisfying itself that the recorded TSR is a genuine reflection of the underlying financial performance of the business.

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

Adjusted earnings per share (EPS) is calculated by dividing the adjusted earnings attributable to equity shareholders of the company by the weighted average number of ordinary shares in issue during the year, excluding any ordinary shares purchased by the company and held in trust (see note 8 of the financial statements for a detailed description of adjusted earnings per share). EPS growth is calculated using the point-to-point method. This method compares the adjusted EPS in the company's accounts for the financial year ended prior to the grant date with the adjusted EPS for the financial year ending three years later and calculates the implicit compound annual growth rate over the period.

PERFORMANCE PERIOD

Three years.

Report on directors' remuneration continued

Selection of performance measures and target setting

In the selection and weighting of performance measures for the annual and long-term incentive awards the committee takes into account Pearson's strategic objectives and short- and long-term business priorities.

In the case of annual incentives, the committee chose sales, earnings per share or operating profit, and operating cash flow as being relevant measures of Pearson's performance against its short-term strategic objectives and business priorities.

In the case of long-term incentives, the committee chose earnings per share growth in order to reward the delivery of the desired outcomes from the strategic effort and because strong bottom-line growth is imperative if we are to improve our total shareholder return and our return on invested capital. We chose return on invested capital because, over the past few years, the transformation of Pearson has significantly increased the capital invested in the business (mostly in the form of goodwill associated with acquisitions) and required substantial cash investment to integrate those acquisitions. We chose total shareholder return relative to the constituents of the FTSE World Media Index because, in line with many of our shareholders, we felt that part of executive directors' rewards should be linked to performance relative to the company's peers.

The performance ranges chosen set a careful balance between upside opportunity and downside risk and are normally based on targets in accordance with the company's operating and strategic plans.

Legacy arrangements under the annual bonus share matching plan

Up to and including 2013 in respect of annual incentives for 2012, awards were made under the annual bonus share matching plan. This plan encouraged executive directors and other senior managers to acquire and hold Pearson shares and aligned the interests of executives and shareholders. Senior managers across the company were invited to invest up to 50% of their after-tax annual incentive in Pearson shares purchased in the market and hold these shares for three years, in return for the opportunity to earn additional free matching shares and dividend shares, depending on performance against a real growth in earnings per share performance condition. Where matching shares vest, participants also receive additional shares representing the gross value of dividends that would have been paid on the matching shares during the performance period and reinvested. The maximum matching award is equal to the number of shares that could have been acquired with the amount of pre-tax annual bonus invested in Pearson shares (i.e. one matching share for every one invested share, grossed up for tax).

Remuneration policy for other employees

The approach to remuneration for the broader employee population varies by level and geography, but is broadly consistent with that of directors:

- The approach to setting base salary increases elsewhere in the company takes into account economic factors, competitive market rates, roles, skills, experience and individual performance.
- Allowances and benefits for employees reflect the local labour market in which they are based.
- As part of their overall retirement arrangements, executive directors participate in the same underlying pension arrangements that have been set up for Pearson employees in the US and the UK.
- Many employees participate in some form of cash-based annual incentive, bonus, profit-share or sales commission plan. Annual incentive plans for the Pearson Executive form the basis of the annual incentive plans below the level of the principal operating companies and establish performance measures and standards and set the ceiling for individual incentive opportunities.
- Approximately 5% of the company's employees below the Pearson Executive – selected on the basis of their role, performance and potential – currently hold time-vesting shares under the long-term incentive plan.
- All 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.

Pay and performance scenario analysis

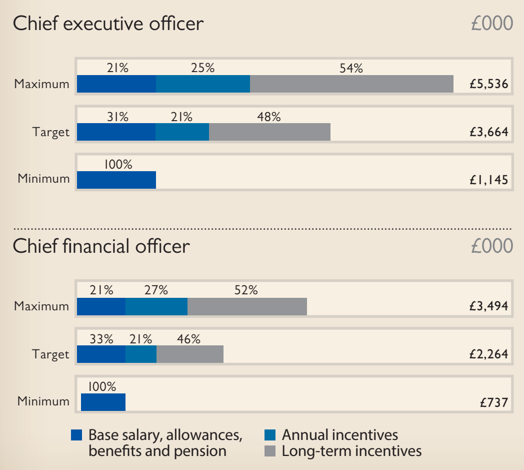
Consistent with its policy, the committee places considerable emphasis on the performance-linked elements i.e. annual and long-term incentives.

The chart overleaf shows what each director could expect to receive in 2014 under different performance scenarios, based on the following definitions of performance:

PERFORMANCE SCENARIO	ELEMENTS OF REMUNERATION AND ASSUMPTIONS
Maximum	2014 base salary; allowances, benefits, and retirement benefits at the same percentage of base salary as in 2013; maximum individual annual incentive as per policy; maximum value of 2013 long-term incentive award
Target	2014 base salary; allowances, benefits, and retirement benefits at the same percentage of base salary as in 2013; target individual annual incentive as per policy; target value of 2013 long-term incentive award (Towers Watson's independent assessment of the expected value of the award i.e. the net present value taking into account all the conditions)
Minimum	2014 base salary; allowances, benefits, and retirement benefits at the same percentage of base salary as in 2013; no annual or long-term incentives

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

On this basis, the relative weighting of fixed and performance-related remuneration and the absolute size of the remuneration packages for the chief executive and the chief financial officer are as follows:



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

Recruitment

The committee expects any new executive directors to be engaged on terms that are consistent with the general remuneration principles outlined in this policy. In particular, the company's policy is that regular variable remuneration would normally be awarded within the same parameters and subject to the same performance conditions as for the current executive directors outlined in the policy, save that the committee may provide that in exceptional circumstances an annual or long-term incentive award may be subject to a requirement of continued service over a specified period or some other specified requirement, rather than a corporate performance condition. The terms of any such exceptional award will be disclosed in the relevant subsequent annual remuneration report.

The committee recognises that it cannot always predict accurately the circumstances in which any new directors may be recruited. The committee may determine that it is in the interests of the company and shareholders to secure the services of a particular individual which may require the committee to take account of the terms of that individual's existing employment and/or their personal circumstances. Examples of circumstances in which the committee expects it might need to do this are:

- where an existing employee of the company is promoted to the board, in which case the company will honour all existing contractual commitments including any outstanding share awards, benefit and pension entitlements;
- where an individual is relocating in order to take up the role in which case the company may provide certain benefits such as reasonable relocation expenses, accommodation for a short period following appointment and assistance with visa applications or other immigration issues and ongoing arrangements such as tax equalisation, annual flights home, and housing allowance;
- where an individual would be forfeiting valuable variable remuneration in order to join the company, in which case the committee may award appropriate compensation. The committee would require reasonable evidence of the nature and value of any forfeited award and would, to the extent practicable, ensure any compensation was provided on a like-for-like basis and was no more valuable than the forfeited award.

In light of the various legacy pension arrangements enjoyed by the incumbent executive directors, in determining the pension arrangements for any new recruit, the committee expects to offer a defined contribution arrangement with company contributions not exceeding those set out on page 84 but would

Report on directors' remuneration continued

have regard to the recruit's existing arrangements, the market norms in the home country and the existing pension vehicles available within the company.

In making any decision on any aspect of the remuneration package for a new recruit, the committee would balance shareholder expectations, current best practice and the requirements of any new recruit and would strive not to pay more than is necessary to achieve the recruitment. The committee would give full details of the terms of the package of any new recruit in the next annual remuneration report.

Pearson expects any new chairman or non-executive director to be engaged on terms that are consistent with the general remuneration principles outlined in the relevant sections of this policy. However, in the case of the chairman, the committee may consider it appropriate to offer a remuneration package that differs from that of the existing incumbent if that is necessary to attract the most capable candidate or to reflect the individual's expected duties.

Service contracts and termination provisions

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

There are no special provisions for notice or compensation in the event of a change of control of Pearson.

It is the company's policy that the company may terminate the chairman's and executive directors' service agreements by giving no more than 12 months' notice.

As an alternative, for executive directors the company may at its discretion pay in lieu of that notice. Payment-in-lieu of notice may be made in equal monthly instalments from the date of termination to the end of any unexpired notice period. In the case of the CEO, payment-in-lieu of notice in instalments may also be subject to mitigation and reduced taking into account earnings from alternative employment.

For executive directors, pay in lieu of notice comprises 100% of the annual salary at the date of termination and the annual cost to the company of providing pension and all other benefits. For the chairman, pay in lieu of notice comprises 100% of the annual fees at the date of termination. In limited circumstances, in addition to making a full payment in lieu of notice, the company may permit an executive director to stay employed after the announcement of his or her departure for a limited period to ensure an effective hand-over and/or allow time for a successor to be appointed.

The company may, depending on the circumstances of the termination, determine that it will not pay the director in lieu of notice and may instead terminate a director's contract in breach and make a damages payment, taking into account as appropriate the director's ability to mitigate his or her loss.

On cessation of employment, save as otherwise provided for under the rules of Pearson's discretionary share plans, executive directors' entitlements to any unvested awards lapse automatically. In the case of injury, disability, ill-health or redundancy (as determined by the committee), where a participant's employing company ceases to be part of Pearson, or any other reason if the committee so decides in its absolute discretion:

- awards that are subject to performance conditions will stay in force as if the participant had not ceased employment and shall vest on the original vesting date;
- awards that are not subject to a performance condition will be released as soon as practicable following cessation of employment;
- the number of shares that are released shall be prorated for the period of the participant's service in the restricted period (although the committee may in its absolute discretion waive or vary the prorating).

In determining whether and how to exercise its discretion under Pearson's discretionary share plans, the committee will have regard to all relevant circumstances distinguishing between different types of leaver, the circumstances at the time the award was originally made, the director's performance and the circumstances in which the director left employment.

On cessation of employment, executive directors, having been notified of participation in an annual incentive plan for the relevant financial year, may, at the committee's discretion, retain entitlement to a pro rata annual incentive for their period of service in the financial year prior to their leaving date. Such pay-out will normally be calculated in good faith on the same terms and paid at the same time as for continuing executive directors.

Eligibility for allowances and benefits including retirement benefits normally ceases on retirement or on the termination of employment for any other reason.

Details of each individual's service agreement are outlined in the table overleaf. Employment agreements for other employees are determined according to local labour law and market practice.

Individual service agreements

POSITION	DATE OF AGREEMENT	NOTICE PERIODS	COMPENSATION ON TERMINATION OF EMPLOYMENT BY THE COMPANY WITHOUT NOTICE OR CAUSE
Chairman	29 July 2005	12 months from the director; 12 months from the company	Payment-in-lieu of notice of 100% of annual fees at the date of termination
Executive directors	31 December 2012 (John Fallon) 17 December 2012 (Robin Freestone)	Six months from the director; 12 months from the company	Payment-in-lieu of notice of 100% of annual salary at the date of termination and the annual cost of pension and all other benefits

Note Under pay-in-lieu of notice, the annual cost of pension for executive directors is normally calculated as the sum, where applicable, of: an amount equal to the company's cost of providing the executive's pension under the pension plan based on the Future Service Company Contribution Rate for the relevant section of the pension plan as stated in the most recent actuarial valuation (as at the date of termination of employment) as limited by the earnings cap; and any cash allowance in lieu of pension or to take account of fact that pension benefits and life assurance cover are restricted by the earnings cap.

Executive directors' non-executive directorships

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

Employment conditions

In accordance with the committee's charter and terms of reference, the committee's remit does not include remuneration matters below that of the chief executive, the other executive directors and other members of the Pearson Executive. However, before the remuneration packages for the Pearson Executive are set for the year ahead, the committee considers a report from the chief executive and chief human resources officer on general pay trends in the market and the level of pay increases across the company as a whole. This helps to ensure that executive remuneration packages are reviewed in the context of the wider organisation.

The company consults with various employee representative bodies – including trade unions and works councils in some jurisdictions – about the company's strategy, competitiveness and performance of the business and other matters affecting employees. The company also conducts an employee engagement survey to find out how people feel about working for Pearson, what they think about the work they do, the opportunities they have and the rewards they get (including a section on pay and benefits). The company uses all of this feedback to inform decisions on people-related activities, resources and investment, local management action plans and wider business unit and organisational strategies.

It is the company's intention to continue to engage with employees and employee representatives in this way in the future.

The committee has not consulted directly with employees on the setting of the directors' remuneration policy.

Shareholder views

The company consults regularly with shareholders on all matters affecting its strategy and business operations. As part of that process, we also engage with shareholders on matters relating to executive remuneration.

The committee continues to be aware of and respond to best practice guidelines of shareholders and their representative bodies.

The committee actively consulted with the company's major shareholders and their representative bodies on the directors' remuneration policy set out in this report. The consultation provided some valuable feedback relating to remuneration policy, company performance and business strategy. Specifically, shareholders commented on the operation of the long-term incentive plan, the use of flexibility and discretion, and the policy on recruitment. They supported the committee's proposals on deferral/holding periods for vested shares and shareholding guidelines. And, on incentive pay-outs, they requested clarification of our arrangements for adjustments for malus and the strengthening of our clawback provisions.

These matters have been addressed in this policy report.

Report on directors' remuneration continued

Future policy table for chairman's and non-executive directors' remuneration

The table below summarises policy with respect to the remuneration of the chairman and non-executive directors:

PURPOSE AND LINK TO STRATEGY

To attract and retain high calibre individuals, with appropriate experience or industry relevant skills, by offering market competitive fee levels.

OPERATION

The chairman is paid a single fee for all of his responsibilities.

The chairman's fee is set at a level that is competitive with those of chairmen in similar positions in comparable companies. The chairman is not entitled to any annual or long-term incentive, retirement or other employee benefits.

The non-executive directors are paid a basic fee. The chairmen and members of the main board committees and the senior independent director are paid an additional fee to reflect their extra responsibilities.

The chairman and the non-executive directors are covered by the company's normal arrangements for directors' and officers' liability insurance and an indemnity in respect of certain third-party liabilities.

The company reimburses the chairman's and non-executive directors' travel and other business expenses and any tax incurred thereon, if applicable.

A minimum of 25% of the basic non-executive directors' fee is paid in Pearson shares that the non-executive directors have committed to retain for the period of their directorships. Shares are acquired quarterly at the prevailing market price with the individual after-tax fee payments.

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

Non-executive directors serve Pearson under letters of appointment which are renewed annually and do not have service contracts. For non-executive directors, there is no notice period or entitlement to compensation on the termination of their directorships.

OPPORTUNITY

The chairman's fees were last reviewed in 2010 and increased with effect from 1 April 2011 with a commitment to review again in 2014. Fees for the non-executive directors were last increased with effect from 1 July 2010.

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

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

The maximum opportunity per director depends on individual duties or combination of duties in accordance with this structure. The total fees payable to the non-executive directors are subject to the limit set out in the Articles of Association of the company (currently £750,000) and as increased by ordinary resolution from time to time.

The fees for the chairman remains unchanged at £500,000 per year.

PERFORMANCE CONDITIONS

None.

PERFORMANCE PERIOD

None.

Annual remuneration report

The remuneration committee presents the annual remuneration report, which will be put to shareholders as an advisory (non-binding) vote at the Annual General Meeting to be held on 25 April 2014.

This report comprises of a number of sections:

- The remuneration committee and its activities
- Voting outcome at 2013 AGM
- Single figure of total remuneration and prior year comparison
- Detail of executive remuneration for 2013
- Detail of long-term share interests including awards made in 2013
- Payments to former directors
- Payments for loss of office
- Interests of directors and value of shareholdings
- Executive directors' non-executive directorships
- Historical performance and remuneration
- Comparative information
- Information on changes to remuneration for 2014.

Report on directors' remuneration continued

The remuneration committee and its activities

Composition

David Arculus chaired the remuneration committee for the year 2013; the other members were Vivienne Cox, Ken Hydon, Joshua Lewis and Glen Moreno. David Arculus, Vivienne Cox, Ken Hydon and Joshua Lewis are independent non-executive directors. Glen Moreno, chairman of the board, is a member of the committee as permitted under the UK Corporate Governance Code.

Internal advisers to the committee

John Fallon, chief executive, Robin Freestone, chief financial officer, Robin Baliszewski, formerly director for people, Melinda Wolfe, chief human resources officer from October 2013, Robert Head, director for executive reward, and Stephen Jones, SVP company secretarial, provided material assistance to the committee during the year. They attended meetings of the committee, although none of them was involved in any decisions relating to his or her own remuneration.

External advisers to the committee

To ensure that the committee receives independent advice, Towers Watson supplies survey data and advises on market trends, long-term incentives and other general remuneration matters. Towers Watson was selected and appointed by the committee through a formal tendering process. Towers Watson also advised the company on health and welfare benefits in the US and provided consulting advice directly to certain Pearson operating companies. Towers Watson is a member of the Remuneration Consultants' Group, the body which oversees the code of conduct in relation to executive remuneration consulting in the UK. During the year, Towers Watson was paid fees for advice to the committee, which were charged on a time spent basis, of £89,129. As part of its annual review of its performance and effectiveness, the committee remains satisfied that Towers Watson's advice was objective and independent and that Towers Watson's provision of other services in no way compromises its independence.

Responsibility

The committee's principal duties are to:

› determine and regularly review the remuneration policy for the executive directors, the presidents of the principal geographic markets and lines of business and other members of the Pearson Executive who report directly to the CEO (Executive Management). This policy includes base salary, annual and long-term incentives, pension arrangements, any other benefits and termination of employment
› regularly review the implementation and operation of the remuneration policy for Executive Management and approve the individual remuneration and benefits packages of the executive directors.

The committee's duties are also to:

› approve the design of, and determine targets for, any performance-related pay plans operated by the company and approve the total payments to be made under such plans
› review the design of the company's long-term incentive and other share plans for approval by the board and shareholders
› advise and decide on general and specific arrangements in connection with the termination of employment of executive directors
› review and approve corporate goals and objectives relevant to CEO remuneration and evaluate the CEO's performance in light of those goals and objectives
› have delegated responsibility for determining the remuneration and benefits package of the chairman of the board
› appoint and set the terms of engagement for any remuneration consultants who advise the committee and monitor the cost of such advice.

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

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

The committee participated in a survey to review its performance and effectiveness in July 2013, looking at areas such as the clarity of roles and responsibilities, the composition of the committee, the use of time, the quality and timeliness of meeting materials, the opportunity for discussion and debate, dialogue with management and access to independent advice.

The committee concluded that it is operating effectively and noted the challenges for the year ahead.

Meetings in 2013

The committee met five times during 2013. The matters discussed and actions taken were as follows:

20 FEBRUARY 2013

- Confirmed the leaving arrangements for Rona Fairhead
- Noted the activity of the standing committee of the board in relation to the operation of the company's equity-based reward programmes
- Noted company's use of equity for employee share plans
- Noted Towers Watson's overview of the current remuneration environment
- Reviewed and approved 2012 annual incentive plan pay-outs
- Reviewed and approved provisional 2010 long-term incentive plan pay-outs
- Approved vesting of 2010 annual bonus share matching awards and release of shares
- Reviewed and approved increases in base salaries for 2013 for the Pearson management committee (now called the Pearson Executive)
- Reviewed 2013 Pearson and operating company annual incentive plan targets
- Reviewed and approved 2013 individual annual incentive opportunities for the Pearson management committee
- Reviewed 2013 long-term incentive awards and associated performance conditions for the Pearson management committee
- Reviewed and noted total remuneration for members of the Pearson management committee for 2012 and 2013
- Reviewed and approved the 2012 report on directors' remuneration
- Reviewed and approved the 2012 annual incentive pay-out for Marjorie Scardino
- Reviewed and approved the 2012 annual incentive pay-out and 2013 remuneration package for John Fallon.

24 APRIL 2013

- Noted the activity of the standing committee of the board in relation to the operation of the company's equity-based reward programmes
- Confirmed 2010 long-term incentive plan pay-outs including element relating to relative shareholder return performance and release of shares
- Confirmed 2013 Pearson and operating company annual incentive plan targets
- Confirmed 2013 long-term incentive awards and associated performance conditions for the Pearson management committee
- Noted feedback on the 2012 report on directors' remuneration
- Discussed new executive remuneration reporting requirements.

24 JULY 2013

- Reviewed the committee's charter and terms of reference
- Discussed 2013 AGM season and shareholder voting
- Noted remuneration packages for a number of internal appointments and one new hire to the Pearson Executive
- Noted John Makinson's remuneration package and contract on secondment to, and appointment as chairman of, Penguin Random House
- Noted Will Ethridge's intention to stand down from the Pearson board and the arrangements for his 2014 employment and retirement
- Noted implications of new executive remuneration reporting requirements and commenced review of executive remuneration policy.

Report on directors' remuneration continued

2 OCTOBER 2013

- Noted the activity of the standing committee of the board in relation to the operation of the company's equity-based reward programmes
- Reviewed the committee's charter and terms of reference
- Reviewed the committee's performance and effectiveness
- Reviewed the status of outstanding long-term incentive awards
- Ratified 2013 long-term incentive awards and associated performance conditions for new appointees to the Pearson Executive
- Considered the approach to 2013 annual incentives in light of company's restructuring plans
- Noted the company's strategy for 2013 long-term incentive awards for executives and managers below the Pearson Executive
- Considered the approach to annual incentives in the light of the company's global education strategy and new organisation
- Continued the review of executive remuneration policy
- Noted the remuneration packages for two new hires to the Pearson Executive.

5 DECEMBER 2013

- Noted the activity of the standing committee of the board in relation to the operation of the company's equity-based reward programmes
- Reviewed and approved the committee's charter and terms of reference
- Discussed Towers Watson's overview of the current remuneration environment and approach to executive pay benchmarking for 2013/2014
- Reviewed the status of outstanding long-term incentive awards
- Considered the approach to annual incentives in the light of the company's global education strategy and new organisation
- Reviewed long-term incentive plan design and operation
- Reviewed the programmes and policies related to equity participation of executives
- Noted the draft format for the 2013 directors' remuneration report.

Voting outcome at 2013 AGM

The following table summarises the details of votes cast in respect of the resolution to approve the directors' remuneration report at the 2013 AGM.

Votes for	Votes against	Total votes cast	Votes withheld (abstentions)
523,204,046	35,545,800	558,749,846	14,082,005
93.64% of votes cast	6.36% of votes cast	68.35% of issued share capital	

While the committee was pleased with the level of support shown by shareholders in respect of this resolution, consideration was given to those shareholders that did not vote in favour of the directors' remuneration report. Through consultation, the committee received feedback from three institutional shareholders who between them accounted for one-third of the votes against to understand better why these shareholders voted against the resolution. The committee subsequently discussed this at their July 2013 meeting. In the light of the feedback, the committee concluded at that time that, notwithstanding any issues arising out of its regular review of executive remuneration policy, there was nothing fundamental or structural within our existing arrangements to cause particular concern to shareholders.

As in previous years and required by law, details of the voting on all resolutions at the 2014 AGM will be announced via the RNS and posted on the Pearson website following the AGM.

http://www.pearson.com/content/dam/pearson-corporate/files/press-releases/2013/20130426_AGM_Poll_Results.pdf

Single total figure of remuneration and prior year comparison

Executive directors

The remuneration received by executive directors in respect of the financial years ending 31 December 2013 and 31 December 2012 was as follows:

Executive director £000s		Base salary	Allowances and benefits	Annual incentive	Retirement benefits	Long-term incentives	Total
Current directors							
John Fallon	2013	750	43	463	330	141	1,727
	2012	146	7	63	61	221	498
Robin Freestone	2013	545	14	341	163	181	1,244
	2012	500	22	252	144	1,121	2,039
Former directors							
Will Ethridge	2013	681	7	227	247	177	1,339
	2012	658	2	293	300	1,135	2,388
Rona Fairhead (stepped down 26 April 2013)	2013	176	14	–	110	47	347
	2012	529	50	192	242	769	1,782
John Makinson (stepped down 1 July 2013)	2013	274	122	301	298	69	1,064
	2012	549	244	238	–	741	1,772
Total	2013	2,426	200	1,332	1,148	615	5,721
	2012	2,382	325	1,038	747	3,987	8,479

Note 1 John Fallon was appointed to the board on 3 October 2012. For the full year for 2012, John Fallon's remuneration reflected nine months in his role as CEO, Pearson International and three months as Pearson CEO designate and was: salary/fees – £506; allowances and benefits £29; annual incentive – £259; retirement benefits – £249; long-term incentives – £909; total – £1,952 (all figures in £000s).

Note 2 In accordance with the regulations, we show a single total figure of remuneration, which includes retirement benefits and long-term incentives in addition to the other elements of remuneration that have been shown in previous reports.

Note 3 Where necessary, the figures for allowances and benefits, long-term incentives and retirement benefits for 2012 have been restated to reflect the revised requirements and valuation methodology.

Note 4 In 2012, the accrued pension over the period for John Makinson decreased because of a transfer made as a result of a pension sharing order.

Note 5 The single figure of remuneration for 2013 includes all awards that were subject to a performance condition where the performance period ended, or was substantially (but not fully) completed, at 31 December 2013 and awards where the performance condition has been satisfied but where the release of shares is subject to a further holding period. The same methodology has been applied for earlier periods and the single figure for earlier reporting periods has been restated where necessary.

Further explanatory details/notes are included in the tables that follow.

Report on directors' remuneration continued

Chairman and non-executive directors

The remuneration paid to the chairman and non-executive directors in respect of the financial years ending 31 December 2013 and 31 December 2012 was as follows:

Director £000s		Salary/ basic fee	Committee chairmanship	Committee membership	Senior independent directorship	Total
Glen Moreno	2013	500	–	–	–	500
	2012	500	–	–	–	500
David Arculus	2013	65	20	10	–	95
	2012	65	20	10	–	95
Vivienne Cox	2013	65	–	15	20	100
	2012	65	–	15	–	80
Ken Hydon	2013	65	25	5	–	95
	2012	65	25	5	–	95
Josh Lewis	2013	65	–	13		78
	2012	65	–	10	–	75
Linda Lorimer (appointed 1 July 2013)	2013	33		–	–	33
	2012	–	–	–	–	–
Harish Manwani (appointed 1 October 2013)	2013	16	–	–	–	16
	2012	–	–	–	–	–
Susan Fuhrman (stepped down 7 August 2013)	2013	39	–	6	–	45
	2012	65	–	10	–	75
Total	2013	848	45	49	20	962
	2012	825	45	50		920

Total aggregate emoluments for executive and non-executive directors were £5.3m in 2013. These emoluments are included with total employee benefit expense in note 5 to the financial statements (page 142).

Detail of executive remuneration for 2013

In this sub-section, we summarise or provide details of each element of remuneration set out in the single figure table as required (page 97).

Base salaries

In accordance with policy, the committee considered a report from the chief executive and chief human resources officer on general pay trends in the market and the level of pay increases across the company as a whole. For 2013, the company had reiterated its starting principles that base compensation provides the appropriate rate of remuneration for the job, taking into account relevant recruitment markets, business sectors and geographic regions and that total remuneration should reward both short- and long-term results, delivering competitive rewards for target performance, but higher rewards for exceptional company performance. For the US and UK, the budget guideline issued at the end of September 2012 for adjustments to base pay for 2013 was 2% although business units were given the flexibility to take into account factors such as their own performance, where they are in the business cycle, and specific market factors. As the year closed and pay budgets for 2013 were confirmed, most businesses remained on an overall 2% salary increase pool. Local inflation rates were taken into account in particular markets.

The increases for the executive directors who served during all or part of 2013 were as follows:

	John Fallon	Robin Freestone	Will Ethridge	Rona Fairhead (stepped down 26 April 2013)	John Makinson (stepped down 1 July 2013)
Base salary at 31 December 2012	£600,000	£500,000	$1,045,500	£529,100	£548,900
Increase	£150,000	£45,000	$20,900	–	–
	25%	9%	2%	–	–
Base salary at 1 January 2013	£750,000	£545,000	$1,066,400	£529,100	£548,900

Note John Fallon was appointed to the board on 3 October 2012 and his base salary was reviewed on his appointment to CEO on 1 January 2013.

Allowances and benefits

During the year the executive directors received a number of benefits as summarised below.

Allowance/benefit £	John Fallon	Robin Freestone	Will Ethridge	Rona Fairhead (stepped down 26 April 2013)	John Makinson (stepped down 1 July 2013)
Location and market premium	–	–	–	–	105,469
Travel	15,387	12,037	–	5,530	6,865
Health	2,405	1,988	5,720	663	1,132
Risk	24,765	253	1,673	8,074	8,605
Total	42,557	14,278	7,393	14,267	122,071

Note 1 Travel benefits comprise company car, car allowance and private use of a driver. Health benefits comprise healthcare, health assessment and gym subsidy. Risk benefits comprise additional life cover and long-term disability insurance.

Note 2 Allowance and benefits for Will Ethridge include US health benefits. Such benefits are self-insured and the value shown here is the fully insured equivalent. There is no employee tax on this value.

Note 3 In addition to the above benefits and allowances that are included in the single figure, the executive directors may also participate in company benefit or policy arrangements that have no taxable value.

Note 4 Additional life cover and long-term disability insurance not covered by the retirement plans were previously reported as 'other pension-related benefit costs' and included in retirement benefits in the 2012 directors' remuneration report.

Report on directors' remuneration continued

Annual incentive

For 2013, annual incentive opportunities were based on the following performance measures and performance against these measures (designated as: – below threshold, < between threshold and target, > between target and maximum and + above maximum) was as follows:

Name	Maximum opportunity (% of salary)	Weighting of performance measures (% of maximum opportunity): Pearson	Operating company	Personal	Performance in 2013 – Pearson: Sales 20%	Underlying growth in adjusted EPS (pre-restructuring) 25%	Underlying growth in adjusted EPS (post-restructuring) 25%	Average working capital to sales ratio 10%	Operating cash flow 20%	Weighted pay-out (% of maximum)	Operating company: Sales 30%	Operating profit (pre-restructuring) 20%	Operating profit (post-restructuring) 20%	Average working capital to sales ratio 10%	Operating cash flow 20%	Weighted pay-out (% of maximum)	Pay-out for 2013 (% of salary)	(£000)
John Fallon	180%	90%	–	10%	<	>	<	–	–	28.1%	–	–	–	–	–	–	61.8%	463
Robin Freestone	170%	80%	–	20%	<	>	<	–	–	26.0%	–	–	–	–	–	–	62.5%	341
Will Ethridge	175%	30%	60% Pearson North America	10%	<	>	<	–	–	26.0%	<	–	–	–	–	10.5%	33.4%	227
John Makinson (stepped down 1 July 2013	160%	30%	60% Penguin Group	10%	<	>	<	–	–	26.0%	>		>	>	+	91.4%	109.8%	301

Note 1 For all plans, Pearson's reported financial results for the relevant period were used to measure performance. In order to incentivise and reward underlying performance, actual results are adjusted for the effect of foreign exchange and for portfolio changes (acquisitions and disposals) and other factors that the committee considers relevant in the performance year. No discretion has been exercised to adjust the resulting underlying pay-outs.

Note 2 Rona Fairhead, who left the company on 30 April 2013, was not eligible for an annual incentive in respect of her service in 2013.

Note 3 Details of performance targets and performance against those targets are not disclosed as the committee deems them to be commercially sensitive.

Retirement benefits

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

Directors' pensions	Plans	Normal retirement age	Accrued pension at 31 Dec 13 £000[1]	Value of defined benefit pension over the period £000[2]	Other pension costs to the company over the period £000[3]	Other allowances in lieu of pension £000[4]	Total annual value in 2013 £000[5]
John Fallon	Pearson Group Pension Plan. Accrual rate of 1/30th of pensionable salary per annum. Taxable and non-pensionable cash supplement	62	74.0	134.8	–	194.7	330
Robin Freestone	Money Purchase 2003 section of the Pearson Group Pension Plan. Taxable and non-pensionable cash supplement	62	–	–	22.0	141.4	163
Will Ethridge	Pearson Inc. Pension Plan and the approved 401(k) plan. Non-qualified Excess Plan	65	227.5	215.2	31.6	–	247
Rona Fairhead	Pearson Group Pension Plan. Accrual rate of 1/30th of pensionable salary per annum. Taxable and non-pensionable cash supplement	62	53.1	65.4	–	44.6	110
John Makinson	Pearson Group Pension Plan. Unfunded Unapproved Retirement Benefits Scheme	62	241.1	298	–	–	298

Note 1 The accrued pension at 31 December 2013 is the deferred pension to which the member would be entitled on ceasing pensionable service on 31 December 2013. For Will Ethridge this is his pension from the US plan and the US SERP. For John Fallon and Rona Fairhead it relates to the pension payable from the UK plan. For John Makinson it relates to the pension from the UK Plan and his unapproved arrangements in aggregate. Robin Freestone does not accrue defined benefits.

Note 2 This column comprises the increase in the directors' accrued pension over the period (net of inflation) multiplied by 20 and from which the directors' contributions are deducted.

Note 3 This column comprises contributions to defined contribution arrangements for UK benefits. For US benefits, it includes company contributions to funded defined contribution plans.

Note 4 This column represents the cash allowances paid in lieu of the previous FURBS arrangements for John Fallon, Robin Freestone and Rona Fairhead. John Makinson's deferred FURBS entitlement is referred to in note 1 above.

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

Note 6 Additional life cover and long-term disability insurance not covered by the retirement plans were previously reported as 'other pension-related benefit costs' and included in retirement benefits in the 2012 directors' remuneration report and are now included as 'allowances and benefits'.

Note 7 There are no additional benefits or special arrangements under the retirement plans for directors who retire before their normal retirement date.

Report on directors' remuneration continued

Details of long-term share interests including awards made in 2013

Long-term incentives

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

Date of award	Share price on date of award	Vesting	Real compound annual EPS growth	Status of award
15/05/13	1,206.0p	15/05/16	–	Outstanding subject to 2012 to 2015 performance
15/05/12	1,152.0p	15/05/15	–	Outstanding subject to 2011 to 2014 performance
20/04/11	1,129.0p	20/04/14	-6.6%	Performance condition not met. Matching share award lapsed
21/04/10	1,024.1p	21/04/13	4.4%	Target met for release of 84.5% of matching share award as reported in report on directors' remuneration for 2012. Shares released on 21 April 2013

The pay-out to performance vesting scale for all awards is as follows:

Performance condition	Pay-out (% of Match)
< 3% real compound annual EPS growth	Nil
3% real compound annual EPS growth	50%
3% to 5% real compound annual EPS growth	50% to 100% sliding scale
5% real compound annual EPS growth	100%
> real 5% compound annual EPS growth	100%

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

The following directors invested part of their after-tax annual incentive in Pearson shares and received conditional matching awards under the annual bonus share matching plan on 15 May 2013 which will vest, subject to performance, on 15 May 2016 as follows:

Name	Matching shares awarded	Share price on date of award	Face value on date of award
John Fallon	6,083	1,206.0p	£73,361

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

Date of award	Share price on date of award	Vesting date	Performance measures (award split equally across three measures)	Performance period	Pay-out at threshold	Pay-out at maximum	Actual performance	% of award vested	Status of award
01/05/13	1,183.0p	01/05/16	Relative TSR	2013 to 2016	30% at median	100% at upper quartile	–	–	Outstanding
			ROIC	2015	0% for ROIC of 8.5%	100% for ROIC of 10.5%	–	–	
			EPS growth	2015 compared to 2012	30% for EPS growth of 6.0%	100% for EPS growth of 12.0%	–	–	
02/05/12	1,161.0p	02/05/15	Relative TSR	2012 to 2015	30% at median	100% at upper quartile	–	–	Outstanding
			ROIC	2014	0% for ROIC of 8.5%	100% for ROIC of 10.5%	–	–	
			EPS growth	2014 compared to 2011	30% for EPS growth of 6.0%	100% for EPS growth of 12.0%	–	–	
03/05/11	1,149.0p	03/05/14	Relative TSR	2011 to 2014	30% at median	100% at upper quartile	44th percentile	Nil	Estimated but still outstanding
			ROIC	2013	25% for ROIC of 9.0%	100% for ROIC of 10.5%	5.4%	Nil	Lapsed
			EPS growth	2013 compared to 2010	30% for EPS growth of 6.0%	100% for EPS growth of 12.0%	-3.3%	Nil	
03/03/10	962.0p	03/03/13	Relative TSR	2010 to 2013	30% at median	100% at upper quartile	48th percentile	Nil	36.7% of shares vested. Three-quarters released on 3 March 2013. If after tax number of shares are retained for a further two years, the remaining quarter will be released on 3 March 2015
			ROIC	2012	25% for ROIC of 8.5%	100% for ROIC of 10.5%	9.1%	47.5%	
			EPS growth	2012 compared to 2009	30% for EPS growth of 6.0%	100% for EPS growth of 12.0%	8.8%	62.5%	

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

The following directors received conditional restricted share awards under the long-term incentive plan on 1 May 2013 which will vest, subject to performance, on 1 May 2016 as follows:

			Face value on date of award	
Name	Restricted shares awarded	Share price on date of award	£	% of 2013 base salary
John Fallon	250,000	1,183.0p	£2,957,500	394%
Robin Freestone	150,000	1,183.0p	£1,774,500	326%
Will Ethridge	150,000	1,183.0p	£1,774,500	260%

Summary of share plan interests

The following tables summarise vested, released, lapsed, held, and outstanding share interests under the share-based incentive plans for executive directors who served throughout 2013. Awards are designated as: ABSMP annual bonus share matching plan, subject to performance conditions; LTIP long-term incentive plan, subject to performance conditions; Dividends where dividend-equivalent shares are added without performance conditions to vested shares under the ABSMP and LTIP and released immediately on award.

Report on directors' remuneration continued

Plan	Award date	Vesting date	Status	John Fallon	Robin Freestone	Will Ethridge
ABSMP	21/04/2010	21/04/2013	Released	6,991	26,287	6,658
ABSMP	20/04/2011	20/04/2014	Vested	0	0	0
			Value £000	£0	£0	£0
			Lapsed	4,539	29,049	4,517
			Held	0	0	0
ABSMP	15/05/2012	15/05/2015	Outstanding	8,917	17,833	4,485
ABSMP	15/05/2013	15/05/2016	Outstanding	6,083	–	–
LTIP	04/03/2008	04/03/2011	Released	24,375	30,468	36,562
LTIP	03/03/2009	03/03/2012	Held	29,887	25,617	29,887
LTIP	03/03/2010	03/03/2013	Released	41,257	34,381	41,257
			Lapsed	50,000	41,667	50,000
			Held	13,752	11,460	13,752
LTIP	03/05/2011	03/05/2014	Vested	0	0	0
			Value £000	£0	£0	£0
			Lapsed	150,000	125,000	150,000
			Held	0	0	0
LTIP	02/05/2012	02/05/2015	Outstanding	100,000	100,000	100,000
LTIP	01/05/2013	01/05/2016	Outstanding	250,000	150,000	150,000
Dividends (LTIP)	04/03/2013	04/03/2013	Released (price 1,168.0p)	6,094	7,617	9,141
			Value £000	£71	£89	£107
Dividends (LTIP)	03/04/2013	03/04/2013	Released (price 1,143.0p)	5,199	4,333	5,199
			Value £000	£59	£50	£59
Dividends (ABSMP)	21/05/2013	21/05/2013	Released (price 1,262.0p)	895	3,366	853
			Value £000	£11	£42	£11
Total			Released	84,811	106,452	99,670
			Vested	0	0	0
			Held	43,639	37,077	43,639
			Outstanding	365,000	267,833	254,485
2013 single figure of remuneration			Value £000	£141	£181	£177

Note 1 Vested means where awards are no longer subject to performance conditions. Released means where shares have been transferred to participants. Held means where awards have vested but are held pending release on the relevant anniversary of the award date. Outstanding means awards that have been granted but are still subject to the achievement of performance conditions.

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

Note 3 Performance conditions and vesting for awards under the bonus share matching and long-term incentive plans are described on pages 102 and 103.

Note 4 The single figure of remuneration for 2013 includes all awards that were subject to a performance condition where the performance period ended, or was substantially (but not fully) completed, at 31 December 2013 and awards where the performance condition has been satisfied but where the release of shares is subject to a further holding period. The same methodology has been applied for earlier periods and the single figure for earlier reporting periods has been restated where necessary.

Note 5 The value of shares included in the single figure of remuneration is the number of shares multiplied by the share price on release (or, if the shares have not yet been released, the average share price over the final quarter of the year which for 2013 was 1,310.45p).

Movements in directors' interests in share options

John Fallon and Robin Freestone also hold options under the worldwide save for shares plan as follows:

Name	Date of grant	Options held as at 31 Dec 13	Option price	Earliest exercise date	Expiry date	Value in 2013 single figure £000
John Fallon	7/5/10	1,930	805.6p	1/8/15	1/2/16	0
Robin Freestone	4/5/12	990	909.0p	1/8/15	1/2/16	0

Note 1 No share option awards were made, vested, or exercised in the year.

Note 2 All share options that become exercisable during a year are included in the single figure of total remuneration for that year. The value included in the single figure of total remuneration is the number of options multiplied by the difference between the value on grant and the market value on the earliest exercise date.

Note 3 No variations to terms and conditions of share options were made during the year.

Note 4 Acquisition of shares under the worldwide save for shares plan is not subject to a performance condition.

Note 5 The market price on 31 December 2013 was 1,341.0p per share and the range during the year was 1,119.0p to 1,365.0p.

Payments to former directors

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

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

Marjorie Scardino

Marjorie Scardino stepped down from the Pearson board on 31 December 2012.

In accordance with her employment agreement, six months after retirement Marjorie Scardino received the distribution of the account cash and share balances of her unfunded unapproved defined contribution retirement plan.

Marjorie also retained certain entitlements on retirement and received the following share releases during 2013:

Plan	Date of award	Number of shares retained	Number of shares lapsed	Number of shares released	Date of release	Number of shares outstanding
ABSMP	21 April 2010	63,497	0	63,497	4 March 2013	0
	20 April 2011	47,630	47,630	0	–	0
LTIP	4 March 2008	97,500	0	97,500	4 March 2013	0
	3 March 2009	76,852	0	76,852	4 March 2013	0
	3 March 2010	280,024 subject to 2012 performance	133,333	146,691	3 March 2013	0
	3 May 2011	266,666 subject to 2013 performance	266,666	0	–	0
	2 May 2012	83,333 subject to 2014 performance	0	0	–	83,333
Dividends (ABSMP)	4 March 2013	–	–	6,160	4 March 2013	0
Dividends (LTIP)	4 March 2013	–	–	38,593	4 March 2013	0
	3 April 2013	–	–	18,484	3 April 2013	0

Note In the case of the 21 April 2010 annual bonus share matching award, the number of shares retained and released comprises the total number of shares originally awarded.

Report on directors' remuneration continued

Rona Fairhead

Rona Fairhead stepped down from the Pearson board on 26 April 2013 and left the company on 30 April 2013.

Rona retained certain entitlements on leaving the company and received the following share releases during 2013:

Plan	Date of award	Number of shares retained	Number of shares lapsed	Number of shares released	Date of release	2013 single figure of remuneration £000	Number of shares held	Number of shares outstanding
LTIP	4 March 2008	30,468	0	30,468	4 March 2013	–	0	0
	3 March 2009	25,617	0	25,617	10 May 2013	–	0	0
	3 March 2010	87,508 subject to 2012 performance	41,667	34,381	3 March 2013	–	0	0
				11,460	10 May 2013	–	0	0
	3 May 2011	97,222 subject to 2013 performance + 40,000 shares	97,222	0	–	–	40,000	0
	2 May 2012	44,444 subject to 2014 performance	0	0	–	–	0	44,444
Dividends	4 March 2013	–	0	7,617	4 March 2013	£30	–	–
	3 April 2013	–	0	4,333	3 April 2013	£17	–	–

Note 1 In the case of the 3 May 2011 long-term incentive award, the committee agreed in December 2012 that, in recognition of the circumstances at the time the award was made, 40,000 of the 165,000 shares originally awarded should vest in full at the normal vesting date. The remaining shares would be retained on her leaving pro rata for service and be released subject to performance in the normal way.

Note 2 The value of dividends included in the 2013 single figure of remuneration is calculated pro rata for service in the year.

John Makinson

On stepping down from the board on 1 July 2013, John Makinson's then remuneration package (base salary, annual incentive, allowances and benefits and retirement benefits) continued to apply for the remainder of 2013. He did not receive a Pearson long-term incentive award for 2013.

John's participation in Pearson share plans continues and he received the following share releases during 2013:

Plan	Date of award	Number of shares retained	Number of shares lapsed	Number of shares released	Date of release	2013 single figure of remuneration £000	Number of shares held	Number of shares outstanding
LTIP	4 March 2008	30,468	0	30,468	4 March 2013	–	0	0
	3 March 2009	25,617	0	–	–	–	25,617	0
	3 March 2010	87,508 subject to 2012 performance	41,667	34,381	3 March 2013	–	11,460	0
	3 May 2011	125,000 subject to 2013 performance	125,000	0	–	–	0	0
	2 May 2012	100,000 subject to 2014 performance	0	0	–	–	0	100,000
Dividends	4 March 2013	–	0	7,617	4 March 2013	£44	–	–
	3 April 2013	–	0	4,333	3 April 2013	£25	–	–

Note The value of dividends included in the 2013 single figure of remuneration is calculated pro rata for service in the year.

Payments for loss of office

Rona Fairhead

As announced on 27 November 2012 and set out in the report on directors' remuneration for 2012, Rona Fairhead stepped down from the board at the Annual General Meeting on 26 April 2013 and left the company on 30 April 2013. Her service agreement dated 24 January 2003 provided for notice periods of six months from the director and 12 months from the company and compensation on termination of employment by the company without notice or cause of 100% of annual salary at the date of termination, the annual cost of pension and all other benefits and 50% of potential annual incentive.

The committee and the board determined that her leaving employment was a consequence of the planned incorporation of the professional education division overseen by Rona into other parts of Pearson's education business, coupled with the smaller size of the Financial Times Group owing to recent major divestments. The company therefore paid compensation amounting to £1,148,195 comprising: £529,100, an amount equal to her annual salary as of her leaving date; £195,815, an amount equal to the annual cost to the company of pension and other benefits (but excluding health care to which she remained entitled for 12 months from her leaving date); and £423,280, an amount equal to half of her maximum annual incentive opportunity. The company also made a contribution toward the cost of outplacement counselling (£50,000) and paid legal fees in connection with her leaving (£6,150).

John Makinson

As first announced on 29 October 2012 and confirmed on 1 July 2013, John Makinson stepped down from the Pearson board to assume his full-time responsibilities as chairman of Penguin Random House on 1 July 2013. There was no payment for loss of office.

John's employment continues under service agreements with Pearson Inc. (for the US portion of his duties) and with Pearson Management Services Limited (for his duties in the rest of the world outside the US). These Pearson entities are entering into secondment agreements with Penguin Random House, pursuant to which John's services as chairman are provided to, and paid for by, Penguin Random House. John is paid an annual base salary, but is no longer entitled to a location and market premium or an annual incentive. He will be eligible to receive a one-off performance-related cash long-term incentive award, the terms of which are being agreed by the remuneration committee of Penguin Random House. He will no longer receive awards under the Pearson long-term incentive plan. Penguin Random House is also meeting the cost of John's accrual of Pearson pension benefits while he is seconded to Penguin Random House.

Will Ethridge

As announced on 23 May 2013, Will Ethridge stepped down from the board on 31 December 2013. There was no payment for loss of office. Will's employment with Pearson Education Inc. continues on the same terms and conditions as previously pending his retirement on 31 December 2014. No compensation for loss of office or severance will be payable on his retirement. On retirement, he will retain entitlement to his 2012 long-term incentive award in full and to two-thirds and one-third respectively of his 2013 and any 2014 long-term incentive awards with shares released subject to performance in 2015, 2016 and 2017.

Report on directors' remuneration continued

Interests of directors and value of shareholdings

Directors' interests

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

	Ordinary shares at 31 Dec 13	Conditional shares at 31 Dec 13	Total number of ordinary and conditional shares at 31 Dec 13	Value (x salary)	Guideline (x salary)	Guideline met
Chairman						
Glen Moreno	150,000	–	–	–	–	–
Executive directors						
John Fallon	262,569	43,639	306,208	4.5	2.00	✓
Robin Freestone	478,507	37,077	515,584	10.5	1.25	✓
Will Ethridge	397,017	43,639	440,656	7.2	1.25	✓
Non-executive directors						
David Arculus	16,301	–	–	–	–	–
Vivienne Cox	1,351	–	–	–	–	–
Ken Hydon	17,818	–	–	–	–	–
Josh Lewis	5,681	–	–	–	–	–
Linda Lorimer (appointed 1 July 2013)	637	–	–	–	–	–
Harish Manwani (appointed 1 October 2013)	180	–	–	–	–	–

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

Note 2 The current value of the executive directors' holdings of ordinary and conditional shares is based on the middle market value of Pearson shares of 1,113.0p on 21 February 2014 against base salaries in 2013. All executive directors comfortably exceeded the shareholding guidelines. The shareholding guidelines do not apply to the chairman and non-executive directors.

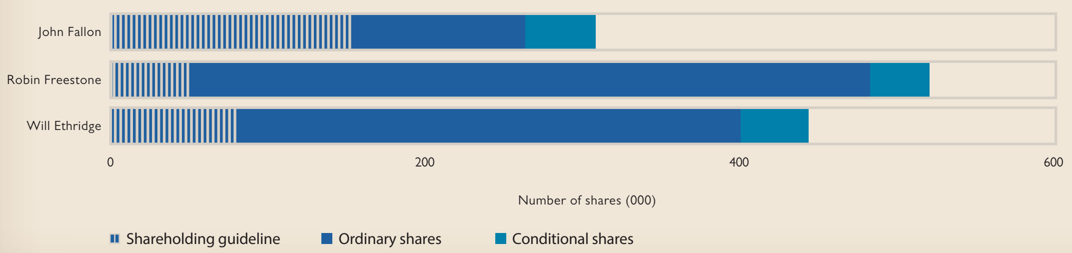
Note 3 Ordinary shares include both ordinary shares listed on the London Stock Exchange and American Depositary Receipts (ADRs) listed on the New York Stock Exchange. The figures include both shares and ADRs acquired by individuals investing part of their own after-tax annual bonus in Pearson shares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

Note 4 The register of directors' interests (which is open to inspection during normal office hours) contains full details of directors' shareholdings and options to subscribe for shares. The market price on 31 December 2013 was 1,341.0p per share and the range during the year was 1,119.0p to 1,365.0p.

Note 5 There were no movements in ordinary shares between 1 January 2014 and a month prior to the sign-off of this report.

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

Interests of directors



Shareholding guidelines for executive directors

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

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

There are currently no mandatory share ownership guidelines below executive director level, although employees are encouraged to become shareholders in the company by retaining shares acquired through the company's discretionary and all-employee stock programmes. The shareholding guidelines do not apply to the chairman and non-executive directors.

Dilution and use of equity

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

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

There are limits on the amount of new-issue equity we can use. In any rolling ten-year period, no more than 10% of Pearson equity will be issued, or be capable of being issued, under all Pearson's share plans, and no more than 5% of Pearson equity will be issued, or be capable of being issued, under executive or discretionary plans.

At 31 December 2013, stock awards to be satisfied by new-issue equity granted in the last ten years under all Pearson share plans amounted to 1.6% of the company's issued share capital. No stock awards granted in the last ten years under executive or discretionary share plans will be satisfied by new-issue equity.

In addition, for existing shares no more than 5% of Pearson equity may be held in trust at any time. Against this limit, shares held in trust at 31 December 2013 amounted to 1.1% of the company's issued share capital.

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

Headroom	2013	2012	2011
All Pearson plans	8.4%	8.3%	8.3%
Executive or discretionary plans	5.0%	5.0%	5.0%
Shares held in trust	3.9%	3.8%	3.2%

Executive directors' non-executive directorships

In accordance with policy, the following executive directors served as non-executive directors elsewhere and retained fees or other benefits for the period covered by this report as follows:

Name	Company	Fees/benefits
Rona Fairhead	HSBC Holdings plc	£83,333

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

Report on directors' remuneration continued

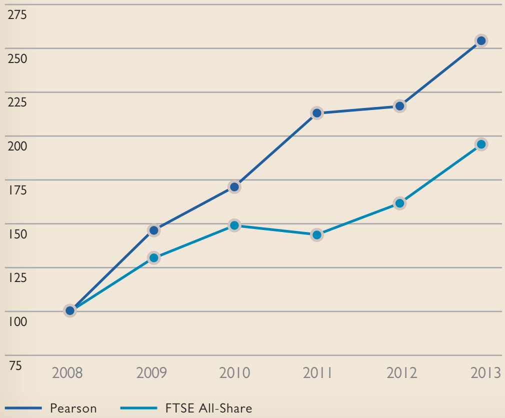
Historical performance and remuneration

Total shareholder return performance

We set out below Pearson's total shareholder return (TSR) performance relative to the FTSE All-Share index on an annual basis over the five-year period 2008 to 2013. 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 new regulations, this section also presents Pearson's TSR performance alongside the single figure of total remuneration for the CEO over the last five years and a summary of the variable pay outcomes relative to the prevailing maximum at the time. The table below summarises the total remuneration for the CEO over the last five years, and the outcomes of annual and long-term incentive plans as a proportion of maximum.

Total shareholder return: five years to 31 December 2013



Financial year ending	2009	2010	2011	2012	2013
Total remuneration – John Fallon (single figure, 000s)	–	–	–	–	1,727
Total remuneration – Marjorie Scardino (single figure, 000s)	6,370	8,466	8,340	5,330	–
Annual incentive – incumbent (% of maximum)	91.3%	92.1%	75.7%	24.2%	34.3%
Long-term incentive – incumbent (% of maximum)	80.0%	97.5%	68.3%	36.7%	Nil

Note 1 Marjorie Scardino stepped down from the board on 31 December 2012 and John Fallon was appointed CEO with effect from 1 January 2013.

Note 2 The annual incentive is the actual annual incentive received by the incumbent as a percentage of maximum opportunity.

Note 3 The long-term incentive is the pay-out of performance-related restricted shares under the long-term incentive plan where the year shown is the final year of the performance period for the purposes of calculating the single total figure of remuneration.

Comparative information

The following information is intended to provide additional context regarding the total remuneration for executive directors.

Relative percentage change in remuneration for CEO

The following table sets out the change between 2012 and 2013 in three elements of remuneration for the CEO, in comparison to the average for all employees.

However, while the committee considers the increase in base pay for the CEO relative to the broader employee population, benefits are driven by local practices and eligibility is determined by level and individual circumstances which do not lend itself to comparison. Similarly, annual incentives are driven by different factors throughout the organisation and so are typically not compared.

	Base salary	Allowances and benefits	Annual incentive	Total
CEO	-24%	-77%	7%	-22%
All employees	5%	11%	31%	8%

Note 1 The figures for the CEO are based on the remuneration of Majorie Scardino for 2012 and of John Fallon for 2013.

Note 2 The figures for all employees reflect average salaries and average employee numbers each year. Annual incentives include all plans, including sales incentives.

Relative importance of pay spend

The committee consider directors' remuneration in the context of the company's allocation and disbursement of resources to different stakeholders.

In particular, we chose operating profit because this is a measure of our ability to reinvest in the company. We include dividends because these constitute an important element of our return to shareholders.

			Year-on-year change	
£m	2013	2012	£m	%
Operating profit	736	932	-196	-21%
Dividends	372	346	26	+8%
Total wages and salaries	1,836	1,610	226	+14%

Note Wages and salaries include continuing operations only and include directors. 2012 is restated on the same basis. Average employee numbers for continuing operations for 2013 were 42,115 (2012: 42,135). Further details are set out in note 5 to the financial statements on page 142.

Information on changes to remuneration for 2014

Executive directors' base salaries

We have undertaken a regular periodic review of base salaries for 2014 taking into account general economic and market conditions, the level of increases made across the company as a whole, the remuneration of executives in similar positions in comparable companies and individual performance.

As a result of this review, the 2014 base salaries for the CEO and CFO are as follows:

	John Fallon	Robin Freestone
Base salary at 31 December 2013	£750,000	£545,000
Increase	£15,000 2.0%	£11,000 2.0%
Base salary at 1 April 2014	£765,000	£556,000

Full details will be set out in the annual remuneration report and included in the single figure of total remuneration for 2014.

Annual incentive

The key design principles underlying the company's approach to annual incentives for 2014 are:

- full alignment of annual incentives with the global education strategy to reinforce a 'one Pearson' focus;
- a clear, transparent, coherent, consistent, organisation-wide approach to incentives and performance management with a common incentive framework for Lines of Business, Geographies and Enabling functions;
- the size of the overall annual incentive pay-out will be linked to overall Pearson performance.

Report on directors' remuneration continued

The principles that underlie the 'one Pearson' approach to funding are that:

- there will be a single annual incentive pool for Pearson which will vary according to the performance of the whole company;
- for 2014, the overall Pearson performance measures and weightings will be: adjusted earnings per share (60% weighting); sales (20%); cash flow (20%);
- there will be a theoretical 'on target' size for the annual incentive pool which is the sum of all employees' annual incentive opportunities;
- there will be scope to flex the size of the pool upwards if performance exceeds target (up to a cap) and downwards if performance falls short of target (down to a threshold below which no annual incentive would be paid). This flex will be sufficiently sensitive to demonstrate a clear link between overall performance and the annual incentive pay-out, but not so sensitive that there is significant uncertainty in the total pay-out. The committee will set a range around which the annual incentive pay-out can flex;
- the Pearson financial targets will be set each year as part of the normal operating plan process. The CEO and CFO will recommend the overall Pearson incentive funding metrics (including performance measures, targets and weightings) to the committee for approval in the normal way;
- the Pearson-derived pay-out may be informed and modified (up or down) reflecting the circumstances at the time consistent with the committee's normal adjustment powers.

In relation to the operation of the annual incentive framework for the executive directors and the Pearson Executive:

- there will be no change in individual annual incentive opportunities;
- for 2014, there would be one mechanism for determining annual incentive for an individual, namely a combination of Pearson-wide performance and individual goals;
- the sum of the CEO's and the Pearson Executives' 'on target' annual incentive constitutes the incentive pool for this group which flexes up or down based on overall Pearson performance;
- individual performance is assessed against goals set at the start of the year;
- individual pay-outs up to individual maximum opportunities and within the total pool are recommended by the CEO (or by the chairman in the case of the CEO himself) for review and, in the case of the executive directors, approval by the committee.

The committee considers the performance targets for 2014 to be commercially sensitive. Details of performance measures, weightings and targets will be disclosed in the annual remuneration report for 2014 if and to the extent that the committee deems them to be no longer commercially sensitive.

Long-term incentives

The committee reviewed the design and operation of the long-term incentives plan with the following changes for performance-related awards to be granted to members of the Pearson Executive in 2014:

- the weighting of the performance metrics will be 50% on earnings per share growth, 33.3% on return on invested capital and 16.7% on relative total shareholder return.
- performance will continue to be tested over three years and 75% of the vested shares will continue to be released at that point. However, there will be a mandatory restriction on participants' ability to dispose of the 75% of the vested shares (other than to meet personal tax liabilities) for a further two years. Furthermore, participants' rights to the release of the 25% of the vested shares will be subject to continued employment over the same period.

We have set targets for the 2014 awards that are consistent with the company's strategic objectives over the period to 2016.

Subject to approval of the company's remuneration policy, the performance measures and targets for the 2014 long-term incentive awards to the executive directors and other members of the Pearson Executive that will be made as soon as practicable after the AGM will be as follows:

Performance measure	Weighting	Performance period	Pay-out at threshold	Pay-out progression	Pay-out at maximum
EPS growth	50%	2016 compared to 2013	30% for EPS growth of 6.0%	Straight-line	100% for EPS growth of 12.0%
ROIC	33.3%	2016	30% for ROIC of 6.5%	50% for ROIC of 7.0%	100% for ROIC of 7.5%
Relative TSR	16.7%	2014 to 2017	30% at median	Straight-line	100% at upper quartile

We will set the level of individual awards consistent with those seen in recent years and below the policy maximum taking into account:

- the face value of individual awards at the time of grant, assuming that performance targets are met in full;
- market practice for comparable companies and market assessments of total remuneration from our independent advisers;
- individual roles and responsibilities; and
- company and individual performance.

At the time of writing, the committee has yet to approve the 2014 long-term incentive awards for the executive directors and other members of the Pearson Executive.

Report on directors' remuneration continued

Full details of individual awards and of the performance measures, weightings and targets for 2014 will be set out in the annual remuneration report for 2014.

For 2015 and onwards, the averaging period for the calculation of relative total shareholder return will be moved to the period running up to the year end and the length of the averaging period will be increased to three months more in line with institutional investors' preferences.

Annual bonus share matching

The previous annual bonus share matching plan will cease to operate with the last awards made in 2013 in respect of annual incentive for 2012. We have not made any compensatory adjustments to annual or long-term incentive opportunities to take this into account.

Fees for the chairman and non-executive directors

The chairman's and non-executive directors' fees were reviewed for 2014.

As a consequence of that review, the basic non-executive directors' fee, and the fees for committee chairmanship and committee membership were increased. Fees for the chairmanship and membership of the reputation and responsibility committee were also introduced for the first time. The salary for the chairman remains unchanged.

The policy and future arrangements are set out on page 92 in the directors' remuneration policy report.

Approved by the board and signed on its behalf by

David Arculus Director
10 March 2014