Consolidated profit and loss account

year ended 31 Dec 2002

all figures in £ millions	NOTE	2002 RESULTS FROM OPERATIONS	2002 OTHER ITEMS	2002 TOTAL	2001 RESTATED RESULTS FROM OPERATIONS	2001 RESTATED OTHER ITEMS	2001 RESTATED TOTAL
Sales (including share of joint ventures)		4,331	–	4,331	4,240	–	4,240
Less: share of joint ventures		(11)	–	(11)	(15)	–	(15)
Sales	2a	4,320	–	4,320	4,225	–	4,225
Group operating profit		496	(302)	194	444	(424)	20
Share of operating (loss)/profit of joint ventures and associates	2c/d	(3)	(48)	(51)	19	(86)	(67)
Total operating profit/(loss)	2b	493	(350)	143	463	(510)	(47)
Loss on sale of fixed assets and investments	4a	–	(13)	(13)	–	(12)	(12)
Loss on sale of subsidiaries and associates	4b	–	(27)	(27)	–	(63)	(63)
Profit/(loss) on sale of subsidiaries and associates by an associate	4c	–	3	3	–	(53)	(53)
Non operating items		–	(37)	(37)	–	(128)	(128)
Profit/(loss) before interest and taxation		493	(387)	106	463	(638)	(175)
Amounts written off investments		–	–	–	–	(92)	(92)
Net finance costs	5	(94)	(37)	(131)	(169)	–	(169)
(Loss)/profit before taxation		399	(424)	(25)	294	(730)	(436)
Taxation	7	(131)	67	(64)	(100)	133	33
(Loss)/profit after taxation		268	(357)	(89)	194	(597)	(403)
Equity minority interests		(27)	5	(22)	(24)	4	(20)
(Loss)/profit for the financial year		241	(352)	(111)	170	(593)	(423)
Dividends on equity shares	8			(187)			(177)
Loss retained				(298)			(600)
Adjusted earnings per share	9			30.3p			21.4p
Loss per share	9			(13.9)p			(53.2)p
Diluted loss per share	9			(13.9)p			(53.2)p
Dividends per share	8			23.4p			22.3p

There is no difference between the loss before taxation and the retained loss for the year stated above and their historical cost equivalents.

The 2001 comparatives have been restated for the adoption of FRS 19 (see note 21).

Consolidated balance sheet

as at 31 Dec 2002

all figures in £ millions	NOTE	2002	2001 RESTATED
Fixed assets			
Intangible assets	11	**3,610**	4,193
Tangible assets	12	**503**	542
Investments: joint ventures	13		
Share of gross assets		**7**	8
Share of gross liabilities		**–**	(1)
		7	7
Investments: associates	14	**106**	893
Investments: other	15	**84**	84
		4,310	5,719
Current assets			
Stocks	16	**734**	849
Debtors	17	**1,057**	1,005
Deferred taxation	21	**174**	272
Investments		**2**	3
Cash at bank and in hand	18	**575**	393
		2,542	2,522
Creditors – amounts falling due within one year			
Short-term borrowing	19	**(249)**	(165)
Other creditors	20	**(1,114)**	(1,203)
		(1,363)	(1,368)
Net current assets		**1,179**	1,154
Total assets less current liabilities		**5,489**	6,873
Creditors – amounts falling due after more than one year			
Medium and long-term borrowing	19	**(1,734)**	(2,607)
Other creditors	20	**(60)**	(54)
		(1,794)	(2,661)
Provisions for liabilities and charges	22	**(165)**	(239)
Net assets		**3,530**	3,973
Capital and reserves			
Called up share capital	23	**200**	200
Share premium account	24	**2,465**	2,459
Profit and loss account	24	**673**	1,138
Equity shareholders' funds		**3,338**	3,797
Equity minority interests		**192**	176
		3,530	3,973

The 2001 comparatives have been restated for the adoption of FRS 19 (see note 21).

The company balance sheet is shown in note 32.

The financial statements were approved by the board of directors on 3 March 2003 and signed on its behalf by

DENNIS STEVENSON ‣ RONA FAIRHEAD

Consolidated statement of cash flows

year ended 31 Dec 2002

all figures in £ millions	NOTE	2002	2001
Net cash inflow from operating activities	27	**529**	490
Dividends from joint ventures and associates		**6**	25
Interest received		**11**	31
Interest paid		**(151)**	(187)
Debt issue costs		**–**	(1)
Dividends paid to minority interests		**(1)**	(9)
Returns on investments and servicing of finance		**(141)**	(166)
Taxation		**(55)**	(71)
Purchase of tangible fixed assets		**(126)**	(165)
Sale of tangible fixed assets		**7**	36
Purchase of investments		**(21)**	(35)
Sale of investments		**3**	22
Capital expenditure and financial investment		**(137)**	(142)
Purchase of subsidiaries	25	**(87)**	(128)
Net cash acquired with subsidiaries		**1**	83
Purchase of joint ventures and associates		**(40)**	(26)
Sale of subsidiaries	26	**3**	41
Net cash disposed with subsidiaries		**(1)**	–
Sale of associates	14	**920**	1
Acquisitions and disposals		**796**	(29)
Equity dividends paid		**(181)**	(174)
Net cash inflow/(outflow) before management of liquid resources and financing		**817**	(67)
Liquid resources acquired		**(65)**	(48)
Collateral deposit reimbursed		**22**	47
Management of liquid resources	27	**(43)**	(1)
Issue of equity share capital		**6**	20
Capital element of finance leases		**(5)**	(7)
Loan facility repaid		**(507)**	(521)
Bonds (repaid)/advanced		**(167)**	507
Collateral deposit reimbursed		**17**	–
Net movement in other borrowings		**(7)**	3
Financing		**(663)**	2
Increase/(decrease) in cash in the year	27	**111**	(66)

Statement of total recognised gains and losses

year ended 31 Dec 2002

all figures in £ millions	NOTE	**2002**	2001 RESTATED
Loss for the financial year		**(111)**	(423)
Other net gains and losses recognised in reserves:			
Currency translation differences		**(317)**	26
Taxation on currency translation differences		**5**	(6)
Total recognised gains and losses relating to the year		**(423)**	(403)
Prior year adjustment – FRS 19	21	**209**	
Total recognised gains and losses		**(214)**	

Reconciliation of movements in equity shareholders' funds

year ended 31 Dec 2002

all figures in £ millions	**2002**	2001 RESTATED
Loss for the financial year	**(111)**	(423)
Dividends on equity shares	**(187)**	(177)
	(298)	(600)
Currency translation differences (net of taxation)	**(312)**	20
Goodwill written back on sale of subsidiaries and associates	**144**	37
Goodwill written back on sale of subsidiaries and associates by an associate	**–**	36
Shares issued	**6**	18
Replacement options granted on acquisition of subsidiary	**1**	2
Net movement for the year	**(459)**	(487)
Equity shareholders' funds at beginning of the year	**3,797**	4,044
Prior period adjustment – FRS 19	**–**	240
Equity shareholders' funds at end of the year	**3,338**	3,797

Independent auditors' report to the members of Pearson plc

We have audited the financial statements which comprise the consolidated profit and loss account, the consolidated balance sheet, the consolidated statement of cash flows, the statement of total recognised gains and losses, the reconciliation of movements in equity shareholders' funds and the related notes. We have also audited the disclosures required by Part 3 of Schedule 7a to the Companies Act 1985, contained in the report on directors' remuneration ('the auditable part').

Respective responsibilities of directors and auditors ▸ The directors' responsibilities for preparing the annual report, the report on directors' remuneration, and the financial statements in accordance with applicable United Kingdom law and accounting standards are set out in the statement of directors' responsibilities.

Our responsibility is to audit the financial statements and the auditable part of the report on directors' remuneration in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards issued by the Auditing Practices Board. This report, including the opinion, have been prepared for and only for, the company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come, save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the auditable part of the report on directors' remuneration have been properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions is not disclosed.

We read the other information contained in the annual report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. The other information comprises only the financial highlights, the chairman's statement, the chief executive's review, the 'Pearson goals' section, the 'business highlights' section, the operating review, the financial review, the board of directors, the directors' report and the unaudited part of the report on directors' remuneration.

We review whether the corporate governance statement within the directors' report reflects the group's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or to form an opinion on the effectiveness of the company's or group's corporate governance procedures or its risk and control procedures.

Basis of audit opinion ▸ We conducted our audit in accordance with auditing standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the auditable part of the report on directors' remuneration. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements and the auditable part of the report on directors' remuneration are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion ▸ In our opinion

- the financial statements give a true and fair view of the state of affairs of the company and the group at 31 December 2002 and the result and cash flows of the group for the year then ended;
- the financial statements have been properly prepared in accordance with the Companies Act 1985; and
- those parts of the report on directors' remuneration required by Part 3 of Schedule 7a to the Companies Act 1985 have been properly prepared in accordance with the Companies Act 1985.

PRICEWATERHOUSECOOPERS LLP ▸ CHARTERED ACCOUNTANTS AND REGISTERED AUDITORS ▸ LONDON 3 MARCH 2003

Notes

The maintenance and integrity of the Pearson Plc website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Index to the financial statements

Notes to the accounts

1 ACCOUNTING POLICIES

Accounting policies have been consistently applied except that FRS 19 'Deferred tax' has been adopted and hence comparative figures have been restated. The effect of this change in accounting policy is disclosed in note 21. The transitional arrangements of FRS 17 'Retirement benefits' have been adopted which require additional disclosures in respect of retirement benefits, as set out in note 10.

a. Basis of accounting ‣ The accounts are prepared under the historical cost convention and in accordance with the Companies Act and applicable accounting standards. A summary of the significant accounting policies is set out below.

b. Basis of consolidation ‣ The consolidated accounts include the accounts of all subsidiaries made up to 31 December. Where companies have become or ceased to be subsidiaries or associates during the year, the Group results include results for the period during which they were subsidiaries or associates.

The results of the Group includes the Group's share of the results of joint ventures and associates, and the consolidated balance sheet includes the Group's interest in joint ventures and associates at the book value of attributable net assets and attributable goodwill.

c. Goodwill ‣ From 1 January 1998 goodwill, being either the net excess of the cost of shares in subsidiaries, joint ventures and associates over the value attributable to their net assets on acquisition or the cost of other goodwill by purchase, is capitalised and amortised through the profit and loss account on a straight-line basis over its estimated useful life not exceeding 20 years. Estimated useful life is determined after taking into account such factors as the nature and age of the business and the stability of the industry in which the acquired business operates, as well as typical life spans of the acquired products to which the goodwill attaches. Goodwill is subject to an impairment review at the end of the first full year following an acquisition, and at any other time if events or changes in circumstances indicate that the carrying value may not be recoverable. Goodwill arising on acquisitions before 1 January 1998 has been deducted from reserves and is charged or credited to the profit and loss account on disposal or closure of the business to which it relates.

d. Sales ‣ Sales represent the amount of goods and services, net of value added tax and other sales taxes, and excluding trade discounts and anticipated returns, provided to external customers and associates.

Revenue from the sale of books is recognised when the goods are shipped. Anticipated returns are based primarily on historical return rates. Circulation and advertising revenue is recognised when the newspaper or other publication is published. Subscription revenue is recognised on a straight-line basis over the life of the subscription.

Revenue from long-term contracts, such as contracts to process qualifying tests for individual professions and government departments, is recognised over the contract term based on the percentage of services provided during the period, compared to the total estimated services to be provided over the entire contract. Losses on contracts are recognised in the period in which the loss first becomes probable and reasonably estimable. Contract losses are determined to be the amount by which estimated direct and indirect costs of the contract exceed the estimated total revenues that will be generated by the contract.

e. Pension costs ‣ The regular pension cost of the Group's defined benefit pension schemes is charged to the profit and loss account in order to apportion the cost of pensions over the service lives of employees in the schemes. Variations arising from a significant reduction in the number of employees are adjusted in the profit and loss account to the extent that the year's regular pension cost, reduced by other variations, exceeds contributions payable for that year. Other variations are apportioned over the expected service lives of current employees in the schemes. The pension cost of the Group's defined contribution schemes is the amount of contributions payable for the year.

f. Post-retirement benefits other than pensions ‣ Post-retirement benefits other than pensions are accounted for on an accruals basis to recognise the obligation over the expected service lives of the employees concerned.

g. Tangible fixed assets ‣ The cost of tangible fixed assets other than freehold land is depreciated over estimated economic lives in equal annual amounts. Generally, freeholds are depreciated at 1% to 5% per annum, leaseholds at 2% per annum, or over the period of the lease if shorter, and plant and equipment at various rates between 5% and 33% per annum.

h. Leases ‣ Finance lease rentals are capitalised at the net present value of the total amount of rentals payable under the leasing agreement (excluding finance charges) and depreciated in accordance with policy g above. Finance charges are written off over the period of the lease in reducing amounts in relation to the written down carrying cost. Operating lease rentals are expensed as incurred.

i. Fixed asset investments ‣ Fixed asset investments are stated at cost less provisions for diminution in value.

j. Share schemes ▸ Shares held by employee share ownership trusts are shown at cost less any provision for permanent diminution in value. The costs of funding and administering the trusts are charged to the profit and loss account in the period to which they relate. The cost of shares acquired by the trusts or the fair market value of the shares at the date of the grant, less any consideration to be received from the employee, is charged to the profit and loss account over the period to which the employee's performance relates. Where awards are contingent upon future events (other than continued employment) an assessment of the likelihood of these conditions being achieved is made at the end of each reporting period and an appropriate provision made.

k. Stocks ▸ Stocks and work in progress are stated at the lower of cost and net realisable value.

l. Pre-publication costs ▸ Pre-publication costs represent direct costs incurred in the development of titles prior to their publication. These costs are carried forward in stock where the title to which they relate has a useful life in excess of one year. These costs are amortised upon publication of the title over estimated economic lives of five years or less, being an estimate of the expected life cycle of the title, with a higher proportion of the amortisation taken in the earlier years.

m. Royalty advances ▸ Advances of royalties to authors are included within debtors when the advance is paid less any provision required to bring the amount down to its net realisable value. The royalty advance is expensed at the contracted royalty rate as the related revenues are earned.

n. Newspaper development costs ▸ Revenue investment in the development of newspaper titles consists of measures to increase the volume and geographical spread of circulation. These measures include additional and enhanced editorial content, extended distribution and remote printing. These extra costs arising are expensed as incurred.

o. Deferred taxation ▸ Provision is made in full for deferred tax that arises from timing differences that have originated but not reversed by the balance sheet date on transactions or events that result in an obligation to pay more tax in the future. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that there will be taxable profits from which the underlying timing differences can be deducted. Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the timing differences are expected to reverse, based on tax rates and laws that have been enacted or substantially enacted by the balance sheet date. Deferred tax assets and liabilities are not discounted. No deferred tax is provided in respect of any future remittance of earnings of foreign subsidiaries or associates where no commitment has been made to remit such earnings.

p. Financial instruments ▸ The Group uses derivative financial instruments to manage its exposure to interest rate and foreign exchange risks. These include interest rate swaps, currency swaps and forward currency contracts. Amounts payable or receivable in respect of interest rate derivatives are accrued with net interest payable over the period of the contract. Where the derivative instrument is terminated early, the gain or loss is spread over the remaining maturity of the original instrument. Where the underlying exposure ceases to exist, any termination gain or loss is taken to the profit and loss account. Foreign currency borrowings and their related derivatives are carried in the balance sheet at the relevant exchange rates at the balance sheet date. Gains or losses in respect of the hedging of overseas subsidiaries are taken to reserves. Gains or losses arising from foreign exchange contracts are taken to the profit and loss account in line with the transactions which they are hedging. Premiums paid on contracts designed to manage currency exposure on specific acquisitions or disposals are charged to the profit and loss account.

The company participates in offset arrangements with certain banks whereby cash and overdraft amounts are offset against each other.

q. Foreign currencies ▸ Profit and loss accounts in overseas currencies are translated into sterling at average rates. Balance sheets are translated into sterling at the rates ruling at 31 December. Exchange differences arising on consolidation are taken directly to reserves. Other exchange differences are taken to the profit and loss account where they relate to trading transactions and directly to reserves where they relate to investments.

The principal overseas currency for the Group is the US dollar. The average rate for the year against sterling was $1.51 (2001: $1.44) and the year end rate was $1.61 (2001: $1.46).

r. Liquid resources ▸ Liquid resources comprise short-term deposits of less than one year and investments which are readily realisable and held on a short-term basis.

s. Retained profits of overseas subsidiaries and associates ▸ No provision is made for any additional taxation, less double taxation relief, which would arise on the remittance of profits retained where there is no intention to remit such profits.

2a ANALYSIS OF SALES

all figures in £ millions	2002 Sales before internet enterprises	2002 Internet enterprises	2002 Sales	2001 Sales before internet enterprises	2001 Internet enterprises	2001 Sales
Business sectors						
Pearson Education	2,752	4	2,756	2,596	8	2,604
FT Group	678	48	726	750	51	801
The Penguin Group	838	–	838	820	–	820
Continuing operations	4,268	52	4,320	4,166	59	4,225
Geographical markets supplied						
United Kingdom	395	16	411	423	10	433
Continental Europe	413	6	419	438	8	446
North America	3,110	29	3,139	2,936	39	2,975
Asia Pacific	248	1	249	239	2	241
Rest of world	102	–	102	130	–	130
Continuing operations	4,268	52	4,320	4,166	59	4,225

all figures in £ millions	2002 Total by source	2002 Inter-regional	2002 Total sales	2001 Total by source	2001 Inter-regional	2001 Total sales
Geographical source of sales						
United Kingdom	644	(25)	619	686	(20)	666
Continental Europe	304	(4)	300	315	(5)	310
North America	3,144	(36)	3,108	2,976	(35)	2,941
Asia Pacific	226	(2)	224	221	(6)	215
Rest of world	69	–	69	93	–	93
Continuing operations	4,387	(67)	4,320	4,291	(66)	4,225

note ▸ The table above analyses sales by the geographical region from which the products and services originate. Inter-regional sales are those made between Group companies in different regions.

2b ANALYSIS OF TOTAL OPERATING PROFIT/(LOSS)

all figures in £ millions	2002 Results from operations before internet enterprises	2002 Internet enterprises	2002 Results from operations	2002 Integration costs	2002 Goodwill amortisation	2002 Goodwill impairment	2002 Operating profit
Business sectors							
Pearson Education	351	(25)	326	(7)	(244)	–	75
FT Group	114	(34)	80	–	(65)	(10)	5
The Penguin Group	87	–	87	(3)	(18)	–	66
Continuing operations	552	(59)	493	(10)	(327)	(10)	146
Discontinued operations	–	–	–	–	(3)	–	(3)
	552	(59)	493	(10)	(330)	(10)	143

2b ANALYSIS OF OPERATING PROFIT/(LOSS) CONTINUED

all figures in £ millions	2002						
	RESULTS FROM OPERATIONS BEFORE INTERNET ENTERPRISES	**INTERNET ENTERPRISES**	**RESULTS FROM OPERATIONS**	**INTEGRATION COSTS**	**GOODWILL AMORTISATION**	**GOODWILL IMPAIRMENT**	**OPERATING PROFIT**
Geographical markets supplied							
United Kingdom	(37)	(35)	(72)	(5)	(25)	–	(102)
Continental Europe	41	(1)	40	–	(8)	–	32
North America	518	(23)	495	(5)	(288)	–	202
Asia Pacific	31	–	31	–	(6)	–	25
Rest of world	(1)	–	(1)	–	–	(10)	(11)
Continuing operations	552	(59)	493	(10)	(327)	(10)	146
Discontinued operations	–	–	–	–	(3)	–	(3)
	552	(59)	493	(10)	(330)	(10)	143

all figures in £ millions	2001 RESTATED						
	RESULTS FROM OPERATIONS BEFORE INTERNET ENTERPRISES	INTERNET ENTERPRISES	RESULTS FROM OPERATIONS	INTEGRATION COSTS	GOODWILL AMORTISATION	GOODWILL IMPAIRMENT	OPERATING LOSS
Business sectors							
Pearson Education	351	(77)	274	(29)	(254)	(8)	(17)
FT Group	132	(60)	72	–	(67)	(3)	2
The Penguin Group	80	–	80	(45)	(19)	(50)	(34)
Continuing operations	563	(137)	426	(74)	(340)	(61)	(49)
Discontinued operations	37	–	37	–	(35)	–	2
	600	(137)	463	(74)	(375)	(61)	(47)
Geographical markets supplied							
United Kingdom	16	(53)	(37)	(33)	(27)	(55)	(152)
Continental Europe	55	(10)	45	–	(6)	–	39
North America	470	(73)	397	(41)	(302)	(3)	51
Asia Pacific	24	–	24	–	(4)	–	20
Rest of world	(2)	(1)	(3)	–	(1)	(3)	(7)
Continuing operations	563	(137)	426	(74)	(340)	(61)	(49)
Discontinued operations	37	–	37	–	(35)	–	2
	600	(137)	463	(74)	(375)	(61)	(47)

note ‣ Internet enterprises consist of the Group's discrete internet operations, including FT.com and Family Education Network. Integration costs in 2002 and 2001 include costs in respect of the Dorling Kindersley and National Computer Systems acquisitions. In 2002, of the goodwill impairment charge, £10m (2001: £58m) relates to the impairment of goodwill arising on acquisition of subsidiaries (see note 11) and £nil (2001: £3m) relates to the impairment of goodwill arising on acquisition of associates. Integration costs, goodwill amortisation and goodwill impairment are included as other items in the profit and loss account. Discontinued operations relate to the withdrawal of the Group from the television business following the disposal of its 22% interest in the RTL Group on 30 January 2002.

2c SHARE OF OPERATING LOSS OF JOINT VENTURES

all figures in £ millions	RESULTS FROM OPERATIONS BEFORE INTERNET ENTERPRISES	INTERNET ENTERPRISES	RESULTS FROM OPERATIONS	INTEGRATION COSTS	GOODWILL AMORTISATION	GOODWILL IMPAIRMENT	OPERATING LOSS
2002							
Pearson Education	(1)	–	(1)	–	–	–	(1)
FT Group	(13)	–	(13)	–	–	–	(13)
The Penguin Group	1	–	1	–	–	–	1
	(13)	–	(13)	–	–	–	(13)

all figures in £ millions	RESULTS FROM OPERATIONS BEFORE INTERNET ENTERPRISES	INTERNET ENTERPRISES	RESULTS FROM OPERATIONS	INTEGRATION COSTS	GOODWILL AMORTISATION	GOODWILL IMPAIRMENT	OPERATING LOSS
2001							
Pearson Education	–	–	–	–	–	–	–
FT Group	(20)	–	(20)	–	–	–	(20)
The Penguin Group	1	–	1	–	–	–	1
	(19)	–	(19)	–	–	–	(19)

2d SHARE OF OPERATING LOSS OF ASSOCIATES

all figures in £ millions	RESULTS FROM OPERATIONS BEFORE INTERNET ENTERPRISES	INTERNET ENTERPRISES	RESULTS FROM OPERATIONS	INTEGRATION COSTS	GOODWILL AMORTISATION	GOODWILL IMPAIRMENT	OPERATING LOSS
2002							
Pearson Education	3	–	3	–	(1)	–	2
FT Group	10	(3)	7	–	(44)	–	(37)
The Penguin Group	–	–	–	–	–	–	–
Continuing operations	13	(3)	10	–	(45)	–	(35)
Discontinued operations	–	–	–	–	(3)	–	(3)
	13	(3)	10	–	(48)	–	(38)

all figures in £ millions	RESULTS FROM OPERATIONS BEFORE INTERNET ENTERPRISES	INTERNET ENTERPRISES	RESULTS FROM OPERATIONS	INTEGRATION COSTS	GOODWILL AMORTISATION	GOODWILL IMPAIRMENT	OPERATING LOSS
2001							
Pearson Education	3	–	3	–	(1)	(3)	(1)
FT Group	8	(10)	(2)	–	(47)	–	(49)
The Penguin Group	–	–	–	–	–	–	–
Continuing operations	11	(10)	1	–	(48)	(3)	(50)
Discontinued operations	37	–	37	–	(35)	–	2
	48	(10)	38	–	(83)	(3)	(48)

2e ANALYSIS OF CAPITAL EMPLOYED

all figures in £ millions	NOTE	2002	2001 RESTATED
Business sectors			
Pearson Education		**3,914**	4,628
FT Group		**410**	427
The Penguin Group		**605**	501
Continuing operations		**4,929**	5,556
Discontinued operations		**–**	763
		4,929	6,319
Geographical location			
United Kingdom		**557**	516
Continental Europe		**258**	243
North America		**3,971**	4,628
Asia Pacific		**125**	139
Rest of world		**18**	30
Continuing operations		**4,929**	5,556
Discontinued operations		**–**	763
		4,929	6,319
Reconciliation of capital employed to net assets			
Capital employed		**4,929**	6,319
Add: deferred taxation	21	**174**	272
Less: provisions for liabilities and charges	22	**(165)**	(239)
Less: net debt excluding finance leases	27	**(1,408)**	(2,379)
Net assets		**3,530**	3,973

3 ANALYSIS OF CONSOLIDATED PROFIT AND LOSS ACCOUNT

all figures in £ millions	2002	2001 RESTATED
Cost of sales	**(2,064)**	(1,902)
Gross profit	**2,256**	2,323
Distribution costs	**(197)**	(200)
Administration and other expenses	**(1,924)**	(2,169)
Other operating income	**59**	66
Net operating expenses	**(2,062)**	(2,303)
Analysed as:		
Net operating expenses – before other items	**(1,760)**	(1,879)
Net operating expenses – other items:		
– Integration costs	**(10)**	(74)
– Goodwill amortisation	**(282)**	(292)
– Goodwill impairment	**(10)**	(58)
Net operating expenses	**(2,062)**	(2,303)

note ‣ Other items are all included in administration and other expenses.

3 ANALYSIS OF CONSOLIDATED PROFIT AND LOSS ACCOUNT CONTINUED

all figures in £ millions	**2002**	2001
Other operating income		
Income from other investments:		
Unlisted	**2**	2
Other operating income (mainly royalties, rights and commission income)	**57**	64
	59	66
Loss before taxation is stated after charging:		
Amortisation of pre-publication costs	**170**	161
Depreciation	**122**	125
Operating lease rentals:		
– Plant and machinery	**11**	31
– Properties	**101**	99
– Other	**13**	17
Auditors' remuneration:		
Audit (Company £20,000; 2001: £20,000)	**3**	2
Non-audit – UK (Company £231,000; 2001: £nil)	**1**	2
Non-audit – Overseas	**2**	3
Non-audit services were as follows:		
US reporting, due diligence and other related work	**1**	2
Taxation advice	**2**	1
Acquisition related work	**–**	2
	3	5

note ▸ There were no fees capitalised in 2002 or 2001.

4a LOSS ON SALE OF FIXED ASSETS AND INVESTMENTS

all figures in £ millions	**2002**	2001
Net loss on sale of property	**(3)**	(2)
Net loss on sale of investments	**(10)**	(10)
Continuing operations	**(13)**	(12)
Taxation	**6**	1

4b LOSS ON SALE OF SUBSIDIARIES AND ASSOCIATES

all figures in £ millions	NOTE	**2002**	2001 RESTATED
Loss on sale of Forum		**(40)**	–
Loss on sale of PH Direct		**(8)**	–
Loss on sale of iForum		**–**	(27)
Net profit/(loss) on sale of other subsidiaries and associates		**3**	(36)
Continuing operations		**(45)**	(63)
Profit on sale of the RTL Group – discontinued operations	14	**18**	–
		(27)	(63)
Taxation		**(6)**	4

4c PROFIT/(LOSS) ON SALE OF SUBSIDIARIES AND ASSOCIATES BY AN ASSOCIATE

all figures in £ millions	2002	2001
Profit/(loss) on sale of Journal of Commerce by the Economist – continuing operations	3	(36)
Loss on sale of subsidiaries and associates by the RTL Group – discontinued operations	–	(17)
	3	(53)

5 NET FINANCE COSTS

all figures in £ millions	NOTE	2002 RESULTS FROM OPERATIONS	2002 OTHER ITEMS	2002 TOTAL	2001 RESULTS FROM OPERATIONS	2001 OTHER ITEMS	2001 TOTAL
Net interest payable							
– Group	6	(94)	–	(94)	(163)	–	(163)
– Associates		–	–	–	(6)	–	(6)
Early repayment of debt and termination of swap contracts		–	(37)	(37)	–	–	–
Total net finance costs		(94)	(37)	(131)	(169)	–	(169)

6 NET INTEREST PAYABLE – GROUP

all figures in £ millions	2002	2001
Interest payable and similar charges:		
Bank loans, overdrafts and commercial paper		
On borrowing repayable wholly within five years not by instalments	(54)	(100)
On borrowing repayable wholly or partly after five years	(51)	(72)
Other borrowings		
On borrowing repayable wholly within five years not by instalments	–	(16)
	(105)	(188)
Interest receivable and similar income:		
On deposits and liquid funds	11	23
Amortisation of swap proceeds	–	2
	11	25
Net interest payable	(94)	(163)

7 TAXATION

all figures in £ millions	NOTE	2002	2001 RESTATED
Analysis of benefit/(charge) in the year:			
Current taxation			
UK corporation tax for the year		**11**	(28)
Adjustments in respect of prior periods		**58**	147
		69	119
Overseas tax for the year		**(63)**	(43)
Joint ventures		**–**	(6)
Associates		**(4)**	(9)
		2	61
Deferred taxation			
Origination and reversal of timing differences:			
UK		**(11)**	4
Overseas		**(56)**	(32)
Adjustments in respect of prior periods		**1**	–
	21	**(66)**	(28)
Taxation		**(64)**	33

The tax for the year is different than the standard rate of corporation tax in the UK (30%). The differences are explained below:

all figures in £ millions	2002	2001 RESTATED
Loss before tax	**(25)**	(436)
Expected benefit at UK corporation tax rate of 30% (2001: 30%)	**8**	131
Effect of overseas tax rates	**11**	37
Effect of tax losses	**(7)**	(1)
Other timing differences	**55**	(98)
Non-deductible goodwill amortisation	**(111)**	(149)
US state taxes	**(10)**	(6)
Adjustments in respect of prior periods	**56**	147
Current tax benefit for the year	**2**	61

all figures in percentages	2002	2001 RESTATED
Tax rate reconciliation		
UK tax rate	**30.0**	30.0
Effect of overseas tax rates	**2.8**	4.5
Other items	**–**	(0.5)
Tax rate reflected in adjusted earnings	**32.8**	34.0

note ▸ Included in the adjustment in respect of prior periods in 2002 is a tax benefit of £45m (2001: £143m) relating to a prior period disposal of a subsidiary and a fixed asset investment.

Both the current and the total tax charge on profit (or loss) before tax will continue to be affected by the fact that there is only very limited tax relief available on the goodwill amortisation charged in the accounts.

The current tax charge will continue to be affected by the utilisation of tax losses and by the impact of other timing differences, in both cases mainly in the United States. Following the adoption of FRS 19 these factors will have only a very limited impact on the total tax rate; as shown in note 21, the Group has recognised a total deferred tax asset of £174m at 31 December 2002 (2001: £272m).

In both 2002 and 2001 the tax charge was materially affected by prior year adjustments; it is not practicable to forecast the possible effect of such items in future years as this will depend on progress in agreeing the Group's tax returns with the tax authorities.

The total charge in future periods will also be affected by any changes to corporation tax rates and/or any other relevant legislative changes in the jurisdictions in which the Group operates. It will also be affected by the mix of profits between the different jurisdictions.

8 DIVIDENDS ON EQUITY SHARES

	2002		2001	
	PENCE PER SHARE	£m	PENCE PER SHARE	£m
Interim paid	9.1	72	8.7	68
Final proposed	14.3	115	13.6	109
Dividends for the year	23.4	187	22.3	177

note ▸ Dividends in respect of the company's shares held by employee share trusts (see note 15) have been waived.

9 EARNINGS/(LOSS) PER SHARE

In order to show results from operating activities on a comparable basis, an adjusted earnings per share is presented which excludes certain items as set out below. The company's definition of adjusted earnings per share may not be comparable to other similarly titled measures reported by other companies.

		2002		2001 RESTATED	
	NOTE	£m	EARNINGS/(LOSS) PER SHARE (P)	£m	EARNINGS/(LOSS) PER SHARE (P)
Loss for the financial year		(111)	(13.9)	(423)	(53.2)
Adjustments:					
– Non operating items		37	4.6	128	16.1
– Integration costs	2b	10	1.3	74	9.3
– Goodwill amortisation	2b	330	41.4	375	47.1
– Goodwill impairment	2b	10	1.3	61	7.7
– Amounts written off investments		–	–	92	11.6
– Other net finance costs	5	37	4.6	–	–
Taxation on above items		(67)	(8.4)	(133)	(16.7)
Minority interest share of above items		(5)	(0.6)	(4)	(0.5)
Adjusted earnings		241	30.3	170	21.4
Weighted average number of shares (millions) – for earnings and adjusted earnings		796.3		795.4	
Effect of dilutive share options		–		–	
Weighted average number of shares (millions) – for diluted loss		796.3		795.4	

note ▸ In 2002 and 2001 the Group made a loss for the financial year (after taking into account goodwill amortisation), consequently the effect of share options is anti-dilutive and there is no difference between the loss per share and the diluted loss per share.

10a EMPLOYEE INFORMATION

The details of the emoluments of the directors of Pearson plc are shown on pages 46 to 60 and form part of these audited financial statements.

all figures in £ millions	**2002**	2001
Staff costs		
Wages and salaries	**1,106**	1,090
Social security costs	**106**	104
Post-retirement costs	**59**	39
	1,271	1,233

	UK	US	OTHER	TOTAL
Average number employed 2002				
Pearson Education	**1,326**	**14,459**	**4,250**	**20,035**
FT Group	**1,914**	**1,140**	**2,169**	**5,223**
The Penguin Group	**1,305**	**2,167**	**890**	**4,362**
Other	**204**	**534**	**1**	**739**
	4,749	**18,300**	**7,310**	**30,359**
Average number employed 2001				
Pearson Education	1,505	12,610	4,344	18,459
FT Group	2,075	1,121	2,340	5,536
The Penguin Group	1,333	2,293	768	4,394
Other	193	444	1	638
	5,106	16,468	7,453	29,027

10b PENSIONS

The Group operates a number of pension schemes throughout the world, the principal ones being in the UK and US. The major schemes are self-administered with the schemes' assets being held independently of the Group. Pension costs are assessed in accordance with the advice of independent qualified actuaries. The UK is a hybrid scheme with both defined benefit and defined contribution sections but, predominantly consisting of defined benefit liabilities. There are a number of defined contribution schemes, principally overseas. The cost of the schemes is as follows:

all figures in £ millions	**2002**	2001
UK Group scheme		
Regular pension cost		
– Defined benefit sections	**11**	9
– Defined contribution sections	**7**	6
Amortisation of surplus	**–**	(5)
	18	10
Other schemes		
Defined benefit schemes	**6**	11
Defined contribution schemes	**30**	14
	36	25
	54	35

note ▸ During 2001, the main defined benefit scheme for US employees was closed to the majority of active members. The UK Group scheme will only offer defined contribution benefits to new joiners from 1 January 2003. The changes to these schemes will give rise to a reduction in defined benefit and an increase in defined contribution costs, the impact taking effect in 2002 in the US and 2003 in the UK.

Included in note 22, there is a pension provision of £36m (2001: £61m) as measured in accordance with SSAP 24.

10b PENSIONS CONTINUED

The most recent full actuarial valuation of the UK Group scheme was performed as at 1 January 2001, using the projected unit method of valuation. It is this valuation that Pearson uses to determine its cash contributions with the goal of remaining fully funded. The market value of the assets of the scheme at this date was £1,166m. The major assumptions used to determine the SSAP 24 charge and level of funding are as follows:

all figures in percentages	UK GROUP SCHEME
Inflation	3.0
Rate of increase in salaries	5.0
Rate of increase for pensions in payment and deferred pensions	3.0
Return on investments	7.0
Rate of increase in dividends	4.3
Level of funding	104.0

The funding policy differs from the accounting policy to the extent that more conservative assumptions are used for funding purposes. The SSAP 24 funding level of 104% is based on the last formal valuation of the UK Group scheme at 1 January 2001. However, the UK Group scheme actuaries have estimated that the surplus arising at 1 January 2001 had been substantially eliminated by 1 January 2002, primarily due to adverse market movements in 2001. The Group has therefore not recognised any amortisation of the surplus for the year ended 31 December 2002. The next full triennial valuation is due to take place in January 2004.

The date of the most recent valuation of the US plan was 31 December 2001.

The disclosures required under the transitional arrangements of FRS 17 for the Group's defined benefit schemes and the UK Group hybrid scheme are set out below. The disclosures for the UK Group hybrid scheme are in respect of both the defined benefit and defined contribution sections.

For the purpose of these disclosures, the valuations of the UK Group scheme and other schemes have been updated by independent actuaries to 31 December 2002. The assumptions used are shown below. Weighted average assumptions have been shown for the other schemes.

	2002		2001	
all figures in percentages	**UK GROUP SCHEME**	**OTHER SCHEMES**	UK GROUP SCHEME	OTHER SCHEMES
Inflation	**2.25**	**3.00**	2.50	3.00
Rate of increase in salaries	**4.25**	**4.50**	4.50	4.50
Rate of inflation linked increase for pensions in payment and deferred pensions	**2.25**	**–**	2.50	–
Rate used to discount scheme liabilities	**5.70**	**6.75**	6.00	7.20

The assets of the UK Group scheme and the expected rate of return on these assets, and the assets of the other defined benefit schemes and the expected rate of return on these assets shown as a weighted average, are as follows:

	UK GROUP SCHEME			
	LONG-TERM RATE OF RETURN EXPECTED AT 31 DEC 2002 %	**VALUE AT 31 DEC 2002 £m**	LONG-TERM RATE OF RETURN EXPECTED AT 31 DEC 2001 %	VALUE AT 31 DEC 2001 £m
Equities	**8.00**	**472**	7.50	657
Bonds	**4.75**	**284**	5.30	293
Properties	**6.50**	**112**	6.30	102
Other	**6.50**	**108**	6.30	42
Total market value of assets		**976**		1,094
Present value of scheme liabilities		**(1,189)**		(1,167)
Deficit in the scheme		**(213)**		(73)
Related deferred tax asset		**64**		22
Net pension liability		**(149)**		(51)

10b PENSIONS CONTINUED

	OTHER SCHEMES			
	LONG-TERM RATE OF RETURN EXPECTED AT 31 DEC 2002 %	VALUE AT 31 DEC 2002 £m	LONG-TERM RATE OF RETURN EXPECTED AT 31 DEC 2001 %	VALUE AT 31 DEC 2001 RESTATED £m
Equities	9.75	33	9.50	37
Bonds	6.00	23	6.50	24
Other	2.75	1	–	–
Total market value of assets		57		61
Present value of scheme liabilities		(96)		(95)
Deficit in the schemes		(39)		(34)
Related deferred tax asset		14		12
Net pension liability		(25)		(22)

note ▸ The measurement of the deficit in the scheme for FRS 17 follows a different approach to SSAP 24. The FRS 17 measurement date is 31 December 2002. The fall in stock markets in 2002 reduced the market value of the UK Group scheme assets and the fall in bond yields (the discount rate) has acted to increase the present value of the UK Group scheme liabilities. This has resulted in an increased deficit in the UK Group scheme under FRS 17.

all figures in £ millions	UK GROUP SCHEME	DEFINED BENEFIT OTHER	TOTAL	DEFINED CONTRIBUTION	TOTAL
Operating charge					
Current service cost	(19)	(3)	(22)	(30)	(52)
Past service cost	–	(1)	(1)	–	(1)
Total operating charge	(19)	(4)	(23)	(30)	(53)
Other finance income/(charge)					
Expected return on pension scheme assets	73	5	78	–	78
Interest on pension scheme liabilities	(68)	(6)	(74)	–	(74)
Net income/(charge)	5	(1)	4	–	4
Net profit and loss impact	(14)	(5)	(19)	(30)	(49)
Statement of total recognised gains and losses					
Actual return less expected return on pension scheme assets	(165)	(11)	(176)		
Experience gains and (losses) arising on the scheme liabilities	17	(1)	16		
Changes in assumptions underlying the present value of the scheme liabilities	3	(4)	(1)		
Exchange differences	–	2	2		
Actuarial loss	(145)	(14)	(159)		
Movement in deficit during the year					
Deficit in scheme at beginning of the year	(73)	(34)	(107)		
Current service cost	(19)	(3)	(22)		
Past service cost	–	(1)	(1)		
Contributions	19	14	33		
Other finance income/(charge)	5	(1)	4		
Actuarial loss	(145)	(14)	(159)		
Deficit in scheme at end of the year	(213)	(39)	(252)		
Related deferred tax asset	64	14	78		
Net pension deficit	(149)	(25)	(174)		

The contribution rate for 2002 for the UK Group scheme was 17.1% of pensionable salaries. It has been agreed with the Trustees that the contribution rate for 2003 will be 17.1% of pensionable salaries plus a one-off contribution of £5m. This is designed to ensure that the UK Group scheme is fully funded.

10b PENSIONS CONTINUED

The experience gains and losses of both the UK Group scheme and other schemes are shown below:

History of experience gains and losses	
Difference between the actual and expected return on scheme assets	£(176)m
As a percentage of year end assets	17%
Experience gains and (losses) on scheme liabilities	£16m
As a percentage of year end liabilities	1%
Total amount recognised in statement of total recognised gains and losses	£(159)m
As a percentage of year end liabilities	12%

If the above amounts had been recognised in the financial statements, the Group's net assets and profit and loss reserve at 31 December 2002 would be as follows:

all figures in £ millions	**2002**	2001 RESTATED
Net assets excluding pension liability (see note below)	**3,566**	4,034
FRS 17 pension liability	**(174)**	(73)
Net assets including FRS 17 pension liability	**3,392**	3,961
Profit and loss reserve excluding pension reserve (see note below)	**709**	1,199
FRS 17 pension reserve	**(174)**	(73)
Profit and loss reserve including FRS 17 pension reserves	**535**	1,126

note ▸ The net assets and profit and loss reserve exclude the pension liability of £36m (2001: £61m) included within provisions (see note 22).

10c OTHER POST-RETIREMENT BENEFITS

The Group provides certain healthcare and life assurance benefits principally for retired US employees and their dependents. These plans are unfunded. Retirees are eligible for participation in the plans if they meet certain age and service requirements. Plans that are available vary depending on the business division in which the retiree worked. Plan choices and retiree contributions are dependent on retirement date, business division, option chosen and length of service. The valuation and costs relating to other post-retirement benefits are assessed in accordance with the advice of independent qualified actuaries.

The cost of the benefits and the major assumptions used, based on a measurement date of 31 December 2001, are as follows:

all figures in £ millions	**2002**	2001
Other post-retirement benefits	**5**	4

all figures in percentages	
Inflation	3.0
Rate of increase in healthcare rates	5-10
Rate used to discount scheme liabilities	7.2

Included in note 22, there is a post-retirement medical benefits provision of £56m (2001: £62m). In accordance with UITF 6, the cost of post-retirement benefits, and related provisions, are based on the equivalent US GAAP standard, FAS 106.

The disclosures required under the transitional arrangements of FRS 17 are set out below.

10c OTHER POST-RETIREMENT BENEFITS CONTINUED

For the purpose of these disclosures the valuation of the schemes has been updated to 31 December 2002 using the assumptions listed below.

all figures in percentages	2002	2001
Inflation	3.00	3.00
Rate of increase in healthcare rates	5-12	5-10
Rate used to discount scheme liabilities	6.75	7.20

The value of the unfunded liability is as follows:

all figures in £ millions	2002	2001 RESTATED
Present value of unfunded liabilities	(63)	(63)
Related deferred tax asset	22	22
Net post-retirement healthcare liability	(41)	(41)
Operating charge		
Current service cost	(1)	
Past service cost	–	
Total operating charge	(1)	
Other finance charge		
Interest on pension scheme liabilities	(4)	
Net charge	(4)	
Net profit and loss impact	(5)	
Statement of total recognised gains and losses		
Experience gains arising on the scheme liabilities	3	
Changes in assumptions underlying the present value of the scheme liabilities	(7)	
Exchange differences	5	
Actuarial gain	1	
Movement in deficit during the year		
Deficit in scheme at beginning of the year	(63)	
Current service cost	(1)	
Contributions	4	
Other finance charge	(4)	
Actuarial gain	1	
Deficit in scheme at end of the year	(63)	
Related deferred tax asset	22	
Net post-retirement deficit	(41)	

The experience gains and losses for the schemes are shown below:

History of experience gains and losses	
Experience gains on scheme liabilities	£3m
As a percentage of year end liabilities	4%
Total amount recognised in statement of total recognised gains and losses	£1m
As a percentage of year end liabilities	2%

10c OTHER POST-RETIREMENT BENEFITS CONTINUED

If the above amounts had been recognised in the financial statements, the Group's net assets and profit and loss reserves at 31 December 2002 would be as follows:

all figures in £ millions	2002	2001 RESTATED
Net assets excluding post-retirement healthcare liability (see note below)	3,586	4,035
FRS 17 post-retirement healthcare liability	(41)	(41)
Net assets including FRS 17 post-retirement healthcare liability	**3,545**	3,994
Profit and loss reserve excluding post-retirement healthcare reserve (see note below)	729	1,200
FRS 17 post-retirement healthcare reserve	(41)	(41)
Profit and loss reserve including FRS 17 post-retirement healthcare reserve	**688**	1,159

note ‣ The net assets and profit and loss reserve exclude the post-retirement healthcare liability of £56m (2001: £62m) included within provisions (see note 22).

11 INTANGIBLE FIXED ASSETS

all figures in £ millions	GOODWILL RESTATED
Cost	
At 31 December 2001 as previously reported	4,950
Prior year adjustment – FRS 19	(84)
As restated	4,866
Exchange differences	(383)
Additions	63
Disposals	(59)
At 31 December 2002	**4,487**
Amortisation	
At 31 December 2001 as previously reported	(689)
Prior year adjustment – FRS 19	16
As restated	(673)
Exchange differences	70
Disposals	18
Provided in the year	(282)
Provision for impairment (see note below)	(10)
At 31 December 2002	**(877)**
Net carrying amount	
At 31 December 2001	4,193
At 31 December 2002	**3,610**

note ‣ In accordance with FRS 11 'Impairment of fixed assets and goodwill' the carrying value of the Group's acquired subsidiaries has been compared to their recoverable amounts, represented by their value in use to the Group. The review has resulted in an impairment charge of £10m (2001: £58m).

12 TANGIBLE FIXED ASSETS

all figures in £ millions	FREEHOLD AND LEASEHOLD PROPERTY	PLANT AND EQUIPMENT	ASSETS IN COURSE OF CONSTRUCTION	TOTAL
Cost				
At 31 December 2001	316	719	7	1,042
Exchange differences	(16)	(37)	–	(53)
Reclassifications	–	3	(3)	–
Owned by subsidiaries acquired	–	14	–	14
Capital expenditure	21	89	16	126
Disposals	(10)	(74)	–	(84)
At 31 December 2002	**311**	**714**	**20**	**1,045**
Depreciation				
At 31 December 2001	(90)	(410)	–	(500)
Exchange differences	5	25	–	30
Provided in the year	(17)	(105)	–	(122)
Owned by subsidiaries acquired	–	(14)	–	(14)
Disposals	6	58	–	64
At 31 December 2002	**(96)**	**(446)**	**–**	**(542)**
Net book value				
At 31 December 2001	226	309	7	542
At 31 December 2002	**215**	**268**	**20**	**503**

Freehold and leasehold property ‣ Net book value includes: freehold of £130m (2001: £150m) and short leases of £85m (2001: £76m).

Capital commitments ‣ The Group had capital commitments for fixed assets, including finance leases, already under contract amounting to £12m at 31 December 2002 (2001: £15m).

Other notes ‣ The net book value of Group tangible fixed assets includes £6m (2001: £10m) in respect of assets held under finance leases. Depreciation on these assets charged in 2002 was £2m (2001: £5m).

13 JOINT VENTURES

	2002		2001	
all figures in £ millions	VALUATION	BOOK VALUE	VALUATION	BOOK VALUE
Unlisted joint ventures	**7**	**7**	7	7

note ‣ The valuations of unlisted joint ventures are directors' valuations as at 31 December 2002. If realised at these values there would be no liability for taxation. The Group had no capital commitments to subscribe for further capital and loan stock.

all figures in £ millions	EQUITY	RESERVES	TOTAL NET ASSETS
Summary of movements			
At 31 December 2001	45	(38)	7
Exchange differences	–	(3)	(3)
Additions	16	–	16
Retained loss for the year	–	(13)	(13)
At 31 December 2002	**61**	**(54)**	**7**

13 JOINT VENTURES CONTINUED

all figures in £ millions	2002 Operating loss	2002 Total net assets	2001 Operating loss	2001 Total net assets
Analysis of joint ventures				
Business sectors				
Pearson Education	(1)	–	–	1
FT Group	(13)	3	(20)	3
The Penguin Group	1	4	1	3
	(13)	7	(19)	7
Geographical markets supplied and location of net assets				
United Kingdom	1	4	(1)	3
Continental Europe	(13)	3	(18)	3
North America	(1)	–	–	1
	(13)	7	(19)	7

all figures in £ millions	2002	2001
Reconciliation to retained loss		
Operating loss of joint ventures	(13)	(19)
UK taxation	–	(6)
Retained loss for the year	(13)	(25)

14 ASSOCIATES

all figures in £ millions	2002 Valuation	2002 Book value	2001 Valuation	2001 Book value
Listed associates	17	17	984	829
Unlisted associates	214	88	258	63
Loans	1	1	1	1
	232	106	1,243	893

note ▸ Principal associates are listed in note 34. The valuations of unlisted associates are directors' valuations as at 31 December 2002. If all associates were realised at these values there would be an estimated liability for taxation, at year end rates, of £nil (2001: £59m). The Group had no capital commitments to subscribe for further capital and loan stock.

all figures in £ millions	Share of equity	Loans	Reserves	Total	Goodwill	Total net assets
Summary of movements						
At 31 December 2001	228	1	7	236	657	893
Exchange differences	(2)	–	1	(1)	(3)	(4)
Additions	20	–	–	20	1	21
Disposals	(182)	–	(1)	(183)	(575)	(758)
Retained profit for the year	–	–	2	2	–	2
Goodwill amortisation	–	–	–	–	(48)	(48)
At 31 December 2002	**64**	**1**	**9**	**74**	**32**	**106**

note ▸ On 30 January 2002, the Group sold its interest in the RTL Group for £920m, giving rise to a profit on sale of £18m, after goodwill written back from reserves of £144m and before tax estimated to be £6m.

14 ASSOCIATES CONTINUED

all figures in £ millions	2002 Operating loss	2002 Total net assets	2001 Operating loss	2001 Total net assets
Analysis of associates				
Business sectors				
Pearson Education	**2**	**8**	(1)	10
FT Group	**(37)**	**98**	(49)	120
Continuing operations	**(35)**	**106**	(50)	130
Discontinued operations	**(3)**	**–**	2	763
	(38)	**106**	(48)	893
Geographical markets supplied and location of net assets				
United Kingdom	**11**	**9**	4	12
Continental Europe	**(1)**	**92**	2	72
North America	**(45)**	**(5)**	(59)	36
Rest of world	**–**	**10**	3	10
Continuing operations	**(35)**	**106**	(50)	130
Discontinued operations	**(3)**	**–**	2	763
	(38)	**106**	(48)	893

all figures in £ millions	2002
Reconciliation to retained profit	
Operating profit of associates (before goodwill amortisation)	**10**
Profit on sale of subsidiaries and associates	**3**
Taxation	**(4)**
Dividends (including tax credits) from unlisted associates	**(7)**
Retained profit for the year	**2**

note ▸ The profit on sale of subsidiaries and associates by an associate is £3m relating to the finalised profit on disposal of the Journal of Commerce by the Economist which took place in 2001 (2001: £(36)m).

The aggregate of the Group's share in its associates is shown below:

all figures in £ millions	2002	2001
Sales	**141**	700
Fixed assets	**28**	270
Current assets	**130**	384
Liabilities due within one year	**(76)**	(360)
Liabilities due after one year or more	**(8)**	(58)
Net assets	**74**	236

15 OTHER FIXED ASSET INVESTMENTS

all figures in £ millions	2002 VALUATION	2002 BOOK VALUE	2001 VALUATION	2001 BOOK VALUE
Listed	67	64	67	55
Unlisted	20	20	29	29
	87	84	96	84

note ‣ The valuations of unlisted investments are directors' valuations as at 31 December 2002. If all investments were realised at valuation there would be a liability for taxation of £nil (2001: £6m).

all figures in £ millions	OWN SHARES HELD	OTHER	TOTAL
Cost			
At 31 December 2001	91	107	198
Exchange differences	–	(4)	(4)
Additions	17	4	21
Disposals	–	(10)	(10)
At 31 December 2002	**108**	**97**	**205**
Provision			
At 31 December 2001	59	55	114
Provided during the year	7	–	7
At 31 December 2002	**66**	**55**	**121**
Net book value			
At 31 December 2001	32	52	84
At 31 December 2002	**42**	**42**	**84**

note ‣ The Pearson Employee Share Trust and Pearson plc Employee Share Ownership Trusts hold 7.9m (2001: 5.5m) Pearson plc ordinary shares which had a market value of £45m at 31 December 2002 (2001: £43m). These shares have been acquired by the trusts, using funds provided by Pearson plc, to meet obligations under various executive and employee option and restricted share plans. Under these plans the participants become entitled to shares after a specified number of years and subject to certain performance criteria being met. Pearson aims to hedge its liability under the plans by buying shares through the trusts to meet the anticipated future liability. Dividends on the shares held by the trusts have been waived.

The Group operates a worldwide Save As You Earn scheme together with a similar scheme for US employees that allows the grant of share options at a discount to the market price of the option granted. The Group has made use of the exemption under UITF 17 not to recognise any compensation charge in respect of these options.

Employer's National Insurance and similar taxes arise on the exercise of certain share options. In accordance with UITF 25 a provision is made, calculated using the market price of the company's shares at the balance sheet date, pro-rated over the vesting period of the options.

16 STOCKS

all figures in £ millions	2002	2001
Raw materials	**22**	32
Work in progress	**36**	45
Finished goods	**297**	370
Pre-publication costs	**379**	402
	734	849

note ▸ The replacement cost of stocks is not materially different from book value.

17 DEBTORS

all figures in £ millions	2002	2001
Amounts falling due within one year		
Trade debtors	**778**	745
Associates	**1**	2
Royalty advances	**109**	103
Other debtors	**51**	49
Prepayments and accrued income	**44**	40
	983	939
Amounts falling due after more than one year		
Royalty advances	**63**	54
Other debtors	**10**	11
Prepayments and accrued income	**1**	1
	74	66
	1,057	1,005

18 CASH AT BANK AND IN HAND

	2002		2001	
all figures in £ millions	GROUP	COMPANY	GROUP	COMPANY
Cash, bank current accounts and overnight deposits	**417**	**–**	300	–
Certificates of deposit and commercial paper	**15**	**–**	15	–
Term bank deposits	**143**	**8**	78	22
	575	**8**	393	22

19 FINANCIAL INSTRUMENTS

A full discussion on treasury policy is given in the Financial Review on pages 33 to 34. Short-term debtors and creditors have been excluded from all the following disclosures, other than currency risk disclosures.

a. Maturity of borrowings and other financial liabilities

The maturity profile of the Group's borrowings and other financial liabilities is shown below:

	2002		2001	
all figures in £ millions	GROUP	COMPANY	GROUP	COMPANY
Maturity of borrowings				
Short-term				
Bank loans and overdrafts	101	175	65	109
10.75% Sterling Bonds 2002	–	–	100	–
5% Euro Bonds 2003	148	148	–	–
Total due within one year	249	323	165	109
Medium and long-term				
Loans or instalments thereof repayable:				
From one to two years	458	338	154	154
From two to five years	616	371	1,285	705
After five years not by instalments	660	660	1,168	1,168
Total due after more than one year	1,734	1,369	2,607	2,027
Total borrowings	1,983	1,692	2,772	2,136

note ▸ At 31 December 2002 £91m (2001: £557m) of debt, including commercial paper, currently classified from two to five years would be repayable within one year if refinancing contracts were not in place. The short-term bank loans and overdrafts of the Group are lower than those of the company because of bank offset arrangements.

	2002			2001		
all figures in £ millions	GROUP FINANCE LEASES	GROUP OTHER FINANCIAL LIABILITIES	GROUP TOTAL	GROUP FINANCE LEASES	GROUP OTHER FINANCIAL LIABILITIES	GROUP TOTAL
Maturity of other financial liabilities						
Amounts falling due:						
In one year or less or on demand	4	11	15	5	11	16
In more than one year but not more than two years	2	8	10	1	9	10
In more than two years but not more than five years	1	16	17	8	18	26
In more than five years	–	22	22	–	11	11
	7	57	64	14	49	63

b. Borrowings by instrument

	2002		2001	
all figures in £ millions	GROUP	COMPANY	GROUP	COMPANY
Unsecured				
10.75% Sterling Bonds 2002	–	–	100	–
5% Euro Bonds 2003	148	148	154	154
9.5% Sterling Bonds 2004	120	–	133	–
4.625% Euro Bonds 2004	338	338	353	353
7.375% US Dollar notes 2006	154	–	170	–
6.125% Euro Bonds 2007	370	370	448	448
10.5% Sterling Bonds 2008	100	100	100	100
7% Global Dollar Bonds 2011	310	310	342	342
7% Sterling Bonds 2014	250	250	278	278
Variable rate loan notes	1	1	72	72
Bank loans and overdrafts and commercial paper	192	175	622	389
Total borrowings	1,983	1,692	2,772	2,136

19 FINANCIAL INSTRUMENTS CONTINUED

c. Undrawn committed borrowing facilities

all figures in £ millions	2002	2001
Expiring within one year	–	–
Expiring between one and two years	–	–
Expiring in more than two years	1,059	1,172
	1,059	1,172

note ▸ All of the above committed borrowing facilities incur commitment fees at market rates.

d. Currency and interest rate risk profile

	2002				
				Fixed rate borrowings	
	Borrowings £m	Total variable rate £m	Total fixed rate £m	Weighted average interest rate %	Weighted average period for which rate is fixed – years
Currency and interest rate risk profile of borrowings					
US dollar	1,350	752	598	5.9	4.0
Sterling	241	161	80	10.5	5.5
Euro	380	305	75	5.2	1.5
Other currencies	12	12	–	–	–
	1,983	1,230	753		

note ▸ There is an interest rate collar instrument which matures in 2007 with a notional value of £31m equivalent, that is classified at year end as a variable rate US dollar borrowing. This instrument limits our interest rate liability above 4.5%.

	2001				
				Fixed rate borrowings	
	Borrowings £m	Total variable rate £m	Total fixed rate £m	Weighted average interest rate %	Weighted average period for which rate is fixed – years
Currency and interest rate risk profile of borrowings					
US dollar	1,829	625	1,204	6.1	3.5
Sterling	520	410	110	9.3	5.1
Euro	404	320	84	5.2	2.4
Other currencies	19	19	–	–	–
	2,772	1,374	1,398		

note ▸ The figures shown in the tables above take into account interest rate, currency swaps and forward rate contracts entered into by the Group. Variable rate borrowings bear interest at rates based on relevant national LIBOR equivalents.

	2002		
all figures in £ millions	Other financial liabilities	Total fixed rate	Total no interest paid
Currency and interest rate risk profile of other financial liabilities			
US dollar	45	5	40
Sterling	8	2	6
Euro	11	–	11
	64	7	57

19 FINANCIAL INSTRUMENTS CONTINUED

d. Currency and interest rate risk profile (continued)

all figures in £ millions	2001 Other financial liabilities	2001 Total fixed rate	2001 Total no interest paid
Currency and interest rate risk profile of other financial liabilities			
US dollar	48	11	37
Sterling	6	3	3
Euro	9	–	9
	63	14	49

all figures in £ millions	2002 US dollar	2002 Sterling	2002 Euro	2002 Other currencies	2002 Total
Currency and interest rate risk profile of financial assets					
Cash at bank and in hand	279	9	67	62	417
Short-term deposits	2	18	127	11	158
Other financial assets	28	6	–	–	34
	309	33	194	73	609
Floating rate	281	27	193	73	574
No interest received	28	6	1	–	35
	309	33	194	73	609

all figures in £ millions	2001 US dollar	2001 Sterling	2001 Euro	2001 Other currencies	2001 Total
Currency and interest rate risk profile of financial assets					
Cash at bank and in hand	166	40	62	32	300
Short-term deposits	10	27	40	16	93
Other financial assets	37	4	3	–	44
	213	71	105	48	437
Floating rate	176	65	102	47	390
No interest received	37	6	3	1	47
	213	71	105	48	437

19 FINANCIAL INSTRUMENTS CONTINUED

e. Currency exposures

The table below shows the extent to which Group companies have monetary assets and liabilities in currencies other than their local currency.

	2002 NET FOREIGN MONETARY ASSETS/(LIABILITIES)				
all figures in £ millions	US DOLLAR	STERLING	EURO	OTHER	TOTAL
Functional currency of entity:					
US dollar	–	2	–	2	4
Sterling	48	–	41	8	97
Euro	–	1	–	6	7
Other currencies	4	4	5	–	13
	52	7	46	16	121

	2001 NET FOREIGN MONETARY ASSETS/(LIABILITIES)				
all figures in £ millions	US DOLLAR	STERLING	EURO	OTHER	TOTAL
Functional currency of entity:					
US dollar	–	–	–	3	3
Sterling	(67)	–	8	5	(54)
Euro	–	–	–	–	–
Other currencies	(5)	(2)	–	–	(7)
	(72)	(2)	8	8	(58)

f. Fair values of financial assets and financial liabilities

The table below shows the book value and the fair value of the Group's financial assets and financial liabilities.

	2002		2001	
all figures in £ millions	BOOK VALUE	FAIR VALUE	BOOK VALUE	FAIR VALUE
Primary financial instruments held or issued to finance the Group's operations				
Other financial assets	34	34	44	44
Other financial liabilities	(64)	(64)	(63)	(63)
Cash at bank and in hand	417	417	300	300
Short-term deposits	158	158	93	93
Short-term borrowings	(249)	(253)	(165)	(165)
Medium and long-term borrowings	(1,734)	(1,877)	(2,607)	(2,527)
Derivative financial instruments held to manage the interest rate and currency profile				
Interest rate swaps	–	26	–	(30)
Currency swaps	–	32	–	16
Foreign exchange contracts	–	4	–	(1)

note ▸ Other financial assets, other financial liabilities, cash at bank and in hand, short-term deposits and short-term borrowings: the fair value approximates to the carrying value due to the short maturity periods of these financial instruments. Medium and long-term borrowings: the fair value is based on market values or, where these are not available, on the quoted market prices of comparable debt issued by other companies. Interest rate swaps: the fair value of interest rate swaps is based on market values. At 31 December 2002 the notional principal value of these swaps was £1,605m (2001: £2,391m). Currency swaps: the fair value of these contracts is based on market values. At 31 December 2002 the Group had £758m (2001: £924m) of such contracts outstanding.

19 FINANCIAL INSTRUMENTS CONTINUED

g. Hedges

The Group's policy on hedges is explained on page 33. The table below shows the extent to which the Group has off-balance sheet (unrecognised) gains and losses in respect of financial instruments used as hedges at the beginning and end of the year. It also shows the amount of such gains and losses which have been included in the profit and loss account for the year and those gains and losses which are expected to be included in next year's or later profit and loss accounts.

all figures in £ millions	GAINS	UNRECOGNISED LOSSES	TOTAL NET GAINS/(LOSSES)
Gains and losses on hedges at 31 December 2001	43	(58)	(15)
Gains and losses arising in previous years that were recognised in 2002	(1)	34	33
Gains and losses arising before 31 December 2001 that were not recognised in 2002	42	(24)	18
Gains and losses arising in 2002 that were not recognised in 2002	71	(27)	44
Unrecognised gains and losses on hedges at 31 December 2002	113	(51)	62
Of which:			
Gains and losses expected to be recognised in 2003	6	–	6
Gains and losses expected to be recognised in 2004 or later	107	(51)	56

20 OTHER CREDITORS

all figures in £ millions	**2002**	2001
Amounts falling due within one year		
Trade creditors	**376**	390
Taxation	**24**	111
Social security and other taxes	**13**	2
Other creditors	**83**	85
Accruals and deferred income	**499**	501
Obligations under finance leases	**4**	5
Dividends	**115**	109
	1,114	1,203
Amounts falling due after more than one year		
Other creditors	**31**	30
Accruals and deferred income	**26**	15
Obligations under finance leases	**3**	9
	60	54

21 DEFERRED TAXATION

all figures in £ millions	
Summary of movements	
At 31 December 2001 as previously reported	**(5)**
Prior year adjustment (see below)	**277**
As restated	**272**
Exchange differences	**(29)**
Transfers	**(3)**
Net release in the year	**(66)**
At 31 December 2002	**174**

all figures in £ millions	**2002**	2001 RESTATED
Deferred taxation derives from:		
Capital allowances	**(47)**	(10)
Tax losses carried forward	**170**	172
Taxation on unremitted overseas earnings	**(16)**	(15)
Other timing differences	**67**	125
	174	272
Deferred taxation not provided		
Relating to revalued assets and timing differences	**–**	–
Relating to gains subject to roll-over relief	**1**	1
	1	1

note ▸ The Group has calculated deferred tax not provided on rolled over gains in 2002, taking into account the indexation allowance which would be deductible on a disposal of the asset into which the gain was rolled.

Prior year adjustment

FRS 19 'Deferred Tax' has been adopted for the first time in these financial statements. The Group previously provided deferred tax using the liability method under SSAP 15 and only recognised deferred tax liabilities to the extent that it was probable that the liabilities would crystallise. Deferred tax assets were only recognised to the extent that their recoverability was assured beyond reasonable doubt. Under FRS 19 the recognition criteria for deferred tax assets has changed, with the result that the Group has recognised a deferred tax asset in respect of US tax losses and other timing differences that are regarded as recoverable against future taxable profits. The adoption of FRS 19 has also had an impact on capitalised goodwill since the restatement of deferred tax balances acquired has had a corresponding effect upon the goodwill recognised on those acquisitions. A prior year adjustment has been made in these financial statements to reflect the adoption of FRS 19 and comparative figures have been restated. The impact on the profit and loss account for 2002 has been to increase the loss after taxation by £45m (£50m relating to the tax charge and an offsetting £5m to goodwill amortisation) and to increase opening shareholders' funds by £209m. The effect on the loss after taxation for 2001 was to increase the loss by £32m.

22 PROVISIONS FOR LIABILITIES AND CHARGES

all figures in £ millions	POST-RETIREMENT	DEFERRED CONSIDERATION	INTEGRATION	REORGANISATIONS	LEASES	OTHER	TOTAL
At 31 December 2001	123	25	29	29	19	14	239
Exchange differences	(11)	(4)	(2)	(2)	(2)	–	(21)
Subsidiaries acquired/disposed	2	–	–	–	(1)	1	2
Deferred consideration arising on acquisitions	–	3	–	–	–	–	3
Released	–	–	–	(3)	(1)	(1)	(5)
Provided	59	–	8	9	7	1	84
Utilised	(81)	(13)	(18)	(14)	(4)	(7)	(137)
At 31 December 2002	**92**	**11**	**17**	**19**	**18**	**8**	**165**

note

a Post-retirement provisions are in respect of pensions, £36m (2001: £61m) and post-retirement medical benefits, £56m (2001: £62m).

b Deferred consideration. During the year, £13m was paid with respect to companies acquired as part of the NCS acquisition in 2000. The balance is expected to be utilised during 2003.

c Integration. These movements relate to The Penguin Group and Pearson Education. £9m has been utilised in relation to properties and a further £9m relating to severance and IT systems. No further integration charges are anticipated in 2003 relating to these prior year acquisitions, and the remaining provision should be utilised in the next three years.

d Reorganisations. £9m has been provided during 2002, mostly relating to the restructuring of our back office systems and processes. £14m has been utilised in the reorganisation of Family Education Network and FT Knowledge. The balance is expected to be utilised in the next two years.

e Lease commitments. These relate primarily to onerous lease contracts, acquired as part of the purchase of subsidiaries, which have various expiry dates up to 2010. The provision is based on current occupancy estimates.

f Other. The balance, which relates to a number of small items, is expected to be utilised over varying time periods.

23 SHARE CAPITAL

	NUMBER OF SHARES (000'S)	£m
Authorised		
Ordinary shares of 25p each		
At 31 December 2002	**1,174,000**	**294**
Called up, allotted and fully paid		
At 31 December 2001	800,589	200
Issued under share option and employee share schemes	1,073	–
At 31 December 2002	**801,662**	**200**

note ▸ The consideration received in respect of shares issued during the year was £6m (2001: £20m).

23 SHARE CAPITAL CONTINUED

	WHEN GRANTED	NUMBER OF SHARES (000'S)	PRICE (P)	ORIGINAL SUBSCRIPTION EXERCISE PERIOD
Options outstanding at 31 December 2002				
Worldwide Save for Shares plans	1995	20	390	2000 – 03
	1996	60	517	2001 – 04
	1997	114	530	2000 – 05
	1998	360	687	2001 – 06
	1999	544	913 – 970	2001 – 07
	2000	217	688 – 1,793	2001 – 08
	2001	532	957 – 1,096	2004 – 09
	2002	1,466	696	2005 – 10
		3,313		
Discretionary share option plans	1994	171	567 – 635	1997 – 04
	1995	194	487 – 606	1998 – 05
	1996	282	584 – 683	1999 – 06
	1997	1,156	664 – 758	2000 – 07
	1998	1,781	847 – 1,090	2001 – 08
	1999	3,681	1,081 – 1,922	2002 – 09
	2000	10,432	64 – 3,224	2000 – 10
	2001	14,599	822 – 1,421	2001 – 11
		32,296		

note ▸ The subscription prices have been rounded up to the nearest whole penny. The figures include replacement options granted to employees of Dorling Kindersley and the Family Education Network following their acquisition. The discretionary share option plans include all options granted under the Pearson Executive Share Option Plans, the Pearson Reward Plan, the Pearson Special Share Option Plan and the Pearson Long Term Incentive Plan.

24 RESERVES

all figures in £ millions	SHARE PREMIUM ACCOUNT	PROFIT AND LOSS ACCOUNT RESTATED
Summary of movements		
At 31 December 2001 as previously reported	2,459	929
Prior year adjustment – FRS 19	–	209
As restated	2,459	1,138
Exchange differences net of taxation	–	(312)
Premium on issue of 1m equity shares	6	–
Goodwill written back on disposal of an associate	–	144
Replacement options granted on acquisition of a subsidiary	–	1
Loss retained for the year	–	(298)
At 31 December 2002	**2,465**	**673**
Analysed as:		
Joint ventures and associates		(45)
Group excluding joint ventures and associates		718

note ▸ Cumulative goodwill relating to acquisitions made prior to 1998, which was deducted from reserves, amounts to £1,031m (2001: £1,249m). During 2002 Pearson plc received £6m on the issue of shares in respect of the exercise of options awarded under various share option plans. Employees paid £6m to the Group for the issue of these shares. The Group has taken advantage of the exemption available by UITF 17 and has not incurred a charge on options granted at a discount to market value for its Inland Revenue approved SAYE schemes and similar overseas schemes. Included in exchange differences are exchange gains of £70m arising on borrowings denominated in, or swapped into, foreign currencies designated as hedges of net investments overseas.

25 ACQUISITIONS

All acquisitions have been consolidated applying acquisition accounting principles.

a. Acquisition of subsidiaries

all figures in £ millions	2002	2001
Tangible fixed assets	–	5
Associates	(3)	(3)
Stocks	(2)	8
Debtors	2	(78)
Creditors	(4)	(19)
Provisions	(3)	(9)
Deferred taxation	–	(1)
Net cash and short-term deposits acquired	25	83
	15	(14)
Equity minority interests	(4)	(2)
Net assets/(liabilities) acquired at fair value	11	(16)
Fair value of consideration:		
Cash	(74)	(52)
Deferred cash consideration	(3)	(10)
Costs accrued	–	(1)
Net prior year adjustments	3	(8)
Total consideration	(74)	(71)
Goodwill arising	**63**	**87**

all figures in £ millions	2002
Acquisition fair values	
Book value of net assets acquired	25
Fair value adjustments	(14)
Fair value to the Group	11

note ‣ Of the fair value adjustments above, £(14)m relates to the finalisation of prior year provisional acquisition values. These adjustments relate primarily to: write down of stock to its recoverable amount and the recognition of a provision for royalty payments. For acquisitions made during 2002 the fair value adjustments are provisional and will be finalised in the 2003 financial statements.

b. Cash flow from acquisitions

all figures in £ millions	2002	2001
Cash – current year acquisitions	74	52
Deferred payments for prior year acquisitions and other items	13	76
Net cash outflow	**87**	**128**

26 DISPOSALS

all figures in £ millions	**2002**	2001 RESTATED
Disposal of subsidiaries		
Intangible assets	**(41)**	(53)
Tangible fixed assets	**–**	(7)
Stocks	**(3)**	(2)
Debtors	**(2)**	(15)
Creditors	**(3)**	14
Taxation	**–**	(5)
Provisions	**1**	1
Net debt	**(1)**	–
Equity minority interest	**3**	–
Net assets disposed of	**(46)**	(67)
Proceeds received	**11**	49
Costs	**(7)**	(7)
Net prior year adjustments	**(3)**	(1)
Loss on sale	**(45)**	(26)
Goodwill written back from reserves	**–**	(37)
Net loss on sale	**(45)**	(63)

all figures in £ millions	**2002**	2001
Cash flow from disposals		
Cash – current year disposals	**11**	49
Costs paid	**(3)**	(8)
Deferred receipts and payments from prior year disposals and other amounts	**(5)**	–
Net cash inflow	**3**	41

27 NOTES TO CONSOLIDATED STATEMENT OF CASH FLOWS

all figures in £ millions	2002 TOTAL	2001 RESTATED CONTINUING	DISCONTINUED	TOTAL
a. Reconciliation of operating profit/(loss) to net cash inflow from operating activities				
Total operating profit/(loss)	**143**	(49)	2	(47)
Share of operating loss/(profit) of joint ventures and associates	**51**	69	(2)	67
Depreciation charges	**122**	125	–	125
Goodwill amortisation and impairment	**292**	350	–	350
Decrease/(increase) in stocks	**43**	(6)	–	(6)
(Increase)/decrease in debtors	**(111)**	102	–	102
Increase/(decrease) in creditors	**64**	(103)	–	(103)
(Decrease)/increase in operating provisions	**(50)**	3	–	3
Other and non-cash items	**(25)**	(1)	–	(1)
Net cash inflow from operating activities	**529**	490	–	490
Dividends from associates	**6**	7	18	25
Purchase of tangible fixed assets	**(126)**	(165)	–	(165)
Capital element of finance leases	**(5)**	(7)	–	(7)
Sale of tangible fixed assets	**7**	36	–	36
Add back: non operating fixed asset disposal proceeds	**–**	(11)	–	(11)
Add back: integration costs	**44**	69	–	69
Operating cash flow	**455**	419	18	437
Operating tax paid	**(46)**	(44)	–	(44)
Operating finance charges	**(104)**	(157)	–	(157)
Operating free cash flow	**305**	218	18	236
Non operating tax paid	**(9)**	(27)	–	(27)
Non operating finance charges	**(37)**	–	–	–
Integration costs	**(44)**	(69)	–	(69)
Total free cash flow	**215**	122	18	140
Dividends paid (including minorities)	**(182)**	(183)	–	(183)
Net movement of funds from operations	**33**	(61)	18	(43)
Acquisitions of businesses and investments	**(124)**	(100)	–	(100)
Disposals of businesses, investments and property	**930**	77	–	77
New equity	**6**	20	–	20
Other non operating items	**(5)**	(8)	–	(8)
Net movement of funds	**840**	(72)	18	(54)
Exchange movements on net debt	**131**	(24)	–	(24)
Total movement in net debt	**971**	(96)	18	(78)

note ‣ Operating cash flow, operating free cash flow and total free cash flow have been disclosed as they are part of Pearson's corporate and operating measures. Tax payments that can be clearly identified with disposals, integration and exchange differences taken to reserves are allocated as non operating tax payments.

27 NOTES TO CONSOLIDATED STATEMENT OF CASH FLOWS CONTINUED

all figures in £ millions	CASH	OVER-DRAFTS	SUB-TOTAL	SHORT-TERM DEPOSITS	DEBT DUE WITHIN ONE YEAR	DEBT DUE AFTER ONE YEAR	FINANCE LEASES	TOTAL
b. Analysis of net debt								
At 31 December 2001	300	(60)	240	93	(105)	(2,607)	(14)	(2,393)
Exchange differences	(15)	4	(11)	(2)	(6)	150	1	132
Acquired with subsidiary	–	–	–	24	–	–	–	24
Other non-cash items	–	–	–	–	(148)	146	1	(1)
Net cash flow	132	(21)	111	43	87	577	5	823
At 31 December 2002	**417**	**(77)**	**340**	**158**	**(172)**	**(1,734)**	**(7)**	**(1,415)**
At 31 December 2000	425	(110)	315	91	(2)	(2,705)	(16)	(2,317)
Exchange differences	(10)	1	(9)	1	–	(16)	–	(24)
Debt issue costs	–	–	–	–	–	1	–	1
Other non-cash items	–	–	–	–	(100)	99	(5)	(6)
Net cash flow	(115)	49	(66)	1	(3)	14	7	(47)
At 31 December 2001	300	(60)	240	93	(105)	(2,607)	(14)	(2,393)

note ‣ Finance leases are included within other creditors in the balance sheet (see note 20).

all figures in £ millions	**2002**	2001
c. Reconciliation of net cash flow to movement in net debt		
Decrease/(increase) in net debt from net cash flow	**111**	(66)
Decrease in net debt from management of liquid resources	**43**	1
Decrease in net debt from other borrowings	**664**	11
Decrease in finance leases	**5**	7
Acquired with subsidiary	**24**	–
Debt issue costs	**–**	1
Other non-cash items	**(1)**	(6)
Exchange differences	**132**	(24)
Movement in net debt in the year	**978**	(76)
Net debt at beginning of the year	**(2,393)**	(2,317)
Net debt at end of the year	**(1,415)**	(2,393)

28 CONTINGENT LIABILITIES

There are contingent Group and company liabilities in respect of indemnities, warranties and guarantees in relation to former subsidiaries and in respect of guarantees in relation to subsidiaries and associates. In addition there are contingent liabilities of the Group in respect of legal claims. None of these claims are expected to result in a material gain or loss to the Group.

29 COMMITMENTS UNDER LEASES

At 31 December 2002, the Group had commitments under leases other than finance leases, to make payments in 2003 as follows:

all figures in £ millions	LAND AND BUILDINGS	OTHER
For leases expiring:		
In 2003	10	3
Between 2004 and 2007	40	16
Thereafter	65	–
	115	19

30 RELATED PARTIES

Joint ventures and associates ▸ Loans and equity advanced to joint ventures and associates during the year and at the balance sheet date are shown in notes 13 and 14. Amounts falling due from joint ventures and associates are set out in note 17. Dividends receivable from joint ventures and associates are set out in notes 13 and 14.

There are no other related party transactions in 2002.

31 POST BALANCE SHEET EVENTS

In January 2003 Interactive Data Corporation announced its acquisition of S&P Comstock for $115m in cash.

32 COMPANY BALANCE SHEET AS AT 31 DEC 2002

all figures in £ millions	NOTE	2002	2001
Fixed assets			
Tangible fixed assets	33	–	–
Investments: subsidiaries	33	6,422	5,384
Investments: own shares held	33	39	24
		6,461	5,408
Current assets			
Debtors:			
Subsidiaries – due within one year		971	2,186
Subsidiaries – due after more than one year		1,453	1,312
Taxation		10	17
Other debtors		1	–
Prepayments and accrued income		–	1
Cash at bank and in hand	18	8	22
		2,443	3,538
Creditors – amounts falling due within one year			
Short-term borrowing	19	(323)	(109)
Subsidiaries		(2,641)	(2,006)
Other creditors		(1)	(1)
Accruals and deferred income		(13)	(15)
Dividends		(115)	(109)
		(3,093)	(2,240)
Net current (liabilities)/assets		(650)	1,298
Total assets less current liabilities		5,811	6,706
Creditors – amounts falling due after more than one year			
Medium and long-term borrowing	19	(1,369)	(2,027)
Subsidiaries		(393)	(392)
Provisions for liabilities and charges		(2)	(2)
		(1,764)	(2,421)
Net assets		4,047	4,285
Capital and reserves			
Called up share capital	23	200	200
Share premium account	33	2,465	2,459
Special reserve	33	397	397
Other reserves	33	50	50
Profit and loss account	33	935	1,179
Equity shareholders' funds		4,047	4,285

The financial statements were approved by the board of directors on 3 March 2003 and signed on its behalf by

DENNIS STEVENSON ▸ **RONA FAIRHEAD.**

33 NOTES TO THE COMPANY BALANCE SHEET

all figures in £ millions	**2002**	2001
Tangible fixed assets (leasehold property)		
Cost	**1**	1
Depreciation	**(1)**	(1)
Net book value	**–**	–

note ‣ The company had no capital commitments for fixed assets at the end of 2002.

all figures in £ millions	
Investment in subsidiaries	
At 31 December 2001	5,384
External acquisition	2
Subscription for additional share capital in subsidiaries	1,085
Disposal to subsidiary	(16)
Provision for diminution in value	(32)
Revaluations	(1)
At 31 December 2002	**6,422**

note ‣ Shares are stated at cost less provisions for diminution in value or directors' valuations.

Own shares held ‣ Amounts included within own shares held relate to Pearson plc ordinary shares held in respect of the Pearson plc Employee Share Ownership Trusts (see note 15).

all figures in £ millions	SHARE PREMIUM ACCOUNT	SPECIAL RESERVE	OTHER RESERVES	PROFIT AND LOSS ACCOUNT	TOTAL
Reserves					
Summary of movements					
At 31 December 2001	2,459	397	50	1,179	4,085
Currency translation differences	–	–	–	(46)	(46)
Premium on issue of 1m equity shares	6	–	–	–	6
Loss for the financial year	–	–	–	(11)	(11)
Dividends	–	–	–	(187)	(187)
At 31 December 2002	**2,465**	**397**	**50**	**935**	**3,847**

note ‣ The special reserve represents the cumulative effect of cancellation of the company's share premium account. As permitted by section 230(4) of the Companies Act 1985, only the Group's profit and loss account has been presented.

34 PRINCIPAL SUBSIDIARIES AND ASSOCIATES

	Country of incorporation or registration
Subsidiaries	
The principal operating subsidiaries are listed below. They operate mainly in the countries of incorporation or registration, the investments are in equity share capital and they are all 100% owned unless stated otherwise.	
Pearson Education	
Pearson Education Inc.	US
Pearson Education Ltd	England
NCS Pearson Inc.	US
FT Group	
The Financial Times Ltd	England
Financial Times Business Ltd	England
Interactive Data Corporation (60%)	US
Les Echos SA	France
Recoletos Grupo de Comunicación SA (79%)	Spain
The Penguin Group	
Penguin Putnam Inc.	US
The Penguin Publishing Co Ltd	England
Dorling Kindersley Holdings Ltd*	England

* Direct investment of Pearson plc.

	Country of incorporation or registration	Class of share	Beneficial interest %	Accounting year end
Associates				
FT Group				
The Economist Newspaper Ltd	England	Ord 5p	50	March
		'B' 5p	100	
		'A' 5p	Nil	
		Trust 5p	Nil	
FT-SE International Ltd	England	Ord £1	50	December

Five year summary

all figures in £ millions	1998 RESTATED	1999 RESTATED	2000 RESTATED	2001 RESTATED	**2002**
Sales					
Continuing operations	1,908	2,977	3,689	4,225	**4,320**
Discontinued operations	487	355	185	–	**–**
	2,395	3,332	3,874	4,225	**4,320**
Sales – underlying growth %	6.7	7.6	10.5	(0.3)	**6.0**
EBITDA*	455	631	590	588	**615**
Trading margin %	13.1	14.0	11.5	10.5	**11.4**
Operating profit before goodwill charge and other items					
Pearson Education	99	254	237	274	**326**
FT Group	118	114	98	72	**80**
The Penguin Group	48	65	79	80	**87**
Continuing operations	265	433	414	426	**493**
Internet enterprises investment					
Pearson Education	–	(3)	(83)	(77)	**(25)**
FT Group	–	(36)	(113)	(60)	**(34)**
	–	(39)	(196)	(137)	**(59)**
Adjusted eps*	36.6p	39.5p	30.6p	21.4p	**30.3p**
Dividends per share*	18.8p	20.1p	21.4p	22.3p	**23.4p**
Net assets	1,237	1,527	4,398	3,973	**3,530**
Deferred taxation	(243)	(266)	(295)	(272)	**(174)**
Provisions for liabilities and charges	253	206	257	239	**165**
Net debt (excluding finance leases)	2,279	1,995	2,301	2,379	**1,408**
Capital employed	3,526	3,462	6,661	6,319	**4,929**
Operating free cash flow per share*	40.3p	43.4p	23.0p	29.6p	**38.3p**

* Before goodwill charge, integration costs and non operating items, and restated to reflect the rights issue of equity shares during 2000 and adoption of FRS 19.

Corporate and operating measures

Sales – underlying growth

Sales growth excluding the impact of acquisitions and disposals and movements in exchange rates.

all figures in £ millions	2002
Underlying increase	248
Portfolio changes	10
Foreign exchange	(163)
Total sales increase	95
Underlying increase	6.0%

Trading margin

Trading profit (operating profit excluding profit from joint ventures, associates and investments) as a proportion of sales.

all figures in £ millions	2002
Total operating profit – Group	496
Investment income	(2)
Trading profit	494
Sales	4,320
Trading margin	11.4%

Operating free cash flow per share*

Operating cash flow less taxation paid on operating profits and interest paid, divided by the weighted average number of shares in issue.

all figures in £ millions	2002
Operating profit	493
Cash conversion	92%
Operating cash flow	455
Tax paid on operating profits	(46)
Interest paid	(104)
Operating free cash flow	305
Weighted average shares in issue (millions)	796.3
Operating free cash flow per share	38.3p

* Before goodwill charge, integration costs and non operating items.

Shareholder Information

Payment of dividends to mandated accounts ‣ Where shareholders have given instruction for payment to be made direct into a bank or building society, this is done through the Bankers Automated Clearing System (BACS), with the associated tax voucher showing the tax credit attributable to the dividend payment sent direct to the shareholder at the address shown on our register. If you wish the tax voucher to be sent to your bank or building society, please inform our registrar, Lloyds TSB Registrars, The Causeway, Worthing, West Sussex BN99 6DA. Telephone 0870 600 3986 or, for those shareholders with hearing difficulties, textphone number 0870 600 3950.

Dividend reinvestment plan (DRIP) ‣ The plan provides the benefit of giving shareholders the right to buy the company's shares on the London stock market with the cash dividend. If you would like further information about the DRIP, please contact Lloyds TSB Registrars. Telephone 0870 241 3018.

Personal Equity Plans (PEPs) and Individual Savings Accounts (ISAs) ‣ The government no longer permits investment to be made in PEPs, although existing PEPs may be continued. Existing Corporate PEP and Single Company PEP holders who require further information about their PEPs should ring the HBOS helpline on 0870 606 6417. Lloyds TSB Registrars offer ISAs in Pearson shares. They can be contacted for information on 0870 242 4244.

Low cost share dealing facility ‣ A postal facility, which provides a simple, low cost way of buying and selling Pearson shares, is available through the company's stockbroker, Cazenove & Co. Limited, 12 Tokenhouse Yard, London EC2R 7AN. Telephone 020 7588 2828.

Shareholder information on-line ‣ Lloyds TSB Registrars provide a range of shareholder information on-line. You can check your holding and find practical help on transferring shares or updating your details at www.shareview.co.uk. Lloyds TSB Registrars can be contacted for information on 0870 600 3970.

Information about the Pearson share price ‣ The current price of Pearson ordinary shares can be obtained from Financial Times CityLine. Telephone 0906 843 3620.

American Depositary Receipts (ADRs) ‣ Pearson's ordinary shares are listed on the New York Stock Exchange in the form of ADRs and traded under the symbol PSO. Each ADR represents one ordinary share. Voting rights as a shareholder may be exercised through The Bank of New York, ADR Department, 101 Barclay Street, New York, New York 10286, telephone 800 BNY ADRS (toll free within the US) or (1) 610 312 5315 (outside the US). All enquiries regarding ADR holder accounts and payment of dividends should be directed to The Bank of New York, the authorised depositary bank for Pearson's ADR programme, at the address given above. Pearson will file with the Securities and Exchange Commission a report on Form 20-F that will contain a US GAAP reconciliation.

Advisers ‣ ***auditors*** PricewaterhouseCoopers LLP ‣ ***bankers*** HSBC Bank Plc ‣ ***broker*** Cazenove & Co. Limited ‣ ***financial advisers*** Lazard Brothers & Co. Limited, J. Henry Schroder & Co. Limited ‣ ***solicitors*** Freshfields Bruckhaus Deringer, Herbert Smith and Morgan, Lewis & Bockius.

FINANCIAL CALENDAR FOR 2003

EX-DIVIDEND DATE	WEDNESDAY 12 MARCH
RECORD DATE	FRIDAY 14 MARCH
LAST DATE FOR DIVIDEND REINVESTMENT ELECTION	THURSDAY 24 APRIL
ANNUAL GENERAL MEETING	FRIDAY 25 APRIL
PAYMENT DATE FOR DIVIDEND AND SHARE PURCHASE DATE FOR DIVIDEND REINVESTMENT	FRIDAY 9 MAY
INTERIM RESULTS	MONDAY 28 JULY
INTERIM DIVIDEND	FRIDAY 26 SEPTEMBER

Principal Addresses

PEARSON UK
80 Strand,
London, WC2R ORL, UK
Telephone +44 (0)20 7010 2000
Facsimile +44 (0)20 7010 6060
E-mail firstname.lastname@pearson.com
www.pearson.com
Registered number 53723

PEARSON US
1330 Avenue of the Americas,
New York City, NY 10019, USA
Telephone +1 212 641 2400
Facsimile +1 212 641 2500
E-mail firstname.lastname@pearson-inc.com
www.pearson.com

PEARSON EDUCATION
One Lake Street, Upper Saddle River, NJ 07458, USA
Telephone +1 201 236 7000 ‣ **Facsimile** +1 515 284 6719
E-mail firstname.lastname@pearsoned.com
www.pearsoneducation.com

THE PENGUIN GROUP
80 Strand, London, WC2R 0RL, UK
Telephone +44 (0)20 7010 2000 ‣ **Facsimile** +44 (0)20 7010 6060
E-mail initiallastname@penguin.com
www.penguin.co.uk
www.penguinputnam.com

THE FINANCIAL TIMES GROUP
Number One Southwark Bridge, London, SE1 9HL, UK
Telephone +44 (0)20 7873 3000 ‣ **Facsimile** +44 (0)20 7873 3076
E-mail firstname.lastname@ft.com
www.ft.com

LES ECHOS
46 Rue la Boétie, Paris 75008, France
Telephone +33 149 53 6565 ‣ **Facsimile** +33 145 61 4892
E-mail initiallastname@lesechos.fr
www.lesechos.fr

RECOLETOS
Paseo de la Castellana 66, 28046 Madrid, Spain
Telephone +34 91 337 3220 ‣ **Facsimile** +34 91 337 3266
E-mail initiallastname@recoletos.es
www.recoletos.es