

# 2017 remuneration policy

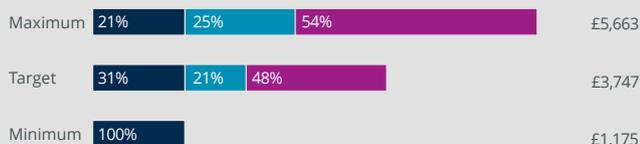
The remuneration committee presents the 2017 directors' remuneration policy (2017 policy), which will be put to shareholders for binding vote at the Annual General Meeting to be held on 5 May 2017. Subject to shareholder approval, the effective date of this policy will be 5 May 2017. However, it is proposed, subject to approval at the AGM, that changes to executive director incentives be made effective from the start of the 2017 performance periods. The intention of the committee is that the policy will remain in place for three years from the date of its approval.

We have evolved our remuneration policy to match our updated remuneration principles:

|  |  |  |   |  |
|--|--|--|---|--|
| <p><b>1</b></p> <p><b>Sustainability and affordability</b></p> <p>Funded through results; strong link to sustainable performance, cost control and appropriate capital allocation.</p> | <p><b>2</b></p> <p><b>Pay for performance</b></p> <p>Pay mix focuses on variable pay; aligned fully with KPIs: EPS; operating profit; sales; operating cash flow; total shareholder return and return on invested capital.</p> | <p><b>3</b></p> <p><b>Flexibility</b></p> <p>Performance metrics linked to strategic imperatives can be selected annually to give us the agility to "move more quickly" in support of Pearson's transformation strategy.</p> | <p><b>4</b></p> <p><b>Alignment</b></p> <p>Incentive plans are designed to reflect sustainable value creation in our drive for growth and efficiency through "becoming a simpler, more focused business".</p> | <p><b>5</b></p> <p><b>Reward for sustainable company performance</b></p> <p>Stretching financial and strategic business imperative metrics support delivery of strategy.</p> |
|--|--|--|---|--|

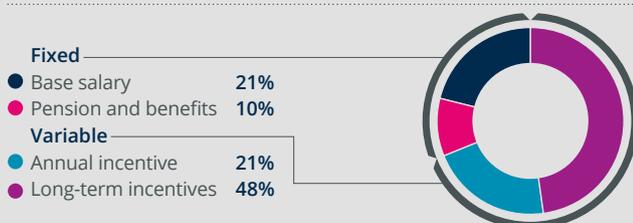
## Pay and performance scenario analysis

### Chief executive officer (John Fallon) £000



- Base salary, allowances, benefits and pension
- Annual incentive
- Long-term incentives

### CEO fixed vs variable at target



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

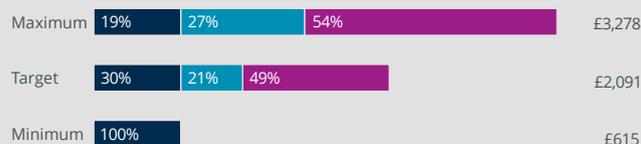
The charts above show what each director could expect to receive in 2017 under different performance scenarios, based on the definitions of performance opposite.

On this basis, the relative weighting of fixed and performance-related remuneration and the absolute size of the remuneration packages for the chief executive officer and the chief financial officer are shown above.

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

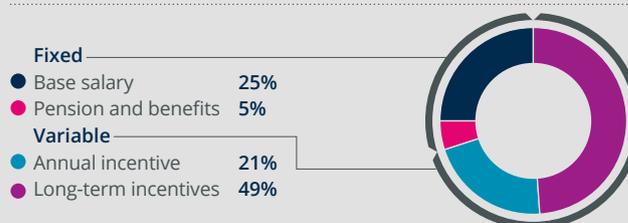
**Note** The value of long-term incentives does not take into account dividend awards that are payable on the release of restricted shares nor any changes in share price. Nor does this infer a precedent for future LTIP awards in 2017 onwards which will be implementation decisions in each year. See p106 for more information on 2017 awards.

### Chief financial officer (Coram Williams) £000



- Base salary, allowances, benefits and pension
- Annual incentive
- Long-term incentives

### CFO fixed vs variable at target



| Performance scenario | Elements of remuneration and assumptions   |
|----------------------|--|
| Maximum              | 2017 base salary; allowances, benefits and retirement benefits at the same percentage of base salary as in 2016; maximum individual annual incentive as per policy; maximum value of 2016 long-term incentive award  |
| Target               | 2017 base salary; allowances, benefits and retirement benefits at the same percentage of base salary as in 2016; target individual annual incentive as per policy; target value of 2016 long-term incentive award (Willis Towers Watson's independent assessment of the expected value of the award i.e. the net present value taking into account all the conditions) |
| Minimum              | 2017 base salary; allowances, benefits and retirement benefits at the same percentage of base salary as in 2016; no annual or long-term incentives   |

## Remuneration policy

### 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 in the context of business performance and conditions prevailing, and is routinely benchmarked against total remuneration for similar positions in comparable companies.

#### Base salary

##### Purpose and link to strategy

- › Helps to recruit, reward and retain.
- › Reflects level, role, skills, experience, the competitive market 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: select UK human capital intensive businesses; and UK and US 'media convergence' companies with a focus on digital, information services and technology. These companies are of a range of sizes relative to Pearson, but the method our independent advisers, Willis 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 and consider base salary levels within the broader FTSE 100. 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 up to 25% over the normal maximum limit in specific individual situations including internal promotions and material changes to the business or the role. This discretion will be exercised only in exceptional circumstances and the committee would consult with major shareholders before doing so, proceeding only where there was clear consensus in favour among those consulted.

##### Performance conditions and period

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.

There is no relevant performance period.

#### 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 healthcare, 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 2016 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, other than in the case of increases in the cost of benefits that are outside Pearson's control and changes in benefit providers. The committee will retain the further discretion to deliver a total value of benefits up to 25% above the normal limit in specific individual situations including changes in individual circumstances such as health status and changes in the role such as relocation. This discretion will be exercised only in exceptional circumstances and the committee would consult with major shareholders before doing so, proceeding only where there was clear consensus in favour among those consulted.

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 and period

None.

There is no relevant performance period.

## 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.

Under the Money Purchase 2003 section of the Pearson Group Pension Plan, 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.

Depending on when they joined the company, directors may participate in the Final Pay section of the Pearson Group Pension Plan, which is closed to new members.

Under the Final Pay section of the Pearson Group Pension Plan, 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.

Executive directors 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 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 Retail Prices Index (All Items). The cap was £150,600 as at 6 April 2016.

UK executive directors 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.

### 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).

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.

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

Coram Williams is a member of the Final Pay section of the Pearson Group Pension Plan with continuous service with a service gap. His pension accrual rate is 1/60th of pensionable salary per annum, restricted to the plan earnings cap.

If any executive director is from, or works, outside the UK, the committee retains a discretion to put in place retirement benefit arrangements for that director in line with local market practice including defined benefit pension arrangements operated by Pearson locally. The maximum value of such arrangement will reflect local market practice at the relevant time. The committee will also honour all pre-existing retirement benefit obligations, commitments or other entitlements that were entered into by a member of the Pearson Group before that person became a director.

### Performance conditions and period

None.

There is no relevant performance period.

# Remuneration policy

## Annual incentives

### Purpose and link to strategy

- › Motivate the achievement of annual business goals and personal objectives.
- › Provide a focus on key financial metrics.
- › Reward individual contribution to the success of the company.
- › Align to strategy execution priorities.

### Operation

Annual incentive 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 plan is designed to incentivise and reward underlying performance. Actual results are adjusted to remove the effect of foreign exchange and portfolio changes (acquisitions and disposals) and other relevant factors that the committee considers do not reflect the underlying performance of the business 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 officer, the individual maximum incentive opportunity that will apply for 2017 is 180% of base salary and 170% for the chief financial officer (which are the same opportunities as applied for 2016).

There is normally no pay-out for performance at threshold.

### Performance conditions and period

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.

The funding of annual incentives will normally be related to the performance against financial and strategic imperatives performance targets. For 2017 and onwards, financial metrics will normally account for at least 75% of the total annual opportunity and be related to the performance against targets for Pearson's adjusted earnings per share and/or operating profit, sales, and operating cash flow. For 2017, the weightings will be: adjusted earnings per share 22.5%, operating profit 22.5%, sales 15% and operating cash flow 15%. The remaining total annual opportunity will be subject to performance metrics linked to strategic imperatives set by the committee as it considers appropriate in each year. These will be linked to:

### Strategic imperatives

KPI

#### Competitive performance

- › Holding or gaining share in major markets
- › Higher Education direct/ecommerce sales to consumers

#### Transformation

- › Delivery of Enabling Programme milestones to upgrade the customer experience, accelerate the digital transformation and the delivery of on-going cost, efficiency and process transformations

#### Culture, talent & brand

- › Improvement in brand favourability and year-on-year improvement in employee engagement survey scores

Each metric will be measured, using third party data or externally audited internal data (where third party data is not available or applicable).

Performance metrics linked to strategic imperatives can be selected annually to support Pearson's transformation strategy.

A pay-out will only be made if a minimum level of performance has been achieved under the financial metrics, as determined by the committee each year.

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.

The performance period is one year.

## 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.

### Operation

Awards of restricted shares are made on an annual basis.

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

Performance will continue to be tested over three years and 75% of the vested shares will be released at that point. However, there is a mandatory restriction on participants' ability to dispose of the 75% of the vested shares (other than to meet personal tax liabilities) for a further two years. Furthermore, participants' rights to the release of the 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 the circumstances described in the recruitment section of this policy below, it is the company's policy not to award restricted shares to executive directors without performance conditions.

The Long-Term Incentive Plan also provides for the grant of stock options. While it is not the committee's intention to grant stock options in 2017 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.

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 payouts 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
- › 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 (and up to 25% over the normal maximum limit) may

be made in exceptional circumstances, for example, for retention purposes or to reflect particular business situations. This discretion will be exercised only in exceptional circumstances and the committee would consult with major shareholders before doing so, proceeding only where there was clear consensus in favour among those consulted.

The committee retains flexibility to make exceptional awards of up to 25% above the normal limit in specific circumstances. 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.

While it is not the committee's intention to grant stock options in 2017 or the foreseeable future, the maximum value of stock option awards would be the equivalent expected value of, and in place 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.

### Performance conditions and period

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. The proportion of the award that vests at threshold level of performance under each performance condition is 25%.

For 2017 and onwards, awards will normally be subject to the achievement of targets for earnings per share, return on invested capital and relative total shareholder return. For 2017, and following shareholder consultation, the weighting of the performance metrics within the Pearson Long-Term Incentive Plan will be changed to 40% earnings per share, 30% return on invested capital and 30% relative total shareholder return (previously, one half, one third and one sixth, respectively).

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 made in 2017 and onwards, TSR will be measured relative to the constituents of the FTSE 100 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 consolidated financial statements for a detailed description of adjusted earnings per share).

The performance period is three years.

## Remuneration policy

### Notes to the policy table

#### 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 identified sales, earnings per share, operating profit, operating cash flow and key strategic business imperatives as being relevant measures of Pearson's performance against its shorter-term strategic objectives and business priorities.

In the case of long-term incentives, the committee judged the following to be most closely matched to sustained delivery of strategy and alignment with shareholders' interests: earnings per share rewards the delivery of the desired outcomes from our strategic growth objectives and is imperative if we are to improve our total shareholder return and our return on invested capital. Return on invested capital is used to track investment returns and to help assess capital allocation decisions within the business. We selected total shareholder return relative to the constituents of the FTSE 100 because, in line with many of our shareholders, we considered that part of executive directors' rewards should be linked to performance relative to companies of comparable size, scale and maturity that are similarly impacted by global macro-economic influences.

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.

#### Pre-existing commitments

In addition to the remuneration arrangements described above, 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, including those entered into at a time when the relevant individual was not a director of Pearson or when the terms of those arrangements were consistent with the shareholder approved directors' remuneration policy then in force.

#### 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 other Pearson employees in the UK

› Many employees participate in some form of cash-based annual incentive, bonus, profit-share or sales commission plan based on annual performance targets and selected senior employees are also eligible to receive share awards. Incentive plans for the Pearson executive management team form the basis of the incentive plans throughout the organisation in 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 management – selected on the basis of their role, performance and potential – currently hold performance or 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.

#### Recruitment

The committee expects any new executive directors to be engaged on the same terms and to be awarded variable remuneration within the same normal limits and subject to the same conditions as for the current executive directors outlined in the policy.

In setting the basic salary for any new executive director, the committee will apply a level appropriate to recruit a suitable candidate, having regard to the factors set out in the future policy table.

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. The committee may do this in the following circumstances:

- › 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 p99 but would 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. 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, payment 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, payment 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. The company may also pay an amount considered to be reasonable by the remuneration committee in respect of fees for legal and tax advice and outplacement support for the departing director.

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 pro-rated for the period of the participant's service in the restricted period (although the committee may in its absolute discretion waive or vary the pro-rating).

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.

## Remuneration policy

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

The rules of Pearson's discretionary share plans make provision for the treatment of awards in respect of corporate activity, including a change of control of Pearson. The committee would act in

accordance with the terms of the awards in these circumstances, which includes terms as to the assessment of performance conditions and time apportionment.

Details of each individual's service agreement are outlined in the table below. 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            | 25 October 2015   | 12 months from the director;<br>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)<br>26 February 2015 (Coram Williams) | 6 months from the director;<br>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 the 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 includes oversight of certain remuneration matters below that of the chief executive, the other executive directors and other members of the Pearson executive management team. Before the remuneration packages for the Pearson executive management team are set for the year ahead, the committee considers reports from the chief executive on general morale and chief human resources officer on retention, general pay trends in the market and the level of pay increases and incentives 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.

In November 2016 we wrote to our key shareholders and the voting advisory agencies, seeking their views on the proposed changes to Pearson's remuneration policy.

The chairman of the Remuneration Committee met or corresponded with a number of our shareholders to understand better their views on our proposals and to answer their questions on why the proposed changes were appropriate.

We received valuable feedback on a number of points, which reflected a significant range of opinions. These matters have been addressed in this policy report.

We are committed to continued engagement going forward and where it concerns the implementation of this policy.

## 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. Following a review of the structure of the fees paid to non-executive directors, the board has determined that it would be appropriate to introduce additional fees for membership and chairmanship of the nomination & governance committee. Having taken independent advice from Willis Towers Watson, the fee that has been set by the board reflects the median level within the FTSE 100.

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 chairman's and non-executive directors' basic fee is paid in Pearson shares that the non-executive directors have committed to retain for the period of their directorships. 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. The chairman and 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 reviewed in 2017 and have not been increased since his appointment. Fees for the non-executive directors were last increased with effect from 1 May 2014. Following a review of fees paid to non-executive directors, the board has determined that most fees will remain unchanged, other than a small increase to apply to membership and chairmanship of the reputation & responsibility committee. A fee has also been introduced for the newly formed nomination & governance committee. These changes will take effect from the AGM on 5 May 2017, subject to the approval of this policy.

The structure of non-executive directors' fees with effect from the date of this policy is as follows:

| Director  | Fee                                    |
|---|--|
| Non-executive director                                | £70,000                                |
| Chairmanship of audit committee                       | £27,500                                |
| Chairmanship of remuneration committee                | £22,000                                |
| Chairmanship of reputation & responsibility committee | £10,000 (£13,000 with effect from AGM) |
| Chairmanship of nomination & governance committee     | £15,000 (with effect from AGM)         |
| Membership of audit committee                         | £15,000                                |
| Membership of remuneration committee                  | £10,000                                |
| Membership of reputation & responsibility committee   | £5,000 (£6,000 with effect from AGM)   |
| Membership of nomination & governance committee       | £8,000 (with effect from AGM)          |
| 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 (excluding the chairman) 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 fee for the chairman remains unchanged at £500,000 per year.

### Performance conditions

None.

### Performance period

None.