Pearson

Pearson plc

Audit Committee - Charter and Terms of Reference

These terms of reference were last reviewed and approved by the Board of Directors ("the Board") on 6 December 2019.

1. Purpose and Primary Duty

The Committee is established by the Board primarily for the purpose of assisting the Board's oversight of: (1) the quality and integrity of the Company's financial reporting and statements and related disclosure, (2) the Company's accounting policies and practices, (3) the external audit, including the appointment, qualification, independence and the performance of the external auditor, (4) the Company's risk management systems and internal control environment including the performance of the internal audit function (i.e. Group Internal Audit), and (5) the Company's compliance with legal and regulatory requirements in relation to financial reporting and accounting matters. The Committee shall also review significant financial returns to regulators and any financial information contained in certain other documents, such as announcements of a price sensitive nature.

2. Membership and Attendance

2.1. Members of the Committee shall be appointed by the Board, on the recommendation of the Nomination & Governance Committee in consultation with the Chair of the Audit Committee. The Committee shall comprise at least three members including, where possible, one member of the remuneration committee.

2.2. The members of the Committee may be removed or replaced and any vacancies shall be filled by the Board upon recommendation of the Committee Chair or Nomination & Governance Committee.

2.3. All members of the Committee shall be independent non-executive directors (as defined by the UK Corporate Governance Code ("the Code")). The Chair of the Board shall not be a member of the Committee. At least one member of the Committee should have recent relevant financial knowledge and at least one member should have competence in accounting or auditing or both, as defined by the Board. All members of the Committee shall meet the applicable independence, financial literacy and other requirements of the stock exchanges where the Company's shares are listed. The Committee as a whole should have competence relevant to the sector in which the company operates.

2.4. Care should be taken to minimise the risk of any conflict of interest that might be seen to give rise to an unacceptable influence.

2.5. The Board shall appoint the Committee Chair who shall be an independent non-executive director. In the absence of the Committee Chair and/or an appointed deputy, the remaining members in attendance at the meeting shall elect one of their number present to chair the meeting.

2.6. Only members of the Committee have the right to attend Committee meetings. However, the Committee may ask individuals such as the Chair, Chief Executive and any relevant senior management to attend all or part of any meeting as and when appropriate and necessary.

2.7. The Committee may ask the Chief Financial Officer, the SVP Internal Audit, Risk & Compliance, VP Internal Audit, and representative(s) of the external auditors to attend all meetings.

2.8. Appointments to the Committee shall be for a period of up to three years, which may be extended for two further three year periods, provided the director remains independent.

3. Secretary

The Company Secretary or his/her nominee shall act as the Secretary of the Committee.

4. Quorum

The quorum necessary for the transaction of business shall be two members. A duly convened meeting of the Committee at which a quorum is present shall be competent to exercise all or any of the authorities, powers and discretions vested in or exercisable by the Committee.

5. Frequency of Meetings

5.1. The Committee shall meet not less than four times a year, usually to coincide with the publication of the Company's financial statements, and at such other times as the Committee Chair, in consultation with the Committee members, shall require. The Committee shall meet separately with representatives of management, the SVP Internal Audit, Risk & Compliance, the VP Internal Audit, and the external auditor at least once per year.

5.2. Outside of the formal meeting programme, the Committee Chair, and to a lesser extent the other Committee members, will maintain a dialogue with key individuals involved in the Company's governance, including the Chair, Chief Executive, Chief Financial Officer, the external audit lead partner, the SVP Internal Audit, Risk & Compliance, and the VP Internal Audit.

6. Agenda for Meetings

The Committee Chair shall develop and set the Committee's agenda, in consultation with the Company's management and, if appropriate, with the external auditors.

7. Notice of Meetings

7.1. Meetings of the Committee shall be summoned by the Secretary of the Committee at the request of any member or at the request of the Chief Financial Officer, the SVP Internal Audit, Risk & Compliance or by the external auditors if they consider it necessary.

7.2. Unless otherwise agreed, notice of each meeting confirming the venue, time and date together with an agenda of items to be discussed, shall be forwarded to each member of the Committee, any other person required to attend and all other non-executive directors, no fewer than seven days prior to the date of the meeting. Supporting papers shall be sent to Committee members and to other attendees as appropriate, at the same time, unless otherwise agreed.

8. Minutes of Meeting

8.1. The Secretary shall minute the proceedings and resolutions of all meetings of the Committee, including recording the names of those present and in attendance.

8.2. The Secretary should ascertain, at the beginning of each meeting, the existence of any conflicts of interest and minute them accordingly.

8.3. Minutes of Committee meetings shall be circulated promptly to all members of the Committee and to the Chair and all members of the Board, unless a conflict of interest exists or it would be inappropriate to do so in the opinion of the Committee Chair. Those in attendance shall receive minutes for the items that were discussed during their attendance.

9. Annual General Meeting ("AGM")

The Committee Chair, or if he is unable to attend, any other member of the Committee, shall attend the AGM prepared to respond to any shareholder questions on the Committee's activities.

10. Duties

The Committee shall carry out the duties below for the Company, major subsidiary undertakings and the group as a whole, as appropriate.

10.1. Internal Control, Risk Assessment and Internal Audit

10.1.1. The Committee shall approve the statements to be made in the annual report concerning internal control policies, procedures for the identification, assessment, management and reporting of risks, and the viability statement.

10.1.2. The Committee shall monitor and keep under review the effectiveness of the Company's risk management and internal control systems and will at least annually review the adequacy and effectiveness of the Company's risk management and internal control systems to satisfy itself that these are sound and provide reasonable assurance against significant loss and/or material financial misstatement. The Committee will carry out a robust assessment of the Company's emerging and principal risks and will satisfy itself that the disclosures in the Company's financial statements relating to risk management and the internal control environment are soundly based and comply with relevant exchange listing requirements.

10.1.3. The Committee shall approve the appointment and dismissal of the SVP Internal Audit, Risk & Compliance and of the VP Internal Audit.

10.1.4. The Committee shall review and approve the role and mandate of internal audit, monitor and review the effectiveness of its work, and annually approve the internal audit charter ensuring it is appropriate for the current needs of the organisation.

10.1.5. The Committee shall satisfy itself that the Group Internal Audit function is adequately resourced, in terms of both quality and quantity of staff and has appropriate access to information to enable it to perform its function effectively and in accordance with the relevant professional standards, and shall approve the annual internal audit plan to ensure it is aligned with the key risks of the business. The Committee shall receive and review regular reports from the SVP Internal Audit, Risk & Compliance on the activities of the function to include, but not limited to, findings from internal audit visits, risk management issues including significant change management projects, fraud and whistleblowing incidents. The Committee shall review and monitor management's responsiveness to the findings and recommendations of the Group Internal Audit function.

10.1.6. The SVP Internal Audit, Risk & Compliance and the VP Internal Audit shall each be given the right of direct access to the Committee Chair, the Board Chair, and to the Committee, and are accountable to the Committee, and at least once a year the Committee should meet with them jointly or individually, without management being present, to discuss their remits and any issues arising from the internal audits carried out.

10.1.7. The Committee shall carry out an annual assessment of the role and effectiveness of the internal audit function, including in the overall context of the company's risk management system and the work of compliance, finance and the external auditor, and as part of this assessment shall:

a) meet with the SVP Internal Audit, Risk & Compliance and the VP Internal Audit without the presence of management to discuss the effectiveness of the function;

b) review and assess the annual internal audit work plan;

c) receive a report on the results of the internal auditors' work;

d) determine whether it is satisfied that the quality, experience and expertise of internal audit is appropriate for the business; and

e) review the actions taken by management to implement the recommendations of internal audit and to support the effective working of the internal audit function.

10.1.8. The Committee shall consider whether an independent, third party review of internal audit effectiveness and processes is appropriate.

10.2. Whistleblowing and Fraud

10.2.1. Where requested by the Board, the Committee shall support the Board in its review of the group's arrangements for its workforce to raise concerns, in confidence and, if they wish, anonymously, about possible improprieties in financial reporting, operational or other matters. . The objective shall be to ensure that arrangements are in place for the proportionate and independent investigation of such matters and appropriate follow up action.

10.2.2. The Committee shall review the group's policies, systems and controls for preventing and detecting fraud, bribery and corruption and receive any reports on non-compliance and shall review its code of corporate conduct/business ethics and its policies for ensuring that the group complies with the relevant regulatory and legal requirements.

10.3. External Audit

10.3.1. The Committee shall consider and make recommendations to the Board, to be put to shareholders for approval at the AGM, for the appointment, re-appointment and removal of the Company's external auditors, the services to be provided by them, their remuneration and the terms of their engagement. Annually the Committee shall consider whether it is appropriate to recommend the reappointment of the external auditors and, if not, recommend to the Board that a tender process is initiated. The Committee shall oversee the selection process for new auditors and if an auditor resigns the Committee shall investigate the issue leading to this and decide whether any action is required. The Committee shall ensure that lead and concurring audit

partners, together with other significant audit partners within the appointed firm are rotated from time to time, but no longer than once every five years for the Company and once every seven years for its subsidiaries, and in accordance with the rules of the stock exchanges where the Company's shares are listed.

10.3.2. The Committee shall ensure that the Company complies with the requirements of the Competition and Markets Authority and the UK implementation of EU Regulation 537/2014 and Directive 2014/56/EU in respect of audit firm tendering and rotation, initially by putting the statutory audit contract out to tender in time for the new firm to be appointed not later than the 2023 audit. Thereafter the Committee shall ensure that at least once every ten years the audit services contract is put out to tender, with a change of firm at least every twenty years, to comply with the regulatory requirements and to enable the Committee to compare the quality and effectiveness of the services provided by the incumbent auditor with those of other audit firms. In respect of such a tender the Committee shall oversee the process and ensure that it complies with all applicable regulatory and legal requirements (including the UK implementation of Article 16 of the EU Regulation) and that all tendering firms have such access as is necessary to information and individuals during the tendering process.

10.3.3. The Committee shall meet with the external auditors at least twice each year, once at the planning stage, where the scope of the audit will be considered, and once post audit at the reporting stage, and shall ensure that any auditor's management letters and management's responses are reviewed. The Committee shall meet the external auditor at least once a year, without management being present, to discuss their remit and any issues arising from the audit.

10.3.4. The Committee shall discuss with the external auditor the factors that could affect audit quality and review and approve the annual audit plan and ensure that it is consistent with the scope of the audit engagement, having regard to the seniority, expertise and experience of the audit team.

10.3.5. The Committee shall review the findings of the audit with the external auditor. This shall include but not be limited to, the following: a discussion of any major issues that arose during the audit; key accounting and audit judgements; the auditor's explanation of how the risks to audit quality were addressed; levels of errors identified during the audit; significant adjustments resulting from the audit; the auditor's view of their interactions with senior management; and any material misstatements detected by the auditors that individually or in aggregate have not been corrected and the management's explanations as to why they have not been adjusted; and any possible impairments of the group's assets.

10.3.6. The Committee shall also review the effectiveness of the audit, including an assessment of the quality of the audit, the handling of key judgements by the auditor and the auditors response to questions from the Committee, as well as review any representation letters requested by the external auditor before they are signed by management; review the management letter and management's response to the auditors findings and recommendations and develop a policy on the supply of non-audit services by the external auditor, taking into account any relevant ethical guidance on the matter.

10.3.7. The Committee shall develop and recommend to the Board, the company's formal policy on the provision of non-audit services by the auditor, including pre-approval of non-audit services by the Committee. The policy should include consideration of the following matters:

a) threats to the independence and objectivity of the external auditor and any safeguards in place;

b) the nature of the non-audit services;

c) whether the external audit firm is the most suitable supplier of the non-audit service;

d) the fees for the non-audit services, both individually and in aggregate, relative to the audit fee; and

e) the criteria governing compensation.

10.3.8. The Committee shall review the relationship with external auditors including (but not limited to):

a) the independence, objectivity, qualifications, experience and performance of the external auditors, taking into account relevant professional and regulatory requirements;

b) any threats to the auditor's independence and the safeguards applied to mitigate those threats including the provision of any non-audit services;

c) satisfying itself that there are no relationships (such as family, employment, investment, financial or business) between the auditor and the Company (other than in the ordinary course of business) which could adversely affect the auditor's independence and objectivity;

d) discussions with the external auditors concerning such issues as compliance with accounting standards and any proposals which the external auditors have made relating to the Company's internal auditing standards;

e) approval of their terms of engagement, including any engagement letter issued at the start of each audit and the scope of the audit;

f) agreeing with the Board a policy regarding the employment of former employees of the Company's auditor, taking into account the Ethical Standard, and legal requirements, and monitoring the implementation of this policy;

g) monitoring the auditor's processes for maintaining independence, its compliance with relevant ethical and professional guidance on the rotation of audit partners, the level of fees paid by the Company compared to the overall fee income of the firm, office and partner and other related requirements;

h) ensuring a proper system is in place to enable co-ordination with the activities of the Group Internal Audit function;

i) evaluating the risks to the quality and effectiveness of the financial reporting process in light of the external auditor's communications with the Committee;

j) assessing annually their qualifications, expertise and resources and the effectiveness of the audit process which shall include a report from the external auditor on their

own internal quality procedures. The Committee should, at least annually, obtain and review: (1) the external audit firm's annual transparency report and the annual report of the FRC's Audit Quality Review team on its work; (2) any material issues raised by the most recent internal quality control review or peer review of the audit firm, or by any investigation by governmental or professional authorities within the last five years, regarding any independent audit carried out by the firm, and any steps taken to address these issues; and (3) all relationships between the auditor and the Company;

k) reviewing the outcome of any regulatory inspections of the external audit of the Company, and considering the implications of any findings for the current or future audits; and

l) considering the risk of the withdrawal of the Company's present auditor from the market.

10.3.9. The Committee shall review and approve the fees to be paid to the external auditor, both for audit and non-audit services and shall ensure that the level of fees is appropriate to enable an effective and high quality audit to be conducted and that there are no prohibited services.

10.4. Financial Reporting

The Committee shall monitor the integrity of the financial statements of the Company, including its annual and half-yearly reports, interim management statements, preliminary results, announcements and any other formal announcements relating to its financial performance, reviewing significant financial reporting issues and judgments which they contain, having regard to matters communicated to it by the external auditor, before submission to the Board. The Committee shall also review any significant financial information contained in other documents. Where the Committee is not satisfied with any aspect of the proposed financial reporting by the company, it shall report its views to the Board.

10.4.1. General

a) To gain an understanding of the current areas of greatest financial risk and how effectively management is managing these.

b) To review significant accounting and reporting policies and issues, including recent professional and regulatory pronouncements, and consider their impact on the financial statements.

10.4.2. Annual report and accounts

a) To review, with both management and the external auditors, the accounting principles, policies and practices adopted in the preparation of the annual financial statements of the group, and the Company's MD&A disclosures, including areas requiring major judgmental considerations, and to review any changes to these principles, policies and practices.

b) To review and challenge whether the Company has followed appropriate accounting standards and made appropriate estimates and judgements, taking into account the views of the external auditor.

c) To satisfy itself that the financial statements meet all relevant statutory requirements, financial reporting standards and accounting practices and the requirements of the stock exchanges where the Company's shares are listed and that there are no unsettled issues of significance between management and the auditors which could affect the accuracy and fairness of the statements.

d) To satisfy itself that the statements on going concern included in the financial statements and the relevant supporting assumptions are soundly based.

e) To provide advice, where requested by the Board, on how, taking into account the Company's position and emerging and principal risks, the prospects of the Company have been assessed, over what period and why the period is regarded as appropriate. Also to provide advice on whether there is a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the chosen period, drawing attention to any qualifications or assumptions as necessary, prior to the Directors making the related 'viability' statement in the Annual Report.

f) To hold discussions with management and the external auditors to ascertain their satisfaction with the results of the completed audit and their views of the adequacy of its scope. To review the principal points raised by the auditors in the "Management Letter" and the management response thereto; to review and discuss with the external auditors material changes to auditing standards.

g) To review the extent to which the financial statements are affected by any unusual transactions in the year and how they are disclosed.

h) To review the methods used to account for significant or unusual transactions where different approaches are possible.

i) To review the clarity of the disclosures in the Company's financial report and the context in which statements are made.

j) To review and challenge all material information presented with the financial statements, such as the strategic report including the non-financial statements and the corporate governance statement, insofar as it relates to the audit and risk management.

k) To review and challenge where necessary the consistency of, and any changes to, significant accounting policies.

10.4.3. Preliminary announcements and interim financial statements

To review the accounting principles, policies and practices adopted in the preparation of the preliminary and interim announcements, significant financial returns to regulators and any financial information contained in certain other documents, such as announcements of a price sensitive nature and obtain explanations from management, Group Internal Audit, and the external auditors as appropriate or required.

10.4.4. Narrative reporting

Where requested by the Board, the Committee should support the Board in concluding whether, taken as a whole, the annual report and accounts are fair, balanced and

understandable and provide the information necessary for shareholders to assess the Company's position and performance, business model and strategy and whether it informs the Board's statement in the annual report on these matters that is required under the Code.

10.4.5. Correspondence with regulators on reporting matters

The Committee will consider all responses to the Company's regulators on reporting matters, liaising with management and the external auditor as appropriate.

10.5. Reporting Responsibilities

10.5.1. The Committee Chair shall report formally to the Board on the Committee's proceedings after each meeting on all matters within its duties and responsibilities and shall make whatever recommendations to the Board it deems appropriate on any area within its remit where action or improvement is needed. The Committee shall also report to the Board on how it has discharged its responsibilities. The report shall include:

a) the significant issues that it considered in relation to the financial statements and how these were addressed;

b) its assessment of the effectiveness of the external audit process, the approach taken to the appointment or reappointment of the external auditor, length of tenure of audit firm, when a tender was last conducted and advanced notice of any retendering plans; and

c) any other issues on which the Board has requested the Committee's opinion.

10.5.2. The Committee shall compile a report to shareholders on its activities to be included in the Company's Annual Report and Accounts. The report should include:

a) the significant issues that the Committee considered in relation to the financial statements and how these issues were addressed, having regard to the matters communicated to it by the auditor;

b) information on any correspondence with the Company's regulators regarding reporting matters, or on any inspections of the external audit of the Company;

c) an explanation of how the Committee has assessed the independence and effectiveness of the external audit process and the approach taken to the appointment or reappointment of the external auditor, information on the length of tenure of the current audit firm, when a tender was last conducted and advance notice of any retendering plans;

d) in the case of a board not accepting the audit committee's recommendation on the external auditor appointment, reappointment or removal, a statement from the audit committee explaining its recommendation and the reasons why the board has taken a different position (this should also be supplied in any papers recommending appointment or reappointment);

e) where there is no internal audit function, an explanation for the absence, how internal assurance is achieved, and how this affects the work of external audit; and

f) an explanation of how auditor independence and objectivity are safeguarded, if the

external auditor provides non-audit services.

10.5.3. In compiling the reports to the Board and shareholders referred to above, the Committee should exercise judgement in deciding which of the issues it considers in relation to the financial statements are significant, but should at least include those matters that have informed the Board's assessment of whether the Company is a going concern and the inputs to the Board's viability statement. The report to shareholders need not repeat information disclosed elsewhere in the annual report and accounts, but could provide cross-references to that information.

10.6. Other Matters

The Committee shall:

10.6.1. have access to sufficient resources in order to carry out its duties, including access to the company secretariat for assistance as required;

10.6.2. be provided with appropriate training, as needed, in the form of an induction programme for new members and on an ongoing basis for all members;

10.6.3. give due consideration to laws and regulations, the provisions of the Code and the requirements of the Financial Conduct Authority's Handbook of rules and guidance, as well as the Sarbanes-Oxley Act and SEC and NYSE requirements in the US and any other applicable rules, as appropriate;

10.6.4. be responsible for the coordination of the internal and external auditors;

10.6.5. oversee any investigation of activities, which are within its charter and terms of reference and act as a court of the last resort;

10.6.6. review other disclosures and documents as determined by the Board;

10.6.7. review in general terms the information to be disclosed in the Company's full year and half year earnings releases, as well as the key messages contained in such releases;

10.6.8. conduct private sessions, periodically, with both Group Internal Audit and the external auditors;

10.6.9. work and liaise as necessary with all other Board committees, taking account of the impact of risk management and internal controls being delegated to different committees;

10.6.10. at least once a year, review its own performance, constitution and charter and terms of reference to ensure it is operating at maximum effectiveness and recommend any changes it considers necessary to the Board for approval; and

10.6.11. review the Company's co-ordinated plans for business continuity and the prevention and detection of fraud, bribery and corruption.

11. Authority

The Committee is authorised:

11.1. to seek any information it requires from any employee of the Company in order to perform its duties;

11.2. to obtain, at the Company's expense, outside legal or other professional advice on any

matters within its charter and terms of reference;

11.3. to call any member of staff to be questioned at a meeting of the Committee as and when required;

11.4. to investigate or commission investigations into any activity within its terms of reference;

11.5. to delegate any of its powers to one or more of its members or the Secretary; and

11.6. to have the right to publish in the Company's annual report details of any issues that cannot be resolved between the Committee and the Board.