

Other financial information

Net finance costs

£ millions	2011	2010
Net interest payable	(55)	(73)
Finance income/(costs) in respect of retirement benefit plans	3	(12)
Net finance costs reflected in adjusted earnings	(52)	(85)
Other net finance (costs)/income	(19)	12
Total net finance costs	(71)	(73)

Net finance costs reported in our adjusted earnings comprise net interest payable and net finance costs relating to post-retirement plans.

Net interest payable in 2011 was £55m, down from £73m in 2010. Although our fixed rate policy reduces the impact of changes in market interest rates, we were still able to benefit from low average US dollar and sterling interest rates during the year.

Year-on-year, average three month LIBOR (weighted for the Group's net borrowings in US dollars and sterling at each year end) fell by 0.1% to 0.3%. This reduction in floating market interest rates helped drive the Group's lower interest charge. These low rates, coupled with interest income on deposits in higher yielding currencies created a decrease in the Group's average net interest payable from 7.9% to 6.5%. The Group's average net debt fell by £82m, reflecting the timing of the reinvestment during 2011 of the proceeds from the Interactive Data disposal.

Net finance income relating to post-retirement plans was £3m in 2011 compared to a net charge of £12m in 2010. Also included in the statutory definition of net finance costs are finance costs on put options and deferred consideration associated with acquisitions, foreign exchange and other gains and losses. Finance costs for put options and deferred consideration are excluded from adjusted earnings as they relate to future earn outs and similar payments on acquisitions and do not reflect cash expended. Foreign exchange and other gains and losses are excluded from adjusted earnings as they represent short-term fluctuations in market value and are subject to significant volatility.

These other gains and losses may not be realised in due course as it is normally the intention to hold the related instruments to maturity. In 2011, the total of these items excluded from adjusted earnings was a charge of £19m compared to a profit of £12m in 2010. The majority of the loss in 2011 relates to foreign exchange differences on a proportion of the unhedged US dollar proceeds from the Interactive Data sale. In 2010 the gain arose largely from foreign exchange on US dollar denominated debt.

Funding position and liquid resources

The Group finances its operations by a mixture of cash flows from operations, short-term borrowings from banks and commercial paper markets, and longer-term loans from banks and capital markets. Our objective is to secure continuity of funding at a reasonable cost from diverse sources and with varying maturities. The Group does not use off-balance sheet special purpose entities as a source of liquidity or for any other financing purposes.

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

£ millions	2011	2010
Cash and cash equivalents	1,369	1,736
Marketable securities	9	12
Net derivative assets	174	134
Bonds	(1,955)	(2,226)
Bank loans and overdrafts	(78)	(73)
Finance leases	(18)	(13)
Net debt	(499)	(430)

Through acquisition activity in 2011, the Group largely reinvested the proceeds of the Interactive Data disposal received in 2010, but these cash outflows were largely offset by cash generated from operations and the proceeds from the disposal of FTSE International, leading to a relatively minor change in the Group's net debt. Reflecting the geographical and currency split of our business, a large proportion of our debt is denominated in US dollars (see note 19 for our policy). The weakening of sterling against the US dollar during 2011 (from \$1.57 to \$1.55:£1) slightly increases the sterling equivalent value of our reported net debt.

Other financial information continued

The Group's credit ratings remained unchanged during the year. The long-term ratings are Baa1 from Moody's and BBB+ from Standard & Poor's, and the short-term ratings are P2 and A2 respectively. The Group's policy is to strive to maintain a rating of Baa1/BBB+ over the long term.

In June 2011, the Group repaid a \$500m bond on its scheduled maturity from available cash and cash equivalents.

The Group has a \$1,750m committed revolving credit facility which matures in November 2015. At 31 December 2011 this facility was undrawn. The facility is used for short-term drawings and providing refinancing capabilities, including acting as a back-up for our US commercial paper programme. This programme is primarily used to finance our US working capital requirements, in particular our US educational businesses which have a peak borrowing requirement in June. At 31 December 2011, no commercial paper was outstanding.

The Group also maintains other committed and uncommitted facilities to finance short-term working capital requirements in the ordinary course of business.

Further details of the Group's approach to the management of financial risks are set out in note 19 to the financial statements.

Taxation

The effective tax rate on adjusted earnings in 2011 was 22.4% as compared to an effective rate of 25.2% in 2010. Our overseas profits, which arise mainly in the US, are largely subject to tax at higher rates than that in the UK (which had an effective statutory rate of 26.5% in 2011 and 28% in 2010). These higher tax rates were offset by amortisation-related tax deductions and, in 2011, by prior year adjustments arising from settlements with tax authorities.

The reported tax charge on a statutory basis was £199m (17.2%) compared to a charge of £146m (21.8%) in 2010. The reduction in the statutory rate is largely due to the low tax charge on the gain on disposal of FTSE together with the effect of the prior year adjustments referred to above.

In total these two items outweighed the favourable effect in 2010 from recognition of tax losses and credits utilised in connection with the Interactive Data sale. The tax charge relating to that sale in July 2010 is included in the profit on discontinued businesses.

Tax paid in 2011 was £151m compared to £335m in 2010. The 2010 payment included £250m relating to the Interactive Data sale. After taking account of the Interactive Data sale, there were higher tax payments in 2011 in the US, following the use of the remaining available losses in 2010, and in the UK.

Discontinued operations

There are no discontinued operations in 2011. Discontinued operations in 2010 relate to Interactive Data Corporation which was sold in July 2010.

Non-controlling interest

In 2011 there are non-controlling interests in the Group's businesses in South Africa, China and India although none of these are material to the Group numbers. The non-controlling interest in the Group's Brazilian business, Sistema Educacional Brasileiro (SEB), was bought out in the first half of 2011. The non-controlling interest in 2010 comprised mainly the publicly-held share of Interactive Data for the period until its disposal in July 2010.

Other comprehensive income

Included in other comprehensive income are the net exchange differences on translation of foreign operations. The loss on translation of £44m in 2011 compares to a gain in 2010 of £173m. Although the Group is principally exposed to movements in the US dollar as a significant proportion of the Group's operations are based in the US, these movements have been less volatile over the course of the last two years and translation gains and losses have been relatively low. In 2010 the US dollar strengthened from an opening rate of £1:\$1.61 to a closing rate at the end of that year of £1:\$1.57. The dollar strengthened slightly again in 2011 closing at £1:\$1.55.

Also included in other comprehensive income in 2011 is an actuarial loss of £64m in relation to post-retirement plans. This loss arose largely because the discount rate assumptions used in the actuarial valuation contributed to an increase in the value of liabilities, offsetting further improvement in asset returns for the UK Group pension plan. In 2010 there was a gain of £71m which arose largely from improved asset returns.

Dividends

The dividend accounted for in our 2011 financial statements totalling £318m represents the final dividend in respect of 2010 (25.7p) and the interim dividend for 2011 (14.0p). We are proposing a final dividend for 2011 of 28p, bringing the total paid and payable in respect of 2011 to 42.0p, a 9% increase on 2010. This final 2011 dividend was approved by the board in February 2012, is subject to approval at the forthcoming AGM and will be charged against 2012 profits. For 2011, the dividend is covered 2.1 times by adjusted earnings.

We seek to maintain a balance between the requirements of our shareholders for a rising stream of dividend income and the reinvestment opportunities which we identify around the Group and through acquisitions. The board expects to raise the dividend above inflation, more in line with earnings growth, thereby maintaining dividend cover at around two times earnings in the long term.

Pensions

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

The charge to profit in respect of worldwide pensions and post-retirement benefits for continuing operations amounted to £93m in 2011 (2010: £102m) of which a charge of £96m (2010: £90m) was reported in operating profit and a net benefit of £3m (2010: net charge £12m) was reported against net finance costs.

The overall deficit on the UK Group plan of £5m at the end of 2010 has become a surplus of £25m at 31 December 2011. This decrease is principally due to continued deficit funding in the year together with improved asset performance. In total, our worldwide deficit in respect of pensions and post-retirement benefits fell from a deficit of £148m in 2010 to a deficit of £141m at the end of 2011.

Acquisitions

In May 2011 the North American Education business acquired Schoolnet, a leading provider of data-driven education software for students and teachers. In June 2011, the International Education business completed the acquisition of EDI plc, a UK-listed education services company operating primarily in the work based learning sector. In November 2011 the North American Education business acquired Connections Education, a company that operates online or virtual public schools in the US and in December 2011 the International Education business acquired Global Education and Technology Group, a leading provider of test preparation services for students in China who are learning English.

Also in the year to 31 December 2011, the Group completed the acquisitions of CTI Education in South Africa, Tutorvista in India, Stark Holding in Germany, TQ in the UK and various other smaller acquisitions.

Net cash consideration for all acquisitions made in the year ended 31 December 2011 including the purchase of the remaining minority in SEB was £896m and provisional goodwill recognised was £620m. In total, acquisitions completed in the year contributed an additional £129m of sales and £9m of operating profit before acquisition costs and intangible amortisation.

Return on invested capital (ROIC)

Our ROIC is calculated as total adjusted operating profit less cash tax, expressed as a percentage of average gross invested capital. ROIC decreased by 1.2 percentage points from 10.3% in 2010 to 9.1% in 2011. This decrease reflects the impact of the Interactive Data disposal, reinvestment of proceeds which (after integration costs) yield lower returns in their first year and higher tax payments following utilisation of US tax losses and settlements.

Other financial information continued

Capital expenditure

Net capital expenditure in the year on property, plant equipment and software amounted to £156m. The analysis of capital expenditure and details of capital commitments are shown in notes 10, 11 and 35 of the financial statements.

Related party transactions

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

Post balance sheet events

There were no significant post balance sheet events.

Supplier payment policy

Operating companies are responsible for agreeing the terms and conditions under which business transactions with their suppliers are conducted. These supplier payment terms vary by operating company reflecting the different industries and countries in which they operate. It is company policy that suppliers are aware of such terms of payment and that payments to them are made in accordance with these, provided that the supplier is also complying with all the relevant terms and conditions. Group trade creditors at 31 December 2011 were equivalent to approximately 32 days of purchases during the year ended on that date. The company does not have any significant trade creditors and therefore is unable to disclose average supplier payment terms.