



Combined Financial Statements 2006  
and Supplementary information  
presented in euros

Inspiring discovery

Reed Elsevier is a world leading provider of Science and Medical, Legal, Education and Business information and workflow solutions.

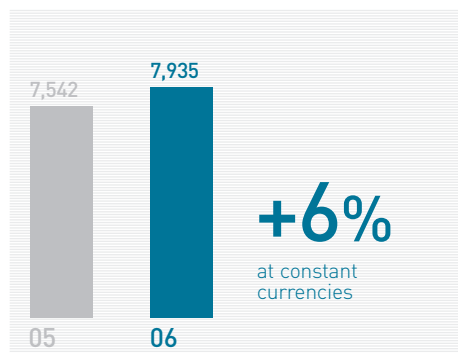
We create authoritative content delivered through leading brands and content driven solutions increasingly embedded in our customers' workflows. We enable our customers to work faster and more effectively.

We continually innovate to expand our product range to ensure that we are increasingly valued partners to our customers.

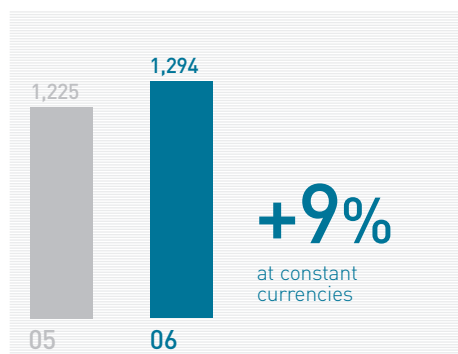
<b>Financial highlights</b>	01
<b>Operating and financial review</b>	02
<b>Reed Elsevier combined financial statements</b>	
Combined financial statements	24
Accounting policies	28
Notes to the combined financial statements	32
Independent auditors' report	61
<b>Directors' remuneration report</b>	62

## Financial highlights

### Revenue (€m)



### Adjusted operating profit (€m)



The 2006 financial results were encouraging. Revenues were up 6%, adjusted operating profits up 9% at constant currencies

## Reed Elsevier combined businesses

For the year ended 31 December	2006 €m	2005 €m	% Change	% Change at constant currencies
<b>Reported figures</b>				
Revenue	7,935	7,542	+5%	+6%
Operating profit	1,294	1,225	+6%	+9%
Profit before tax	1,060	1,023	+4%	+8%
Profit attributable to shareholders	916	675	+36%	+42%
Net borrowings	3,448	3,933		
<b>Adjusted figures</b>				
Operating profit	1,799	1,667	+7%	+9%
Profit before tax	1,546	1,463	+6%	+9%
Profit attributable to shareholders	1,170	1,101	+6%	+9%
Operating cash flow	1,693	1,577	+7%	+7%
Operating margin	22.4%	22.1%		
Operating cash flow conversion	95%	95%		

The Reed Elsevier combined businesses encompass the businesses of Reed Elsevier Group plc and Elsevier Reed Finance BV, together with their two parent companies, Reed Elsevier PLC and Reed Elsevier NV (the "Reed Elsevier combined businesses"). The results of Reed Elsevier PLC reflect its shareholders' 52.9% economic interest in the Reed Elsevier combined businesses. The results of Reed Elsevier NV reflect its shareholders' 50% economic interest in the Reed Elsevier combined businesses. The respective economic interests of the Reed Elsevier PLC and Reed Elsevier NV shareholders take account of Reed Elsevier PLC's 5.8% interest in Reed Elsevier NV.

Adjusted figures are presented as additional performance measures and are stated before the amortisation of acquired intangible assets, acquisition integration costs, disposals and other non operating items, related tax effects and movements on deferred tax balances not expected to crystallise in the near term. Reconciliations between the reported and adjusted figures are provided in the notes to the combined financial statements.

The percentage change at constant currencies refers to the movements at constant exchange rates, using 2005 full year average and hedge rates.

## Operating and financial review



**ELSEVIER**

Elsevier is a world leading provider of scientific, technical and medical information and solutions



LexisNexis is a global provider of authoritative legal, tax, regulatory, public records, news and business information and workflow solutions



Harcourt Education is a leading publisher serving the pre-Kindergarten to Grade 12 schools and assessment markets in the US and internationally



Reed Business is a leading global business-to-business publisher and exhibition organiser

## Introduction

Reed Elsevier is a world leading publisher and information provider. The principal operations are in North America and Europe and comprise science, medical, legal, education and business publishing. Total revenues for the year ended 31 December 2006 were €7,935m.

Reed Elsevier is well positioned in markets with attractive growth prospects and has a clear investment led growth strategy focused on building revenue momentum across all our businesses.

Long term growth in our markets is expected to be sustained by the continuing demand for professional information. In addition, professionals are looking for significant improvements in productivity through access to highly functional online services and associated workflow solutions.

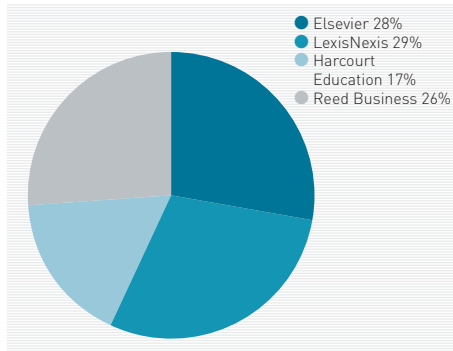
Following a detailed review, Reed Elsevier has sharpened its strategic focus to best capitalise on the growing digital opportunities in its markets. Reed Elsevier will derive the best returns on its brand franchises and digital investments by focusing on the science, medical, legal and business markets. Accordingly, Reed Elsevier has announced the planned sale of the Harcourt Education division.

### Forward looking statements

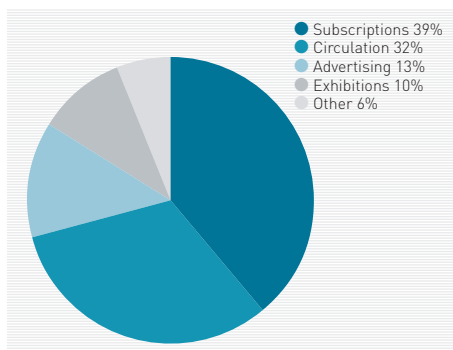
The Reed Elsevier Annual Reports and Financial Statements 2006 – supplementary information presented in euros contain forward looking statements within the meaning of Section 27A of the Securities Act 1933, as amended, and Section 21E of the Securities Exchange Act 1934, as amended. These statements are subject to a number of risks and uncertainties and actual results and events could differ materially from those currently being anticipated as reflected in such forward looking statements. The terms 'expect', 'should be', 'will be', and similar expressions identify forward looking statements. Factors which may cause future outcomes to differ from those foreseen in forward looking statements include, but are not limited to: general economic conditions and business conditions in Reed Elsevier's markets; exchange rate fluctuations; customers' acceptance of its products and services; the actions of competitors; legislative, fiscal and regulatory developments; changes in law and legal interpretation affecting Reed Elsevier's intellectual property rights and internet communications; and the impact of technological change.

## Strategy

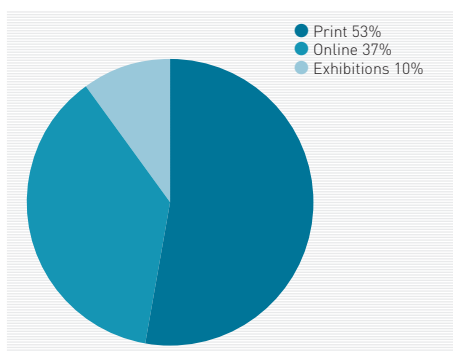
### Revenue by division



### Revenue by source



### Revenue by media



Reed Elsevier is well positioned in markets with attractive growth prospects and has a clear investment led strategy built around four priorities, closely linked to financial strategy

**Deliver authoritative content through leading brands.** Reed Elsevier delivers authoritative, and to a great extent proprietary, content of the highest quality through market leading brands. In its publications and services Reed Elsevier's professional customers find the essential data, analysis and commentary to support their decisions. Editorial investment and selective acquisitions are generating new sources of content to widen the product offering to customers, and to expand into new segments and geographic regions. As online information sources increase, Reed Elsevier's trusted leadership brands play an ever more vital role.

**Drive online solutions.** Over the last five years digital revenues have built to €2.9bn or 37% of total revenues. Authoritative information, technology enabled and increasingly integrated into customer workflows, is making Reed Elsevier's customers more effective professionally and making Reed Elsevier a more valued partner.

As Reed Elsevier's customers and core markets rapidly migrate online, there are opportunities to leverage its leadership brands and authoritative proprietary content. Digital technology enables Reed Elsevier to move up the value chain with its customers by providing a range of innovative solution orientated products that become embedded in their workflow. This will play a major part in Reed Elsevier's strategy going forward.

**Improve cost efficiency.** Digital growth and an increasingly synergistic portfolio provide opportunities to further leverage scale and commonalities across the business, sharing skill sets, resources and collective experience. Substantial cost savings have been made over the last five years, and there are further opportunities across the supply chain and in technology and infrastructure to continue this progress. Improving cost efficiency remains a fundamental feature of Reed Elsevier.

**Selective portfolio development.** In addition to significant internal investment, Reed Elsevier will continue to allocate capital and resources to pursue selective acquisition opportunities that accelerate its strategy and overall business progress. Reed Elsevier has spent €2.1bn on acquisitions over the last five years, focused on strong brands and proprietary content, customer workflow solutions, leading technologies and expansion into attractive adjacent markets, most notably in legal solutions, risk management, health and e-business.

### Financial strategy

Reed Elsevier expects progress in the development of its digital business to deliver good revenue growth and, with improvements in cost efficiency and organisational effectiveness, this will flow through at a higher rate to operating profitability. Additional financial benefits are delivered through leverage and fiscal efficiency. With an increasing and substantial portion of the revenues being delivered by subscription based products and the trend to longer term contracts, Reed Elsevier will be a more consistent business.

Reed Elsevier aims to distribute 70-80% of free cash flow through dividends and share buybacks. The balance will be invested in the business, mainly through acquisitions, so maintaining capital efficiency aligned to its strategy. Reed Elsevier's capital will be invested in growth areas which will make sustainable returns in excess of the risk adjusted cost of capital. Reed Elsevier aims to maintain its credit rating in order to take advantage of opportunities within its markets and access the cheapest sources of borrowing.

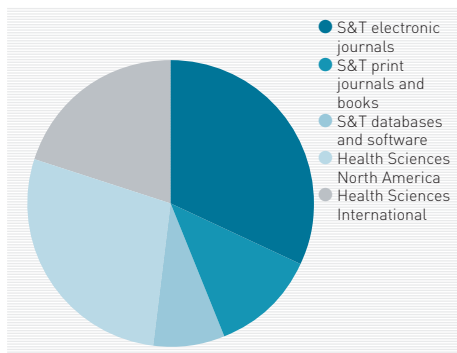
This business and financial strategy is directed at delivering good revenue growth, continuous margin improvement, strong cash generation and growing returns on capital. These are targeted to deliver consistent adjusted earnings per share growth of a minimum 10% annually at constant currencies. Our incentive programmes are designed in support of these strategies and in creating shareholder value.

## Description of business

### Elsevier

Elsevier provides its customers with scientific, technical and medical content and tools that improve productivity in research, healthcare and health education. Total revenues for the year ended 31 December 2006 were €2,236m. Elsevier is a global business with principal operations located in Amsterdam, London, Oxford, New York, Philadelphia, St Louis, San Francisco, Paris, Munich, Madrid, Singapore, Tokyo and Delhi.

#### Elsevier portfolio



Elsevier serves a global network of 7,000 editors, 70,000 editorial board members, 200,000 referees, and more than 500,000 authors. Its products reach more than 10 million researchers in 4,500 institutions, 5 million students, and 15 million doctors, nurses and health professionals.

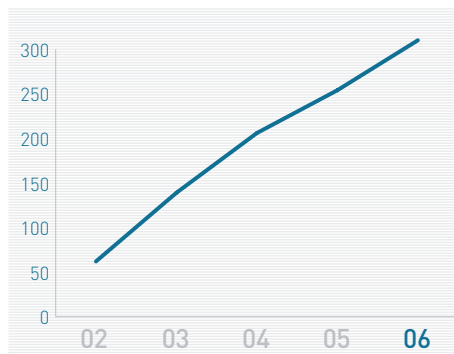
Growth in the scientific information market is driven by increases in research output, R&D spend, the number of researchers worldwide, and the need for improved research efficiency. In healthcare, growth is driven by advances in medical science and the shift from activity-based to outcomes-based models of patient care and associated demands for increased productivity.

The Science & Technology division of Elsevier is the world's leading global academic journal publisher. Its customers are the world's libraries, scientists and professionals, who rely on Elsevier to provide high quality content, to review, publish, disseminate, and preserve research findings, and to

Elsevier provides its customers with scientific, technical and medical content and tools that improve productivity in research, healthcare and health education

create innovative workflow tools to improve their efficiency in using that information. Each year Science & Technology publishes over 170,000 new research articles in some 1,200 journals and over 1,000 new book titles, as well as secondary material in the form of supporting bibliographic data, indexes and abstracts, and tertiary information in the form of review and reference works. Its flagship electronic product, ScienceDirect, is the world's largest database of journal articles and is accessed by over 10 million users each year. ScienceDirect holds over 8 million scientific articles and an expanding portfolio of books online, which currently includes 55 major reference works, 151 book series and seven handbooks in 170 volumes.

#### ScienceDirect online usage



Full text article downloads (millions)

Elsevier's growing online offerings also include Scopus, an abstract and index database and navigational tool, which now has nearly 30 million abstracts of scientific research articles from 15,000 peer reviewed publications, over 15 million patents, and references to over 200 million web pages.

The Health Sciences division of Elsevier serves medical researchers, practising professionals, educators and students globally. It publishes over 700 journals, including a number of journals for learned societies, and over 2,000 book titles and clinical reference works annually. Growth in electronic health information is accelerating and the business continues to expand its portfolio of online health information tools for education, practitioner reference, and point of care decision making. Elsevier's

clinical reference and decision support products include MD Consult, which now has over 7.5 million page views per month and more than 1,700 institutional customers. Health Sciences provides online and multimedia products for use by both medical faculties and students to support core textbooks, including Evolve, which now has more than 700,000 registered users and, through the acquisition of Health Education Systems Inc diagnostic tests for nursing and allied health markets. Internationally, Elsevier leverages its print and online content into new markets through foreign language versions.

Elsevier aims to make valued contributions to the science and health communities by combining world class content with productivity enhancing solutions for scientific researchers and health professionals worldwide. Its key strategic areas of focus are: quality of content; customer service and customer relations; development of productivity enhancing online solutions; expanded penetration of high growth markets; and organisational efficiency.



↑ **Scopus** The world's largest abstract and citation database of scientific research, Scopus indexes the bibliographic information of 15,000 titles from 4,000 different publishers and covers all scientific disciplines.

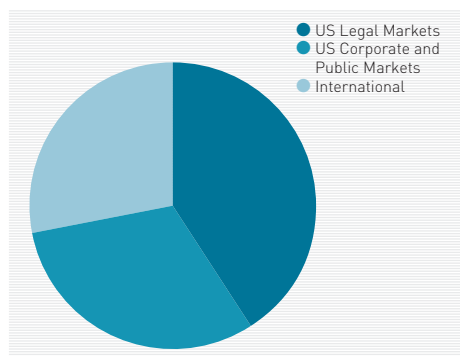
LexisNexis provides legal, tax, regulatory, risk management, information analytics and business information solutions aligned to the workflow of professional, business and government customers internationally

Elsevier's print science journals are generally sold to libraries on a paid subscription basis, with subscription agents facilitating the administrative process. Medical and healthcare print journals are mostly sold to individuals through direct mail and learned societies. Electronic products are generally sold directly to libraries, hospitals, corporations and end users. Books are sold through book stores, both traditional and online, wholesalers and, particularly in medical and healthcare markets, directly to end users. Competition within the science and technology and medical publishing fields is generally on a title by title and product by product basis. Competing journals, books and databases are typically published by learned societies and other professional publishers.

### LexisNexis

LexisNexis provides legal, tax, regulatory, risk management, information analytics and business information solutions aligned to the workflow of professional, business and government customers internationally. Total revenues for the year ended 31 December 2006 were €2,308m.

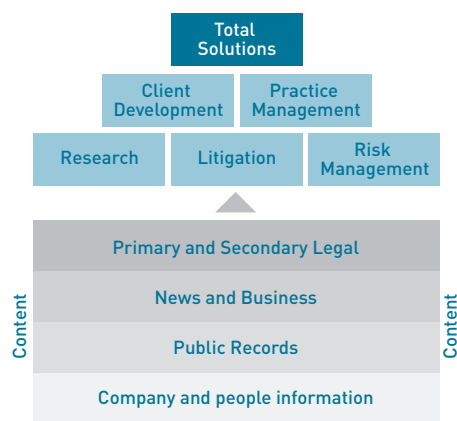
### LexisNexis portfolio



Legal and regulatory markets worldwide are seeing continuing growth driven by the increasing level of legislation and litigation, as well as the increasing number of lawyers. Additional opportunities are also developing beyond the core research market, through the delivery of value added solutions to meet demands for greater legal efficiency and productivity.

Increasingly legal information and services are being delivered online, with considerable potential to deliver such products and solutions in markets outside the United States where online migration is at significantly lower levels than in the US legal market. In recent years, LexisNexis has, with its comprehensive US public records databases, expanded in the market for risk management and information analytics. This is growing rapidly due to increasing consumer credit losses and fraud and the demand for identity verification.

LexisNexis in the United States offers legal information products in electronic and print formats to law firms and practitioners, law schools, corporate and tax counsel and federal, state and local governments. Headquartered in New York, the principal operations are located in Ohio, New York, Colorado, New Jersey and Florida.



↑ LexisNexis Total Solutions help legal and other professionals achieve excellence with products and solutions in Client Development, Research, Practice Management, Litigation Services, Risk Management and Information Analytics.

US Legal Markets' Total Solutions help legal professionals achieve excellence in the business and practice of law with products and solutions in Client Development, Research, Practice Management and Litigation Services. Client Development solutions include the Martindale Hubbell electronic network that showcases the qualifications and credentials of over one million lawyers and law firms

worldwide, a suite of business intelligence tools that help lawyers find and target clients, and customer relationship management workflow tools. In Research, the division provides statutes and case law for all 50 US states as well as research, analysis and citation services from Matthew Bender, Michie and Shepard's. Practice Management solutions include time and billing, case management, cost recovery and document management. Litigation Services include a range of workflow solutions for litigators including electronic discovery, evidence management, case analysis, court docket tracking, e-filing, expert identification and legal document preparation.

The Corporate and Public Markets division offers LexisNexis products and services to corporations, federal government agencies and academic institutions together with news, business, financial and public records content. Its risk management and information analytics applications are designed to assist customers in managing risk through fraud detection and prevention, identity verification, pre-employment screening and due diligence.



↑ Lexis.com provides an integrated set of legal research tools including legal, news, business and public records content.

Outside the United States, LexisNexis International serves markets in Europe, Canada, Africa, Asia Pacific and Latin America with a range of local and international legal, tax, regulatory and

## Description of business continued

business information in electronic and print formats. The most significant businesses are in the UK and France.

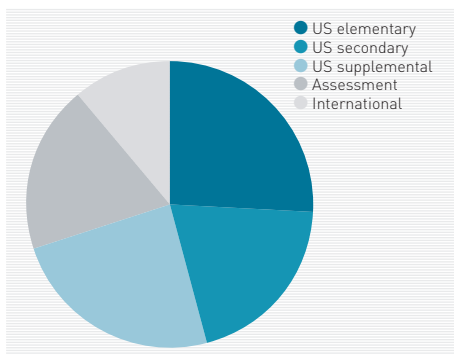
LexisNexis aims to be the leading provider of productivity enhancing information and information-based workflow solutions in its markets. The key strategic areas of focus are: to expand the business from research into Total Solutions; to grow a significant business in risk management and information analytics; to expand internationally through innovative online products and solutions; and to continuously improve cost effectiveness.

LexisNexis's principal competitor in US legal markets is West (The Thomson Corporation), while the principal competitors in US corporate and public markets are West, Factiva (Dow Jones) and Choicepoint. Major international competitors include The Thomson Corporation, Wolters Kluwer and Factiva.

## Harcourt Education

Harcourt Education publishes school textbooks and related instructional and assessment materials, principally in the United States, the United Kingdom, Australia, New Zealand and southern Africa. Headquartered in New York, the principal operating locations are in Florida, Texas and Oxford. Total revenues for the year ended 31 December 2006 were €1,307m.

### Harcourt portfolio



Growth in Harcourt Education's markets is driven by long standing commitments to improve educational standards. Such commitments remain strong and

Growth in Harcourt Education's markets is driven by long standing commitments to improve educational standards

require sustained investment in proven educational programmes. In recent years, there has also been further emphasis on the measurement of the educational results of students, both to monitor and assist improvement in individual educational outcomes and to improve accountability. Overall funding for education is expected to continue to increase.

In the United States, Harcourt School Publishers is a publisher of print and technology enabled instructional materials for students in kindergarten to 6th grade. Holt, Rinehart and Winston offers educational textbooks and related instructional materials for students in middle and secondary schools. The major customers of Harcourt Education's US schools publishing businesses are state boards of education and local district and school boards.

Of the 50 US states, 20 periodically purchase educational programmes through an adoption process. This process entails state education committees approving a shortlist of education materials from which school districts can purchase. The remaining 30 states without an adoption process, known as open territories, allow individual school districts to purchase any educational programmes.

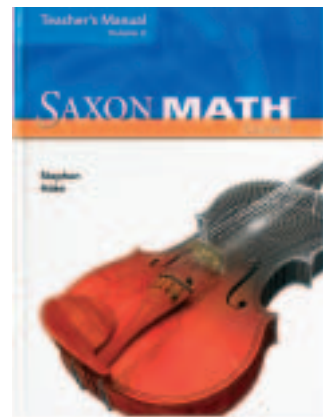
Harcourt Education has achieved strong market performances in recent years both in the adoption states and open territories based on strong curriculum product in key subjects such as reading and literature, science and health and elementary maths and social studies.

Harcourt Achieve is a publisher of supplemental school and adult education materials as well as providing professional development services for teachers. Greenwood-Heinemann publishes monograph and reference lists and professional resources for teachers.

Harcourt Assessment develops assessment products and services for elementary, secondary and higher education as well as tests for practising

and research psychologists. In educational testing, it provides a range of achievement, aptitude and guidance testing services for measuring student progress. It is well known for the Stanford Achievement Test, now in its 10th edition. In clinical testing, it provides psychologists with assessment tests for many aspects of human behaviour, intelligence and development. The Wechsler products, including the Wechsler Preschool and Primary Scale of Intelligence, are licensed for publication in over 30 countries.

Outside the United States, Harcourt Education International is a provider of textbooks and related instructional materials to the UK primary, secondary and vocational schools and college markets through the Heinemann, Rigby and Ginn imprints and other English language markets in Australia, New Zealand and southern Africa.



↑ **Saxon Math** The Saxon Math series for US schools grades K-12 provides an incremental approach to instruction that delivers measurable student improvement – as shown by years of research.

Harcourt Education aims to be the leading provider of educational resources to improve student performance. The key strategic areas of focus are: to sustain high quality, effective product through strong editorial processes in new publishing and continuous innovation; to expand online teaching and assessment resources; to deepen customer relationships to become the provider of choice of customised solutions; and to improve cost effectiveness through further upgrade of organisational

Business to business magazines and community websites provide an effective marketing channel through which advertisers reach their target audiences. Reed Exhibitions organises trade exhibitions and conferences internationally, with 460 events in 38 countries

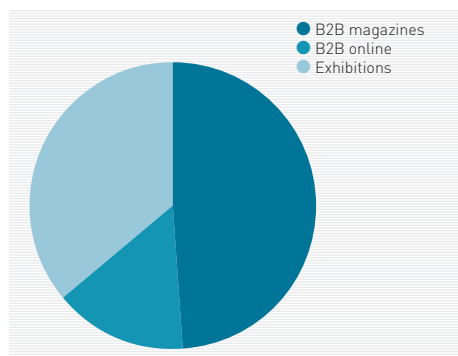
capabilities, investment in technology and cost reduction.

The principal competitors of Harcourt Education are Pearson, McGraw Hill and HM Riverdeep.

## Reed Business

Reed Business provides information and marketing solutions to business professionals in the United States, the United Kingdom, continental Europe, Australia and Asia. The division also organises trade exhibitions internationally. Total revenues for the year ended 31 December 2006 were €2,084m.

### Reed Business portfolio



Business to business magazines and community websites provide an effective marketing channel through which advertisers reach their target audiences, increasingly delivered through leading brands in each sector. Alongside print magazines, demand is growing for online products which provide improvements in productivity through quicker and easier access to more comprehensive and searchable data. Business to business marketing spend has been driven historically by levels of corporate profitability, which itself has followed overall growth in GDP and business investment.

Reed Business Information publishes over 400 trade magazines, directories, newsletters and loose leaf publications, and over 200 websites and online services. Important magazine titles include Variety and Interior Design in the United States; Computer Weekly, Estates

Gazette, Flight International and New Scientist in the United Kingdom; and Elsevier and FEM in the Netherlands. Reed Business Information also publishes directories in selected markets. Through its Reed Construction Data business, it provides nationwide coverage of construction project information for the United States.

In the majority of Reed Business Information's sectors, strong demand is being seen for online services. Reed Business Information has been particularly successful in developing online products and services, which have been growing at over 20% per annum and now account for 24% of Reed Business Information revenues. These products include totaljobs.com, a major online recruitment site in the UK; ICIS-LOR, a global information and pricing service for the petrochemicals sector; zibb.nl, a business information service in the Netherlands; and Kellysearch.com, an industrial search engine which is being launched internationally.



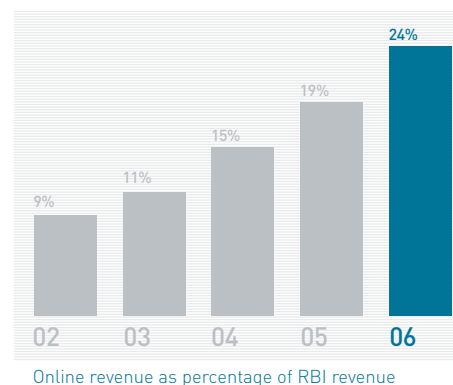
↑ **totaljobs.com** is the UK's leading commercial recruitment website, attracting nearly 2 million unique jobseekers every month. With over 100,000 vacancies at any one time, totaljobs.com is one of the UK's fastest growing online recruitment businesses.

Reed Exhibitions organises trade exhibitions and conferences internationally, with 460 events in 38 countries, attracting over 90,000 exhibitors and more than six million visitors annually. Its exhibitions and conferences encompass a wide

range of sectors including IT, manufacturing, aerospace, leisure, electronics, food and hospitality, travel and entertainment. Increasingly Reed Exhibitions is also developing online services to increase the effectiveness and efficiency of its trade shows.

Reed Business aims to be the first choice of business professionals for information and decision support in its individual markets and for marketing services. Its key strategic areas of focus are: to continue to grow rapidly existing and new online products and services in key markets; to continue to develop print franchises through brand extensions and redesign; to further upgrade the portfolio through investment, acquisition and divestment; to expand geographically in fast growing markets; and to continuously improve organisational effectiveness through investment in people, further development of online competencies, and cost reduction programmes.

### RBI online revenue



Business to business magazines are primarily distributed on a "controlled circulation" basis in the United States, whereby the product is delivered without charge to qualified buyers within a targeted industry group based on circulation lists developed and maintained by the publisher. Magazines distributed on this basis are wholly dependent on advertising for their revenues. In the United Kingdom, business magazines are distributed both on a "controlled circulation" basis and a "paid circulation" basis. In the Netherlands, a higher proportion of

## Resources and investment

publications is sold by "paid circulation". Distribution of magazines is conducted primarily through national postal services, supplemented by news-stand sales through unaffiliated wholesalers. Online products and services are generally sold through dedicated sales forces and intermediaries, including revenue sharing arrangements with other online service providers, and by direct promotion. Exhibition space is sold through industry specific and national sales teams.

Reed Business Information's titles compete with a number of publishers on a title by title basis in individual market sectors, the largest competitors being: Advanstar, CMP Media (United Business Media), Hanley Wood, McGraw Hill, Prism and Nielsen in the United States; EMAP Business Communications, Nielsen and CMP Media in the United Kingdom; and Wolters Kluwer and Nielsen in the Netherlands. Reed Business Information competes for online advertising with other business-to-business websites as well as Google and other search engines. Competition in trade exhibitions and conferences is very fragmented. Within the United States, the main competitor is Nielsen. Outside the United States, competition comes primarily from industry focused trade associations and convention centre and exhibition hall owners.



↑ **Variety** is the entertainment and media industry's premier source of news and analysis. The Chinese edition is published biweekly.

Reed Elsevier's most important resources are its intangible publishing assets and its workforce of some 36,800 employees.

### Market leading brands

Reed Elsevier's businesses own numerous market leading brands, imprints, titles and technology platforms.

Within Elsevier, ScienceDirect is the world's largest full text online scientific research service. Many of Elsevier's journals are the foremost publications in their field and a primary point of reference for new research. The Lancet has been publishing medical research, news and analysis since 1823. Similarly, Elsevier's booklist contains numerous pre-eminent and long standing titles.



↑ **The Lancet** is a leading independent and authoritative journal in global medicine. It was first published in 1823.

Within LexisNexis, lexis.com is recognised as one of the foremost online research tools for practising lawyers, providing subscribers with access to 5 billion searchable documents. The Shepard's Citations Service is a well known and highly reputed reference resource ("Shepardizing" is a common process for US lawyers checking the authority of cases or statutory references).

Many of the Harcourt Education brands and imprints, including Harcourt School and Holt, Rinehart & Winston have

maintained market leading positions for over fifty years. The Stanford Achievement Test Series is the most widely recognised educational achievement test in the United States.

Reed Business's well known magazine titles such as Variety, Estates Gazette and Elsevier are widely read for their authoritative content and up to date industry intelligence, while many of the Reed Exhibitions shows, which include World Travel Market, Mipim, MIDEM, Batimat and the PGA Merchandise Show, are acknowledged as the premier marketing events in their field.



↑ **Reed Exhibitions** is the world's leading events organiser. With over 460 events in 2006, it brought together over six million industry professionals from around the world.

### Investment

Reed Elsevier maintains and enhances the value of its intangible assets through continuous investment in the brands and imprints, new publishing, innovative product and market development, and in the technology platforms and publishing infrastructure on which they are based. Increasingly, investment is being made in developing digital workflow solutions.

Within Elsevier, the most significant investments in recent years have been in the ScienceDirect platform, digitisation of the archive of over 8 million research articles, and in the Scopus database. Other significant areas of investment have been in new online clinical reference tools and other e-health products and in online editorial and production systems.

## Resources and investment continued

In LexisNexis, substantial investment has been made in Total Solutions offerings such as Total Litigator and Total Practice Advantage. Alongside this, major investments have been made in technology, in particular in online research functionalities and in the development of the global online delivery platform. These investments are critical to providing integrated workflow solutions to our customers. Significant investment has also been made in new content development and in expanded sales and marketing activities. A major second data centre expanded operational capabilities and provides greater flexibility in continuous delivery.

Harcourt Education maintains significant and expanding investment in new educational textbook programmes and online technology resources, and has continued to develop its classroom based online assessment product and the Unison scoring, administration and reporting platform.

Within Reed Business, the focus has been on developing new online products and services, including webzines, recruitment sites, search and subscription information and data services. Ongoing investment includes the international expansion of the Kellysearch online industrial search engine and the continuing development of the successful totaljobs.com online recruitment website together with investment in the enabling infrastructure for all these web services. Reed Exhibitions has continued to expand its portfolio through new launches and geographical expansion.

These investments are largely embedded within the cost base of the businesses as new product development and market initiatives are a continuous activity.

Reed Elsevier's most important resources are its intangible publishing assets and its workforce of 36,800 employees

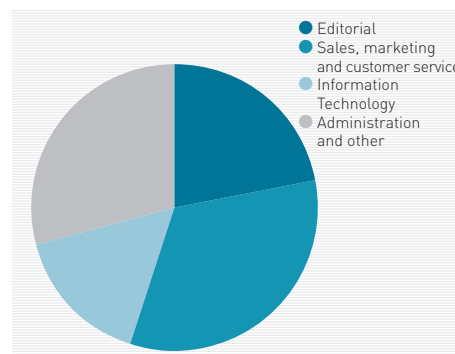
### Workforce

Reed Elsevier's workforce is highly skilled and a large proportion are graduates. We employ some 6,000 IT specialists and developers, 8,000 editorial staff, and some 12,000 specialist marketing, sales and customer service staff. Reed Elsevier aims to be an employer of choice, known for its best practices in recruiting and developing employees.

We seek to employ a workforce which reflects the diversity of our customers and communities. Our labour and employment practices are consistent with the principles of the United Nations Global Compact regarding fair and non-discriminatory labour practices. Every two years or so we conduct a global employee opinion survey to identify areas for improvement. Every employee in the company takes part in the annual Personal Development Programme, which reviews skills and performance and identifies opportunities for recognition and advancement. The Personal Development Programme is also the primary tool for assessing and planning employee training.

Reed Elsevier's remuneration policies are designed to attract, retain and motivate employees of the highest calibre and experience needed to shape and execute strategy. The remuneration packages of the directors and senior executives comprise a balance between "fixed" remuneration and "variable performance related" incentives, including a variable annual cash bonus based on achievement of financial performance measures and individual key performance objectives, and longer term incentive schemes. Pension scheme membership is offered to all employees in the United Kingdom, the Netherlands, the United States and a number of other countries.

### Workforce



## Risks

The key risks facing Reed Elsevier arise from the highly competitive and rapidly changing nature of our markets

The key risks facing Reed Elsevier arise from the highly competitive and rapidly changing nature of our markets, the increasingly technological nature of our products and services, the international nature of our operations, and legal and regulatory uncertainties. Certain businesses are also affected by the impact on publicly funded customers of changes in funding and by cyclical pressures on advertising and promotional spending. Reed Elsevier has an established risk management procedure that is embedded into the operations of the businesses and is reviewed by the Boards and Audit Committees. Important specific risks that have been identified and are being addressed include:

- Reed Elsevier's businesses are dependent on the continued acceptance by our customers of our products and services and the prices which we charge for them. We cannot predict whether there will be changes in the future which will affect the acceptability of products, services and prices to our customers.
- We are investing significant amounts to develop and promote electronic products and platforms. The provision of these products and services is very competitive and is to some extent subject to factors outside our control such as competition from new technologies and changes in regulation. There is no assurance that this investment will produce satisfactory long term returns.
- Reed Elsevier's businesses are increasingly dependent on electronic platforms and networks, primarily the internet, for delivery of products and services. Although plans and procedures are in place to reduce such risks, our businesses could be adversely affected if their electronic delivery platforms and networks experience a significant failure, interruption, or security breach.

- Our products and services are largely comprised of intellectual property content delivered through a variety of media. We rely on trademark, copyright, patent and other intellectual property laws to establish and protect our proprietary rights in these products and services. However, there is a risk that our proprietary rights could be challenged, limited, invalidated or circumvented.
- We operate a number of pension schemes around the world, the largest schemes being of the defined benefit type in the UK, the US and the Netherlands. The assets and obligations associated with defined benefit pension schemes are particularly sensitive to changes in the market values of assets and the market related assumptions used to value scheme liabilities.
- Our businesses operate in over 100 locations worldwide and our earnings are subject to taxation in many differing jurisdictions and at differing rates. We seek to organise our affairs in a tax efficient manner, taking account of the jurisdictions in which we operate. However, tax laws that apply to Reed Elsevier businesses may be amended by the relevant authorities. Such amendments, or their application to Reed Elsevier businesses, could adversely affect our reported results.

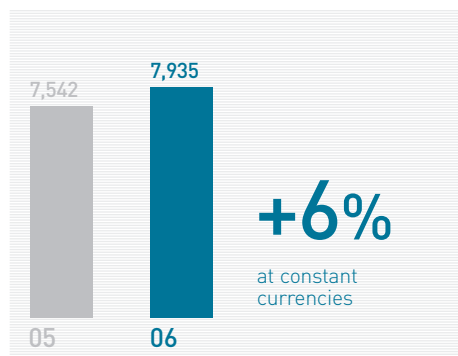
The Reed Elsevier combined financial statements are expressed in pounds sterling and euros and are, therefore, subject to movements in exchange rates on the translation of the financial information of businesses whose operational currencies are other than sterling and euros. The United States is our most important market and, accordingly, significant fluctuations in the US dollar exchange rate could significantly affect our reported results.

Further details on risk management and internal control procedures are set out in the Structure and Corporate Governance report within the Reed Elsevier Annual Reports and Financial Statements 2006 on pages 26 to 31.

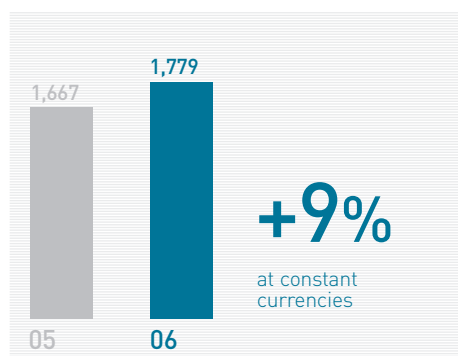
We recognise that Reed Elsevier and its businesses have a direct impact on the environment, principally through the use of energy and water and waste generation and in our supply chain through paper use and print and production technologies. We are committed to reducing these impacts, whenever possible, by limiting resource use and by efficiently employing sustainable materials and technologies. We require our suppliers and contractors to meet the same objectives. We seek to ensure that Reed Elsevier's businesses are compliant with all relevant environmental legislation and, accordingly, whilst environmental issues are important, we do not consider that they constitute a significant risk for Reed Elsevier.

## Operating review

### Revenue (€m)



### Adjusted operating profit (€m)



Adjusted figures and constant currency growth rates are used by Reed Elsevier as additional performance measures and are defined on page 20. Unless otherwise indicated, all percentage movements in the operating review refer to performance at constant exchange rates.

Reported figures are reconciled to the adjusted figures in the notes to the combined financial statements. Unallocated items comprise corporate costs, return on pension scheme assets and interest on pension scheme liabilities.

Reed Elsevier combined businesses	2006 €m	2005 €m	Change at constant currencies
<b>Revenue</b>			
Elsevier	2,236	2,097	+8%
LexisNexis	2,308	2,140	+8%
Harcourt Education	1,307	1,315	0%
Reed Business	2,084	1,990	+5%
<b>Total</b>	<b>7,935</b>	7,542	+6%
<b>Adjusted operating profit</b>			
Elsevier	683	655	+10%
LexisNexis	559	493	+13%
Harcourt Education	190	235	-19%
Reed Business	354	313	+14%
Unallocated items	(7)	(29)	
<b>Total</b>	<b>1,779</b>	1,667	+9%

## Divisional performance summary

Elsevier delivered revenues and adjusted operating profits ahead 8% and 10% respectively at constant currencies, or 5% and 8% before acquisitions and disposals. Growth was driven by strong subscription renewals and widening distribution of its scientific and medical journals and databases, as well as new online product sales and a successful book publishing programme. In Health, our market strategies in electronic health information services are accelerating through the launch of electronic reference materials, medical education resources, and specialist information services and workflow tools to enhance the efficacy of clinical diagnosis and treatment.

LexisNexis saw revenues and adjusted operating profits up 8% and 13% respectively at constant currencies, or 7% and 13% before acquisitions. Subscription renewals were strong, good growth was seen in new sales of its online information solutions both in the US and internationally, and in the Risk Information and Analytics business. The Total Solutions strategy launched in the year has gained good traction in the market, focused on the distinctive needs of lawyers across major areas of their workflow. In Risk Information and Analytics, the Seisint business saw strong revenue growth and delivered a 10% post tax return in only its second full year of ownership.

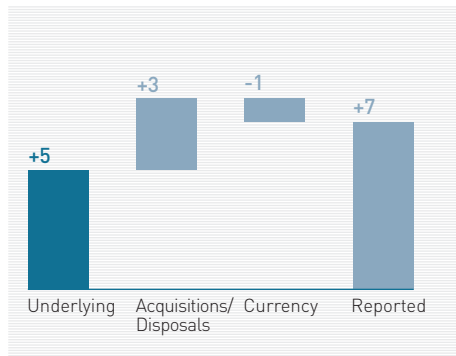
Harcourt Education held revenues flat at constant currencies despite a weaker market. Adjusted underlying operating profits were 20% lower, largely reflecting investment ahead of the much stronger 2007 state textbook adoption market and the significant impact of underperformance and contract cost overruns in Assessment. Harcourt's US basal and supplemental businesses performed well to grow revenues 1% against a textbook market estimated to be down 6%. Harcourt won the leading share, at 38%, in the new state textbook adoptions in which it participated and the supplemental business saw a good market response to its new publishing.

Reed Business revenues and adjusted operating profits were up 5% and 14% respectively at constant currencies, both in total and underlying. The online information services grew at over 20%, more than compensating for print migration, and the Exhibition business performed strongly. Reed Business has grown its digital revenues to \$400m over the last five years almost entirely through organic investment and new product launches, leveraging its brands, content and market positions. With 24% of the revenues of the magazines and information businesses now from online services, the overall growth trajectory is encouraging.

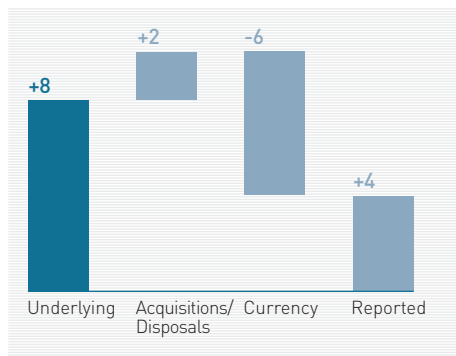
Elsevier

www.elsevier.com

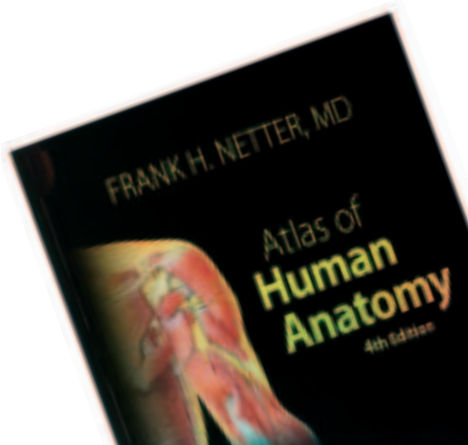
## Revenue growth (%)



## Adjusted operating profit growth (%)



↓ **Netter** A new 4th edition Netter's Atlas of Human Anatomy was published in June 2006. It contains over 940 illustrations of the human body with unsurpassed clarity and accuracy.



Elsevier had strong subscription renewals, widening distribution of its scientific and medical journals and databases, growing new online product sales and a successful book publishing programme

	2006 €m	2005 €m	Change at constant currencies
<b>Revenue</b>			
Science & Technology	1,164	1,146	+4%
Health Sciences	1,072	951	+13%
	<b>2,236</b>	2,097	+8%
<b>Adjusted operating profit</b>	<b>683</b>	655	+10%
Adjusted operating margin	<b>30.6%</b>	31.3%	+0.7pts

Revenues and adjusted operating profits were ahead 8% and 10% respectively at constant currencies, or 5% and 8% before acquisitions and disposals. Underlying operating margins were 0.9 percentage points ahead before acquisition and currency effects, driven by revenue growth, stabilising investment levels and further supply chain efficiency.

The Science & Technology business saw organic revenue growth of 5% at constant currencies reflecting strong journal subscription renewals, at 97%, widening distribution through an expanded sales force, and good growth in online databases. ScienceDirect usage continues to grow at over 20% and e-only contracts now account for 45% of journal subscription revenues. The Scopus abstract and indexing database has been well received in the market and is seeing good conversion of trials into firm contracts.

Early in the year, the Science & Technology business was reorganised into a more market-focused organisation, to better serve large academic and government institutions as well as to focus more directly on smaller and mid sized institutions, the corporate sector, and societies and individuals. Customer satisfaction scores have significantly improved during the year as a result of the sustained programme to improve service levels, and new products and marketing strategies are being developed for under-penetrated segments.

In Health Sciences, revenue growth was 13% at constant currencies, or 6% underlying. Strong growth was seen in the nursing and allied health professional sectors and in new society

journal publishing. Online revenues are growing rapidly, up 37% in total, as the medical community increasingly adopts online information services to drive productivity and enhance outcomes. The year saw increasing penetration of the ScienceDirect and MDConsult products and further launches made and planned of electronic reference materials, medical education resources, and specialist information services and workflow tools.

The integration of the MediMedia MAP businesses acquired in August 2005 is now complete, with revenue growth initiatives building momentum and adjusted operating margins improved significantly. The acquisition in May of the Gold Standard drug information database and related products is accelerating our market strategies in electronic health information services to enhance the efficacy of clinical diagnosis and treatment. In December, the Endeavor software business was sold following a reappraisal of its position within Elsevier's overall market strategies.

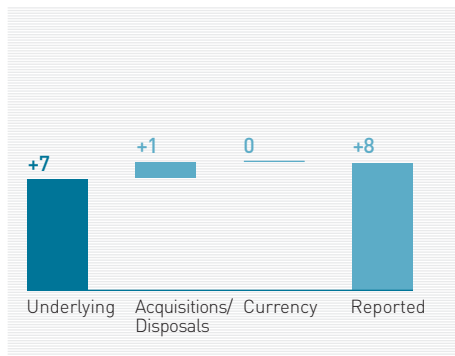
At reported exchange rates, adjusted operating margins were 0.7 percentage points lower largely reflecting the low, but rapidly improving, margins of the MediMedia acquisition made in 2005 as well as the impact of the rolling three year currency hedging programme as the US dollar decline over the last few years works its way through the hedge rates.

The outlook for Elsevier is positive. Subscription renewals are strong, customer satisfaction is improving, our publishing programmes are expanding, new electronic product is developing well, and distribution is widening.

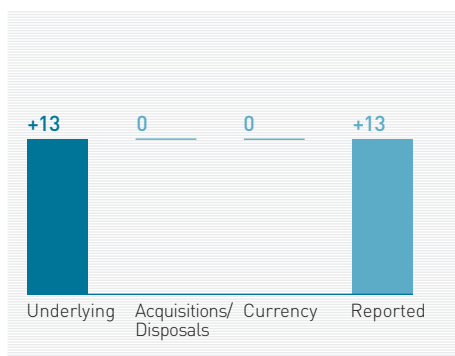
## LexisNexis

www.lexisnexis.com

## Revenue growth (%)



## Adjusted operating profit growth (%)



↓ **LexisNexis Total Litigator** provides US litigators with a complete and integrated set of online tools and services to assist them in managing cases through each step of the litigation process.



LexisNexis saw strong subscription renewals, good growth in new sales of its online information solutions both in the US and internationally, and further good growth in risk information and analytics

	2006 €m	2005 €m	Change at constant currencies
<b>Revenue</b>			
United States	1,660	1,549	+8%
International	648	591	+9%
	<b>2,308</b>	2,140	+8%
<b>Adjusted operating profit</b>	<b>559</b>	493	+13%
Adjusted operating margin	<b>24.2%</b>	23.1%	+1.1pts

Revenues and adjusted operating profits were up 8% and 13% respectively at constant currencies, or 7% and 13% before acquisitions. This 7% organic revenue growth compares with 6% in 2005 and 4% in 2004 and reflects the strengthening momentum in the business. The adjusted operating margin was 1.1 percentage points higher reflecting the good revenue growth and tight cost control.

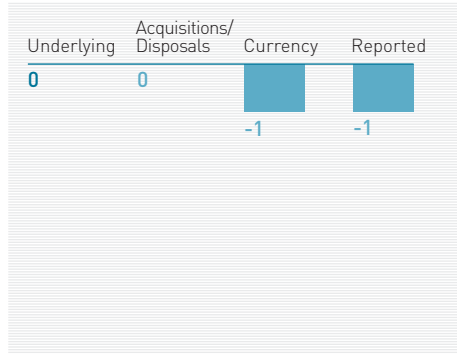
In US Legal Markets, strong subscription renewals and additional online information and solutions sales to both large and small firms drove organic growth of 6%. The Total Solutions strategy launched in the year has gained good traction in the market, focused on the distinctive needs of lawyers across four major areas of their workflow: litigation, client development, research and practice management. An integrated solutions product was also launched for the risk management market. The product portfolio was expanded through organic development and selective acquisition: Casesoft (litigation case analysis), Dataflight (online repository and tools for evidence management).

In Corporate and Public Markets organic revenue growth was 8% with continued strengthening in online news and business information, higher patent volumes and strong demand in risk management. The Seisint business acquired in September 2004 saw continued strong revenue growth and LexisNexis' existing risk management business has now been fully migrated to the Seisint technology platform. The Seisint business delivered a 10% post tax return in only its second full year of ownership, and returns continue to grow.

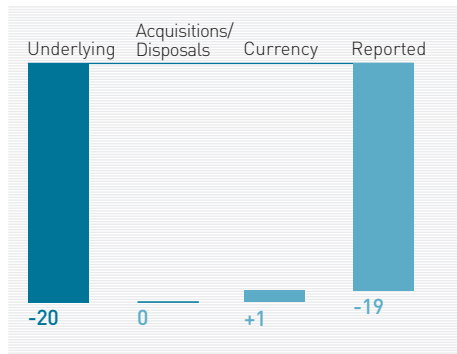
The LexisNexis International business outside the US saw underlying revenue growth of 8% driven by the growing demand for LexisNexis' online information services across its markets and new publishing. The Total Solutions strategy is also being rolled out in these international markets behind increasing online penetration. In the UK this was accelerated with the acquisition of Visualfiles (case management and compliance tools). Particularly strong growth was seen in the UK, France, Germany, Canada and South Africa.

The outlook for LexisNexis is positive. Revenue momentum is good, with strong subscription renewals, increasing take up of new online services and total solutions across our markets, and strong demand growth in risk management.

Revenue growth (%)



Adjusted operating profit growth (%)



↓ **Holt Online Learning** Holt, Rinehart and Winston has more than 3 million registered users of its online textbooks and programme resources. More than an online copy of our print books, these resources include dynamic and interactive tutorials and planning and assessment tools for US schools grades 6-12.



Harcourt Education’s basal textbook and supplemental businesses performed well against a weaker education market to hold overall revenues flat. Profits were lower through investment ahead of major adoptions and underperformance in Assessment

	2006 €m	2005 €m	Change at constant currencies
<b>Revenue</b>			
US Schools & Testing	1,170	1,177	0%
International	137	138	+1%
	<b>1,307</b>	1,315	0%
<b>Adjusted operating profit</b>	<b>190</b>	235	-19%
Adjusted operating margin	<b>14.5%</b>	17.9%	-3.4pts

Revenues at Harcourt Education were flat against the prior year at constant currencies, whilst adjusted operating profits were 19% lower, or 20% lower before minor disposals. Adjusted operating margin was 3.4 percentage points lower at 14.5% largely reflecting sales and marketing investment ahead of the much stronger 2007 adoption market, sales mix and the impact of the underperformance in Assessment.

The Harcourt US K-12 basal and supplemental businesses have performed well both achieving 1% revenue growth in a US textbook market estimated to be down around 6%. (The weaker market reflects the state textbook adoption cycle and reduced spending by elementary schools in non-adoption states partly as a result of significant prior year spending on federally supported Reading First programmes.) Harcourt won the leading market share, at 38%, in new state textbook adoptions in which it participated, with great success from new publishing particularly in the secondary schools market in literature and language arts, science and social studies. A good market response to new publishing in the supplemental business, and more manageable backlist attrition, continues the recovery in this business as it replaces traditional supplemental product with more comprehensive intervention programmes, and reorientates sales and marketing activities from individual school to district level.

The assessment business saw revenues 4% lower reflecting the net loss of state testing contracts and lower catalog sales. Operational difficulties surrounding a major state testing contract and knock on effects on other contracts resulted in significant cost overruns. New management were appointed in the year and organisational changes made which are beginning to make a real difference to the business. Whilst revenues are expected to decline further due to lost contracts, the actions taken have positioned the business for a recovery in performance and margin this year and next.

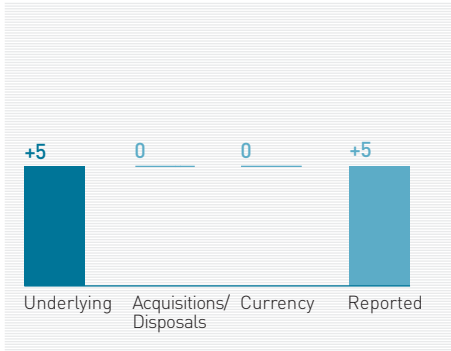
The Harcourt Education International business saw revenues 1% higher. Strong growth in South Africa and in UK export sales were offset by a weak performance in a flat UK market.

The outlook for Harcourt Education is positive. The textbook adoption cycle has entered a strong growth phase, the new textbook programmes for 2007 are being well received in the market, and the pipeline is strong with a high level of development activity. The new publishing in the supplemental business is gaining momentum and Assessment is on a firm recovery path. Organisational changes in the business are expected to deliver increasingly integrated market strategies and significant further cost efficiencies.

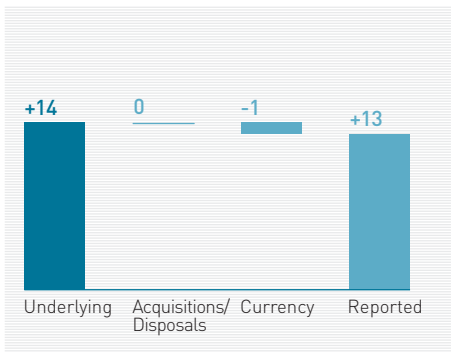
## Reed Business

www.reedbusiness.com

### Revenue growth (%)



### Adjusted operating profit growth (%)



↓ **New Scientist** has chronicled the way science and technology have transformed our understanding of the world and ourselves since 1956. New Scientist celebrated its fiftieth anniversary last year and sold over 200,000 copies worldwide of its special anniversary edition.



Reed Business's online information services grew rapidly, more than compensating for print migration, and the exhibitions business again performed strongly

	2006 €m	2005 €m	Change at constant currencies
<b>Revenue</b>			
Reed Business Information	1,317	1,302	+1%
Reed Exhibitions	767	688	+12%
	<b>2,084</b>	1,990	+5%
<b>Adjusted operating profit</b>	<b>354</b>	313	+14%
Adjusted operating margin	<b>17.0%</b>	15.7%	+1.3pts

Revenues and adjusted operating profits were 5% and 14% ahead respectively at constant currencies, with acquisitions and disposals having no overall effect on these growth rates. Adjusted operating margins were 1.3 percentage points higher, reflecting the strong growth in the exhibitions business and tight cost control.

At Reed Exhibitions, revenues were 12% higher, or 10% underlying. Strong growth was seen in key shows across the principal geographies in the US, Europe and Asia Pacific, with particularly good performances in Japan and in the international Midem entertainment and property shows held in Cannes. Whilst much of B2B marketing is moving online, the demand for exhibitions remains very strong as exhibitors and buyers place great value on physical meetings and events to balance other information sources and connections. Underlying profit growth was 16% including 6% from share of joint ventures cycling in. The net effect of other biennial shows cycling in and out is broadly neutral. The Sinopharm exhibitions acquired in a joint venture in China in 2005 are performing well ahead of plan and new shows are to be launched in 2007.

The Reed Business Information magazine and information businesses saw continued strong underlying growth in online services of over 20%, more than compensating for the 3% decline in print as the business migrates online. Overall RBI revenues were up 2% underlying. With 24% of revenues now from online services, the overall growth trajectory is encouraging. Adjusted operating profits were up 12% through continued action on costs as resources are rebalanced to the digital opportunity.

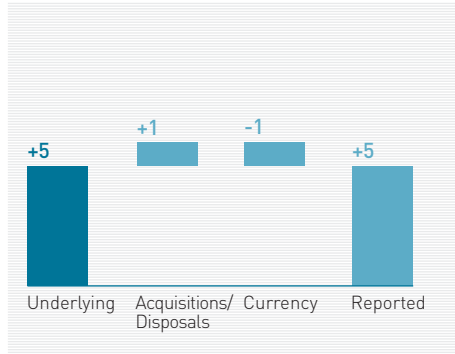
In the US, RBI underlying revenues were 2% lower. Online revenues are growing rapidly, particularly from advertising in community sites and new services, and are close to offsetting the print decline seen across most sectors. In the UK, RBI underlying revenues were up 6% reflecting the strong growth in online recruitment (up 39%) and online subscription services (up 17%). Online revenues now account for 41% of RBI UK revenues with strong growth and new launches set to increase this further. Print revenues benefited from innovative publishing and design. In continental Europe underlying revenues were up 3%, with again good growth in new online services and some further recovery in advertising markets. Revenues in Asia grew 6%.

As part of a repositioning of the portfolio, the US manufacturing product news tabloid business was sold during the year as well as a number of other titles and North American manufacturing shows. In January 2007 RBI acquired Buyerzone, a fast growing online service for matching vendors and buyers in procurement tendering that can be leveraged across RBI's categories.

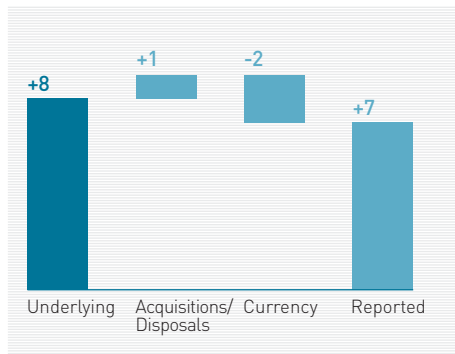
The outlook for Reed Business is encouraging. Strong demand for online services, good growth in exhibitions and ongoing portfolio management are steadily repositioning the business for good long term growth.

## Financial review continued

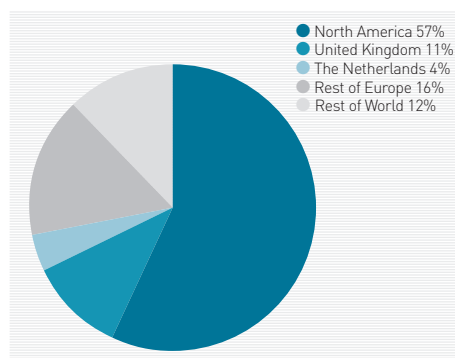
### Revenue growth (%)



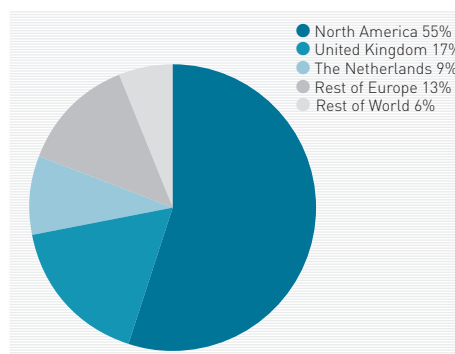
### Adjusted operating profit growth (%)



### Revenue by geographical market



### Revenue by geographical origin



## Reed Elsevier combined businesses

	2006 €m	2005 €m	Change %	Change at constant currencies
<b>Reported figures</b>				
Revenue	<b>7,935</b>	7,542	+5%	+6%
Operating profit	<b>1,294</b>	1,225	+6%	+9%
Profit before tax	<b>1,060</b>	1,023	+4%	+8%
Net borrowings	<b>3,448</b>	3,933		
<b>Adjusted figures</b>				
Operating profit	<b>1,779</b>	1,667	+7%	+9%
Profit before tax	<b>1,546</b>	1,463	+6%	+9%
Operating cash flow	<b>1,693</b>	1,577	+7%	+7%
Operating margin	<b>22.4%</b>	22.1%		
Operating cash flow conversion	<b>95%</b>	95%		

Adjusted figures are presented as additional performance measures and are stated before the amortisation of acquired intangible assets, acquisition integration costs, disposals and other non operating items, related tax effects and movements on deferred tax balances not expected to crystallise in the near term. Reconciliations between the reported and adjusted figures are provided in the notes to the combined financial statements.

### Income statement

Revenue, at €7,935m, increased by 5%. At constant exchange rates, revenue was 6% higher, or 5% excluding acquisitions and disposals.

### Reported figures

Reported operating profit, after amortisation of acquired intangible assets and acquisition integration costs, at €1,294m, was up 6%. The increase reflects the strong underlying operating performance, partly offset by the effect of a weaker US dollar hedge rate applicable for Elsevier journal subscription revenues and other currency translation effects.

The amortisation charge in respect of acquired intangible assets amounted to €436m, up €33m, principally as a result of recent acquisitions.

Acquisition integration costs amounted to €34m (2005: €30m). Net losses on business disposals and other non operating items were €1m (2005: net gain €2m).

The reported profit before tax, including amortisation of acquired intangible assets, acquisition integration costs and non operating items, at €1,060m, was up 4%.

The reported tax charge of €141m compares with a charge of €346m in the prior year principally reflecting favourable settlement of tax on prior year disposals and movements on deferred tax balances arising on unrealised exchange differences on long term inter-affiliate lending. These deferred tax movements are

recognised in the income statement but are not expected to crystallise in the foreseeable future.

The reported attributable profit of €916m compares with a reported attributable profit of €675m in 2005, reflecting the strong operating performance and the lower reported tax charge.

### Adjusted figures

Adjusted figures are used by Reed Elsevier as additional performance measures and are stated before amortisation of acquired intangible assets and acquisition integration costs, and, in respect of earnings, reflect a tax rate that excludes the effect of movements in deferred taxation assets and liabilities that are not expected to crystallise in the near term. Profit and loss on disposals and other non operating items are also excluded from the adjusted figures. Comparison at constant exchange rates uses 2005 average and hedge exchange rates.

Adjusted operating profit, at €1,779m, was up 7%. At constant exchange rates, adjusted operating profits were up 9%, or 8% excluding acquisitions and disposals. Underlying operating margins improved by 0.7 percentage points. Overall adjusted operating margins, up 0.3 percentage points at 22.4%, were held back by the inclusion of lower margin acquisitions and currency effects, most particularly the year on year movement in hedge rates in Elsevier's journal subscriptions. (The net benefit of the Elsevier science journal hedging programme is lower in 2006 than in 2005 as the effect of the

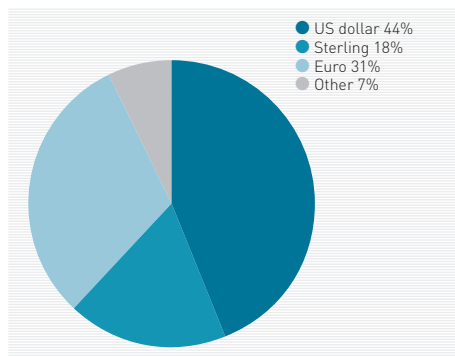
weaker US dollar is systematically incorporated within the three year rolling hedging programme.)

Within adjusted operating profit, the net pension expense (including the net pension financing items included within operating profit) was €29m lower than in the prior year principally reflecting a wider differential between the return on plan assets and interest on pension obligations. The charge for share based payments was €72m (2005: €83m). Restructuring costs, other than in respect of acquisition integration, were €31m (2005: €37m).

Net finance costs, at €233m, were €29m higher than in the prior year due to higher short term interest rates and the financing cost of acquisitions and the share repurchase programme, partly offset by the benefit of strong free cash flow.

Adjusted profit before tax was €1,546m, up 6% compared to the prior year. At constant exchange rates, adjusted profit before tax was up 9%.

#### Currency profile adjusted profit before tax



The effective tax rate on adjusted earnings was 24.1% (2005: 24.6%). The effective tax rate on adjusted earnings excludes the effect of movements in deferred taxation assets and liabilities that are not expected to crystallise in the near term, and more closely aligns with cash tax costs. Adjusted operating profits and taxation are also grossed up for the equity share of taxes in joint ventures.

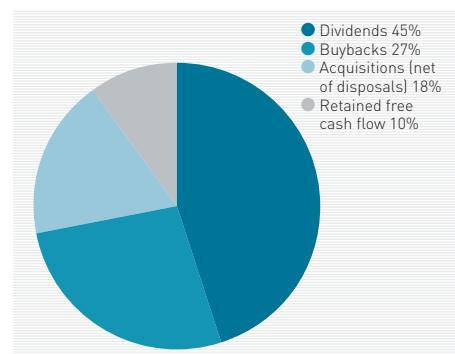
The adjusted profit attributable to shareholders of €1,170m was up 6% compared to the prior year. At constant exchange rates, adjusted profit attributable to shareholders was up 9%.

#### Cash flows and debt

Adjusted operating cash flow was €1,693m, up 7%, and 7% at constant currencies. The rate of conversion of adjusted operating profits into cash flow was 95% (2005: 95%) reflecting the continuing focus on capital discipline and managing working capital as the business expands.

Capital expenditure included within adjusted operating cash flow was €288m (2005: €285m), including €159m in respect of capitalised development costs included within intangible assets. Spend on acquisitions was €251m including deferred consideration payable. An amount of €128m was capitalised as acquired intangible assets and €150m as goodwill. Acquisition integration spend in respect of these and other recent acquisitions amounted to €37m principally in respect of the MediMedia MAP integration. Disposal proceeds amounted to €70m.

#### Use of free cash flow



Free cash flow – after interest and taxation – was €1,201m, up €85m. Dividends paid to shareholders in the year amounted to €545m (2005: €491m). Share repurchases by the parent companies amounted to €319m. Additional shares of the parent companies were purchased by the employee benefit trust for €100m to

meet future obligations in respect of share based remuneration. Net proceeds from share issuance under share option programmes were €137m.

Net borrowings at 31 December 2006 were €3,448m (2005: €3,933m), a decrease of €485m since 31 December 2005 principally due to foreign exchange translation effects following the significant weakening of the US dollar between the beginning and end of the year. These translation effects decreased net debt by €333m. Additionally, net debt benefited from the free cash flow less dividends and share buy backs and acquisition spend.

Gross borrowings after fair value adjustments at 31 December 2006 amounted to €4,479m, denominated mostly in US dollars, and were partly offset by the fair value of related derivatives of €257m and cash balances totalling €774m invested in short term deposits and marketable securities. After taking into account interest rate and currency derivatives, a total of 68% of Reed Elsevier's gross borrowings (equivalent to 88% of net borrowings) were at fixed rates and had a weighted average remaining life of 5.2 years and interest coupon of 5.2%.

The net pension deficit, ie pensions obligations less pension assets, at 31 December 2006 was €351m (2005: €591m). The reduction in the deficit of €240m principally arises from the good asset returns and the increase in long term corporate bond yields which are used to discount the pension obligations.

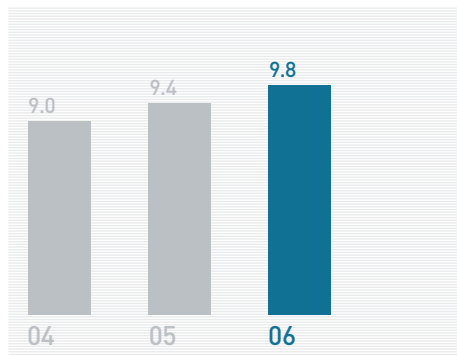
#### Capital employed and returns

The capital employed in the business at 31 December 2006 was €13,528m (2005: €14,169m), after adding back accumulated amortisation of acquired intangible assets and goodwill. The decrease of €641m principally arises from currency translation effects (€1,063m), most particularly from the weakening of the US dollar between 1 January and 31 December 2006, partly offset by acquisition spend of €240m and the lower net pension deficit.

## Financial review continued

The return on average capital employed in the year was 9.8% (2005: 9.4%). This return is based on adjusted operating profits, less tax at the 24% effective rate, and the average of the capital employed at the beginning and end of the year retranslated at average exchange rates. The improvement in the year reflects the good underlying profit growth and capital discipline.

### Return on capital employed (%)



Acquisitions typically dilute the overall return initially, but build quickly to deliver longer term returns well over Reed Elsevier's average for the business. The recent acquisitions made in the years 2004 to 2006 are delivering post tax returns in 2006 of 10%, 6% and proforma 5% respectively and continue to grow well.

### Accounting policies

#### Introduction

The accounting policies of the Reed Elsevier combined businesses are described in the combined financial statements. The Reed Elsevier combined financial statements and the consolidated financial statements of Reed Elsevier PLC and Reed Elsevier NV are presented in accordance with International Financial Reporting Standards (IFRS).

The most significant accounting policies in determining the financial condition and results of the combined businesses, and those requiring the most subjective or complex judgment, relate to the valuation of goodwill and intangible assets, share based remuneration, pensions and taxation.

The return on average capital employed in the year was 9.8% (2005: 9.4%). The improvement in the year reflects the good underlying profit growth and capital discipline

Revenue recognition policies, while an area of management focus, are generally straightforward in application as the timing of product or service delivery and customer acceptance for the various revenue types can be readily determined. Allowances for product returns are deducted from revenues based on historical return rates. Where sales consist of two or more components that operate independently, revenue is recognised as each component is completed by performance, based on attribution of relative value.

Pre-publication costs incurred in the creation of content prior to production and publication are deferred and expensed over their estimated useful lives based on sales profiles. Such costs typically comprise direct internal labour costs and externally commissioned editorial and other fees. Estimated useful lives generally do not exceed five years. Annual reviews are carried out to assess the recoverability of carrying amounts.

Development spend embraces investment in new product and other initiatives, ranging from the building of new online delivery platforms, to launch costs of new services, to building new infrastructure applications. Launch costs and other operating expenses of new products and services are expensed as incurred. The costs of building product applications and infrastructure are capitalised as intangible assets and amortised over their estimated useful lives. Impairment reviews are carried out annually.

#### Goodwill and intangible assets

Reed Elsevier's accounting policy is that, on acquisition of a subsidiary or business, the purchase consideration is allocated between the net tangible and intangible assets other than goodwill on a fair value basis, with any excess purchase consideration representing goodwill. The valuation of intangible assets represents the estimated economic value in use, using standard valuation methodologies, including as appropriate, discounted cash flow, relief

from royalty and comparable market transactions. Acquired intangible assets are capitalised and amortised systematically over their estimated useful lives, subject to annual impairment review. Appropriate amortisation periods are selected based on assessments of the longevity of the brands and imprints, the market positions of the acquired assets and the technological and competitive risks that they face. Certain intangible assets in relation to acquired science and medical publishing businesses have been determined to have indefinite lives. The longevity of these assets is evidenced by their long established and well regarded brands and imprints, and their characteristically stable market positions.

The carrying amounts of goodwill and indefinite lived intangible assets in each business are regularly reviewed for impairment at least twice a year. The carrying amounts of all other intangible assets are reviewed where there are indications of possible impairment. An impairment review involves a comparison of the carrying value of the asset with estimated values in use based on latest management cash flow projections. Key areas of judgment in estimating the values in use of businesses are the forecast long term growth rates and the appropriate discount rates to be applied to forecast cash flows. Based on the latest value in use calculations, no goodwill or intangible assets were impaired as at 31 December 2006.

#### Share based remuneration

Share based remuneration is accounted for in accordance with IFRS 2 – Share Based Payment and is determined based on the fair value of an award at the date of grant, and is spread over the vesting period on a straight line basis, taking into account the number of shares that are expected to vest. The fair value of awards is determined at the date of grant by use of a binomial or Monte Carlo simulation model as appropriate, which requires judgments to be made regarding share price volatility, dividend yield, risk free rates

of return and expected option lives. The number of awards that are expected to vest requires judgments to be made regarding forfeiture rates and the extent to which performance conditions will be met. These assumptions are determined in conjunction with independent actuaries based on historical data and trends.

### Pensions

Pension costs are accounted for in accordance with IAS19 – Employee Benefits.

Accounting for defined benefit pension schemes involves judgment about uncertain events, including the life expectancy of the members, salary and pension increases, inflation, the return on scheme assets and the rate at which the future pension payments are discounted. Estimates for these factors are used in determining the pension cost and liabilities reported in the financial statements. These best estimates of future developments are made in conjunction with independent actuaries. Each scheme is subject to a periodic review by the independent actuaries.

For defined contribution schemes, the net cost represents contributions payable.

### Taxation

The Reed Elsevier combined businesses seek to organise their affairs in a tax efficient manner, taking account of the jurisdictions in which they operate. A number of acquisitions and disposals have been made in recent years giving rise to complex tax issues requiring management to use its judgment to make various tax determinations. Although Reed Elsevier is confident that tax returns have been appropriately compiled, the application and interpretation of tax legislation is subject to uncertainty and there are risks that further tax may be payable on certain transactions or that the deductibility of certain expenditure for tax purposes may be disallowed. Reed Elsevier's policy is to make provision for

tax uncertainties where it is considered probable that tax payments may arise.

Reed Elsevier's policy in respect of deferred taxation is to provide in full for all taxable temporary differences using the balance sheet liability method. Deferred tax assets are only recognised to the extent that they are considered recoverable based on forecasts of available taxable profits against which they can be utilised over the near term.

### Treasury policies

The boards of Reed Elsevier PLC and Reed Elsevier NV have requested that Reed Elsevier Group plc and Elsevier Reed Finance BV have due regard to the best interests of Reed Elsevier PLC and Reed Elsevier NV shareholders in the formulation of treasury policies.

Financial instruments are used to finance the Reed Elsevier businesses and to hedge transactions. Reed Elsevier's businesses do not enter into speculative transactions. The main treasury risks faced by Reed Elsevier are liquidity risk, interest rate risk and foreign currency risk. The boards of the parent companies agree overall policy guidelines for managing each of these risks and the boards of Reed Elsevier Group plc and Elsevier Finance SA agree policies (in conformity with parent company guidelines) for their respective business and treasury centres. These policies are summarised below.

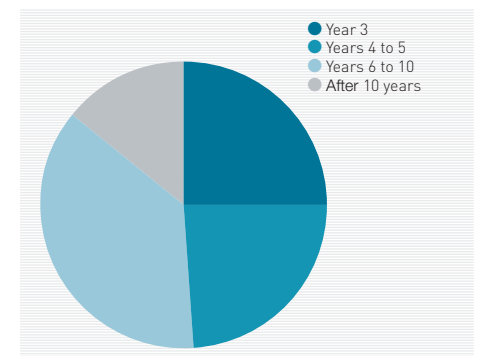
### Liquidity

Reed Elsevier maintains a range of borrowing facilities and debt programmes to fund its requirements, at short notice and at competitive rates. The significance of Reed Elsevier Group plc's US operations means that the majority of debt is denominated in US dollars and is raised in the US debt markets. A mixture of short term and long term debt is utilised and Reed Elsevier maintains a maturity profile to facilitate refinancing. Reed Elsevier's policy is that no more than US\$1.0bn of term debt issues should mature in any 12-month period. In addition, minimum levels of net debt with maturities over three years and five

years are specified, depending on the level of the total borrowings.

After taking account of the maturity of committed bank facilities that back short term borrowing and after utilising available cash resources, at 31 December 2006, no borrowings mature in the next two years, 25% of borrowings mature in the third year, 24% in the fourth and fifth years, 37% in the sixth to tenth years, and 14% beyond the tenth year.

### Maturity profile of borrowings



In April 2006 Reed Elsevier renegotiated and amended the terms of its US\$3.0bn committed credit facility. At 31 December 2006, Reed Elsevier had access to US\$3.0bn (2005: US\$3.0bn) of committed bank facilities, of which US\$77m was drawn. These facilities principally provide back up for short term debt but also security of funding for future acquisition spend in the event that commercial paper markets are not available. All these committed facilities expire within two to three years (2005: two to three years).

### Interest rate exposure management

Reed Elsevier's interest rate exposure management policy is aimed at reducing the exposure of the combined businesses to changes in interest rates. The proportion of interest expense that is fixed on net debt is determined by reference to the level of interest cover. Reed Elsevier uses fixed rate term debt, interest rate swaps, forward rate agreements and a range of interest rate options to manage the exposure. Interest rate derivatives are used only

to hedge an underlying risk and no net market positions are held.

At 31 December 2006, after taking account of interest rate and currency derivatives in a designated hedging relationship, US\$3.8bn of Reed Elsevier's net debt was denominated in US dollars and net interest expense was fixed or capped on approximately US\$2.7bn of forecast US dollar net debt for the next 12 months. This fixed or capped net debt reduces to approximately US\$1.2bn by the end of the third year and reduces further thereafter with all but US\$0.1bn of fixed rate term debt (not swapped back to floating rate) having matured by the end of 2012.

At 31 December 2006, fixed rate US dollar term debt (not swapped back to floating rate) amounted to US\$1.3bn and had a weighted average life remaining of 8.3 years (2005: 6.7 years) and a weighted average interest coupon of 6.0%. Designated interest rate derivatives in place at 31 December 2006, which fix or cap the interest cost on an additional US\$1.5bn (2005: US\$0.7bn) of variable rate US dollar debt, have a weighted average maturity of 1.4 years (2005: 2.2 years) and a weighted average interest rate of 4.5%.

#### Foreign currency exposure management

Translation exposures arise on the earnings and net assets of business operations in countries other than those of each parent company. These exposures are hedged, to a significant extent, by a policy of denominating borrowings in currencies where significant translation exposures exist, most notably US dollars.

Currency exposures on transactions denominated in a foreign currency are required to be hedged using forward contracts. In addition, recurring transactions and future investment exposures may be hedged, within defined limits, in advance of becoming contractual. The precise policy differs

according to the commercial situation of the individual businesses. Expected future net cash flows may be covered for sales expected for up to the next 12 months (50 months for Elsevier science and medical subscription businesses up to limits staggered by duration). Cover takes the form of foreign exchange forward contracts.

As at 31 December 2006, the amount of outstanding foreign exchange cover designated against future transactions was US\$1.2bn.

### Elsevier Reed Finance BV

#### Structure

Elsevier Reed Finance BV, the Dutch parent company of the Elsevier Reed Finance BV group ("ERF"), is directly owned by Reed Elsevier PLC and Reed Elsevier NV. ERF provides treasury, finance and insurance services to the Reed Elsevier Group plc businesses through its subsidiaries in Switzerland: Elsevier Finance SA ("EFSA"), Elsevier Properties SA ("EPSA") and Elsevier Risks SA ("ERSA"). These three Swiss companies are organised under one Swiss holding company, which is in turn owned by Elsevier Reed Finance BV.

#### Activities

EFSA, EPSA and ERSA each focus on their own specific area of expertise.

EFSA is the principal treasury centre for the combined businesses. It is responsible for all aspects of treasury advice and support for Reed Elsevier Group plc's businesses operating in Continental Europe, South America, the Pacific Rim, China and certain other territories, and undertakes foreign exchange and derivatives dealing services for the whole of Reed Elsevier. EFSA also arranges or directly provides Reed Elsevier Group plc businesses with financing for acquisitions and product development and manages cash pools and investments on their behalf. EPSA is responsible for the exploitation of tangible and intangible property rights whilst ERSA is

responsible for insurance activities relating to risk retention.

#### Major developments

In 2006, EFSA acted as arranger of a Euro Commercial Paper programme and a term debt issue on behalf of Reed Elsevier (Investments) plc, a subsidiary of Reed Elsevier Group plc, renegotiated various banking and cash management arrangements in Continental Europe and Asia and continued to provide advice to Reed Elsevier Group plc companies regarding interest and foreign currency exposures and electronic collections and payment solutions.

The average balance of cash under management in 2006, on behalf of Reed Elsevier Group plc and its parent companies, was approximately \$0.5bn.

#### Liabilities and assets

At the end of 2006, 88% (2005: 87%) of ERF's gross assets were held in US dollars and 10% (2005: 12%) in euros, including \$8.5bn (2005: \$8.1bn) and €0.8bn (2005: €0.9bn) in loans to Reed Elsevier Group plc subsidiaries. Loans made to Reed Elsevier Group plc businesses are funded from equity, long term debt of \$1.3bn and short term debt of \$0.8bn backed by committed bank facilities. Term debt is derived from a Swiss domestic public bond issue, bilateral term loans and private placements. Short term debt is primarily derived from euro and US commercial paper programmes.

## Key performance measures

The key financial performance measures used by Reed Elsevier and the bases of their calculation are as follows:

- **Revenue** – as reported in the financial statements.
- **Adjusted operating profit** – reported operating profit before amortisation of acquired intangible assets, acquisition integration costs, and share of taxation of joint ventures.
- **Adjusted operating margin** – adjusted operating profit expressed as a percentage of revenue.
- **Adjusted profit before tax** – reported profit before tax before amortisation of acquired intangible assets, acquisition integration costs, share of taxation of joint ventures, disposals and other non operating items.
- **Effective tax rate on adjusted profit before tax** – reflects the tax rate excluding movements on deferred tax balances not expected to crystallise in the near term, more closely aligning with cash taxes payable, and includes the benefit of deductible tax amortisation on acquired goodwill and intangible assets.
- **Adjusted profit attributable to shareholders** – reported profit attributable to shareholders before amortisation of acquired intangible assets, acquisition integration costs, disposals and other non operating items, related tax effects and movements on deferred tax balances not expected to crystallise in the near term.
- **Adjusted earnings per share** – adjusted profit attributable to shareholders of each parent company divided by the respective average number of ordinary shares in issue in the period.

→ **Adjusted operating cash flow** – cash generated from operations plus dividends from joint ventures less net capital expenditure on property, plant and equipment and internally developed intangible assets, and excluding payments in relation to acquisition integration costs.

→ **Constant currency growth** – growth rates calculated using the prior year average and hedge exchange rates.

→ **Underlying growth** – constant currency growth rates excluding acquisitions and disposals.

→ **Return on capital employed** – adjusted operating profit less taxation (at the effective rate for the year) expressed as a percentage of capital employed, being the aggregate of gross goodwill and acquired intangible assets, property, plant and equipment, internally developed intangible assets, working capital, less net pension obligations and provisions.

The source data for calculating the key performance measures is obtained from the Reed Elsevier financial reporting system.

The adjusted figures are adopted as key performance measures since they measure performance without reference to non cash amortisation of intangible assets, mostly acquired in prior periods, which has no operational relevance to current performance. Acquisition integration expenses are excluded since they are a direct function of the relevant acquisition activity and not a reflection of ongoing operational performance. Underlying growth, excluding acquisitions and disposals, is measured to give a proper assessment of year on year organic growth without distortion for part year contributions. Constant currency growth is measured to give a better reflection of year on year performance before translation and other currency effects in arriving at the reported

figures in the reporting currencies of the parent companies.

Performance in respect of the principal key performance measures for Reed Elsevier is described in the Chairman and Chief Executive's Report and the Operating and Financial Review above.

The derivations of adjusted operating profit, adjusted profit before tax, adjusted profit attributable, and adjusted operating cash flow are disclosed in the notes to the combined financial statements. The derivation of the adjusted earnings per share of the parent companies is shown in the notes to the Reed Elsevier PLC and Reed Elsevier NV consolidated financial statements.



# Reed Elsevier Combined financial statements presented in euros

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Combined income statement	24
Combined cash flow statement	25
Combined balance sheet	26
Combined statement of recognised income and expense	27
Combined shareholders' equity reconciliation	27
Accounting policies	28
Notes to the combined financial statements	32
Independent auditors' report	61

## Combined income statement

For the year ended 31 December	Note	2006 €m	2005 €m
<b>Revenue</b>	1	<b>7,935</b>	7,542
Cost of sales		<b>(2,915)</b>	(2,759)
Gross profit		<b>5,020</b>	4,783
Selling and distribution costs		<b>(1,688)</b>	(1,635)
Administration and other expenses		<b>(2,065)</b>	(1,946)
Operating profit before joint ventures		<b>1,267</b>	1,202
Share of results of joint ventures		<b>27</b>	23
<b>Operating profit</b>	2	<b>1,294</b>	1,225
Finance income	6	<b>31</b>	52
Finance costs	6	<b>(264)</b>	(256)
Net finance costs		<b>(233)</b>	(204)
Disposals and other non operating items	7	<b>(1)</b>	2
<b>Profit before tax</b>		<b>1,060</b>	1,023
Taxation	8	<b>(141)</b>	(346)
<b>Net profit for the year</b>		<b>919</b>	677
Attributable to:			
Parent companies' shareholders		<b>916</b>	675
Minority interests		<b>3</b>	2
<b>Net profit for the year</b>		<b>919</b>	677

## Combined cash flow statement

For the year ended 31 December	Note	2006 €m	2005 €m
<b>Cash flow from operating activities</b>			
Cash generated from operations	10	1,917	1,786
Interest paid		(253)	(223)
Interest received		18	16
Tax paid		(250)	(250)
<b>Net cash from operating activities</b>		<b>1,432</b>	<b>1,329</b>
<b>Cash flows from investing activities</b>			
Acquisitions	10	(240)	(463)
Purchases of property, plant and equipment		(129)	(136)
Expenditure on internally developed intangible assets		(159)	(149)
Purchase of investments		(13)	(4)
Proceeds on disposals of property, plant and equipment		3	12
Proceeds from other disposals		70	52
Dividends received from joint ventures		24	23
<b>Net cash used in investing activities</b>		<b>(444)</b>	<b>(665)</b>
<b>Cash flows from financing activities</b>			
Dividends paid to shareholders of the parent companies		(545)	(491)
Increase/(decrease) in bank loans, overdrafts and commercial paper		105	(718)
Issuance of other loans		598	794
Repayment of other loans		(495)	(132)
Repayment of finance leases		(18)	(19)
Proceeds on issue of ordinary shares		137	37
Purchase of treasury shares		(419)	(39)
<b>Net cash used in financing activities</b>		<b>(637)</b>	<b>(568)</b>
<b>Increase in cash and cash equivalents</b>	10	<b>351</b>	<b>96</b>
<b>Movement in cash and cash equivalents</b>			
At start of year		432	317
Increase in cash and cash equivalents		351	96
Exchange translation differences		(9)	19
<b>At end of year</b>		<b>774</b>	<b>432</b>

## Combined balance sheet

As at 31 December	Note	2006 €m	2005 €m
<b>Non-current assets</b>			
Goodwill	13	4,175	4,424
Intangible assets	14	3,761	4,349
Investments in joint ventures	15	108	104
Other investments	15	75	64
Property, plant and equipment	16	444	458
Net pension assets	4	30	–
Deferred tax assets	18	253	388
		<b>8,846</b>	<b>9,787</b>
<b>Current assets</b>			
Inventories and pre-publication costs	19	943	920
Trade and other receivables	20	2,150	2,098
Cash and cash equivalents		774	432
		<b>3,867</b>	<b>3,450</b>
<b>Assets held for sale</b>			
		–	88
<b>Total assets</b>		<b>12,713</b>	<b>13,325</b>
<b>Current liabilities</b>			
Trade and other payables	21	2,882	2,893
Borrowings	22	1,372	1,314
Taxation		714	813
		<b>4,968</b>	<b>5,020</b>
<b>Non-current liabilities</b>			
Borrowings	22	3,107	3,305
Deferred tax liabilities	18	1,266	1,431
Net pension obligations	4	381	591
Provisions	24	42	64
		<b>4,796</b>	<b>5,391</b>
<b>Liabilities associated with assets held for sale</b>			
		–	16
<b>Total liabilities</b>		<b>9,764</b>	<b>10,427</b>
<b>Net assets</b>		<b>2,949</b>	<b>2,898</b>
<b>Capital and reserves</b>			
Combined share capitals	26	285	277
Combined share premiums	27	2,800	2,635
Combined shares held in treasury	28	(562)	(136)
Translation reserve	29	(201)	130
Other combined reserves	30	607	(30)
<b>Combined shareholders' equity</b>		<b>2,929</b>	<b>2,876</b>
Minority interests		20	22
<b>Total equity</b>		<b>2,949</b>	<b>2,898</b>

## Combined statement of recognised income and expense

For the year ended 31 December	Note	2006 €m	2005 €m
<b>Net profit for the year</b>		<b>919</b>	677
Exchange differences on translation of foreign operations		<b>(300)</b>	346
Actuarial gains/(losses) on defined benefit pension schemes	4	<b>204</b>	(54)
Fair value movements on available for sale investments		<b>4</b>	4
Fair value movements on cash flow hedges		<b>79</b>	(15)
Tax recognised directly in equity	8	<b>(88)</b>	(4)
<b>Net (expense)/income recognised directly in equity</b>		<b>(101)</b>	277
Transfer to net profit from hedge reserve (net of tax)		<b>(7)</b>	(28)
<b>Total recognised income and expense for the year</b>		<b>811</b>	926
Attributable to:			
Parent companies' shareholders		<b>808</b>	924
Minority interests		<b>3</b>	2
<b>Total recognised income and expense for the year</b>		<b>811</b>	926

## Combined shareholders' equity reconciliation

For the year ended 31 December	Note	2006 €m	2005 €m
<b>Total recognised net income attributable to the parent companies' shareholders</b>		<b>808</b>	924
Dividends declared	12	<b>(545)</b>	(491)
Issue of ordinary shares, net of expenses		<b>137</b>	37
Increase in shares held in treasury	28	<b>(419)</b>	(39)
Increase in share based remuneration reserve		<b>72</b>	83
<b>Net increase in combined shareholders' equity</b>		<b>53</b>	514
Combined shareholders' equity at start of year		<b>2,876</b>	2,362
<b>Combined shareholders' equity at end of year</b>		<b>2,929</b>	2,876

## Accounting policies

The Reed Elsevier combined financial statements are prepared in accordance with International Financial Reporting Standards (IFRS) as endorsed by the European Union.

The Reed Elsevier accounting policies under IFRS are set out below.

### Basis of preparation

The equalisation agreement between Reed Elsevier PLC and Reed Elsevier NV has the effect that their shareholders can be regarded as having the interests of a single economic group. The Reed Elsevier combined financial statements ("the combined financial statements") represent the combined interests of both sets of shareholders and encompass the businesses of Reed Elsevier Group plc and Elsevier Reed Finance BV and their respective subsidiaries, associates and joint ventures, together with the parent companies, Reed Elsevier PLC and Reed Elsevier NV ("the combined businesses").

The combined financial statements form part of the statutory information to be provided by Reed Elsevier NV, but are not for a legal entity and do not include all the information required to be disclosed by a company in its financial statements under the UK Companies Act 1985 or the Dutch Civil Code. Additional information is given in the Annual Reports and Financial Statements of the parent companies set out on pages 106 to 143 of the Reed Elsevier Annual Reports and Financial Statements 2006. A list of principal businesses is set out on page 157 of the Reed Elsevier Annual Reports and Financial Statements 2006.

In addition to the figures required to be reported by applicable accounting standards, adjusted profit and operating cash flow figures have been presented as additional performance measures. Adjusted figures are shown before the amortisation of acquired intangible assets, acquisition integration costs, disposals and other non operating items, related tax effects and movements in deferred taxation assets and liabilities that are not expected to crystallise in the near term. Adjusted operating profits are also grossed up to exclude the equity share of taxes in joint ventures. Adjusted operating cash flow is measured after dividends from joint ventures and net capital expenditure, but before payments in relation to acquisition integration costs.

### Foreign exchange translation

These combined financial statements are presented in euros and are supplementary to the combined financial statements presented in pounds sterling in the Reed Elsevier Annual Reports and Financial Statements 2006.

Transactions in foreign currencies are recorded at the rate of exchange prevailing on the date of the transaction. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at the rate prevailing on the balance sheet date. Exchange differences arising are recorded in the income statement other than where hedge accounting applies (see Financial Instruments).

Assets and liabilities of foreign operations are translated at exchange rates prevailing on the balance sheet date. Income and expense items of foreign operations are translated at the average exchange rate for the period. Exchange differences arising are classified as equity and transferred to the translation reserve. When foreign operations are disposed of, the related cumulative translation differences are recognised within the income statement in the period.

Reed Elsevier uses derivative financial instruments, primarily forward contracts, to hedge its exposure to certain foreign exchange risks. Details of Reed Elsevier's accounting policies in respect of derivative financial instruments are set out below.

### Revenue

Revenue represents the invoiced value of sales less anticipated returns on transactions completed by performance, excluding customer sales taxes and sales between the combined businesses.

Revenues are recognised for the various categories of turnover as follows: subscriptions – on periodic despatch of subscribed product or rateably over the period of the subscription where performance is not measurable by despatch; circulation – on despatch; advertising – on publication or over the period of online display; exhibitions – on occurrence of the exhibition; educational testing contracts – over the term of the contract on percentage completed against contract milestones.

Where sales consist of two or more independent components, revenue is recognised on each component, as it is completed by performance, based on attribution of relative value.

### Employee benefits

The expense of defined benefit pension schemes and other post-retirement employee benefits is determined using the projected unit credit method and charged in the income statement as an operating expense, based on actuarial assumptions reflecting market conditions at the beginning of the financial year. Actuarial gains and losses are recognised in full in the statement of recognised income and expense in the period in which they occur. Past service costs are recognised immediately to the extent that benefits have vested, or, if not vested, on a straight line basis over the period until the benefits vest.

Net pension obligations in respect of defined benefit schemes are included in the balance sheet at the present value of scheme liabilities, less the fair value of scheme assets. Where schemes are in surplus, i.e. assets exceed liabilities, the net pension assets are separately included in the balance sheet. Any net pension asset is limited to the extent that the asset is recoverable through reductions in future contributions.

The expense of defined contribution pension schemes and other employee benefits is charged in the income statement as incurred.

**Share based remuneration**

The fair value of share based remuneration is determined at the date of grant and recognised as an expense in the income statement on a straight line basis over the vesting period, taking account of the estimated number of shares that are expected to vest. Market based performance criteria are taken into account when determining the fair value at the date of grant. Non-market based performance criteria are taken into account when estimating the number of shares expected to vest. The fair value of share based remuneration is determined by use of a binomial or Monte Carlo simulation model as appropriate. All Reed Elsevier's share based remuneration is equity settled.

**Borrowing costs**

All borrowing costs are expensed as incurred unless hedge accounting applies (see Financial Instruments).

**Taxation**

The tax expense represents the sum of the tax payable on the current year taxable profits, adjustments in respect of prior year taxable profits, and the movements on deferred tax that are recognised in the income statement.

The tax payable on current year taxable profits is calculated using the applicable tax rates that have been enacted, or substantively enacted, by the balance sheet date.

Deferred tax is the tax arising on differences between the carrying amounts of assets and liabilities in the financial statements and their corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that, based on current forecasts, it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Deferred tax is not recognised on temporary differences arising in respect of goodwill that is not deductible for tax purposes.

Deferred tax is calculated using tax rates that are expected to apply in the period when the liability is expected to be settled or the asset realised. Full provision is made for deferred tax which would become payable on the distribution of retained profits from foreign subsidiaries, associates or joint ventures.

Movements in deferred tax are charged or credited in the income statement, except when they relate to items charged or credited directly to equity, in which case the deferred tax is also recognised in equity. Deferred tax credits in respect of share based remuneration are recognised in equity to the extent that expected tax deductions exceed the related expense.

**Goodwill**

On the acquisition of a subsidiary or business, the purchase consideration is allocated between the net tangible and intangible assets on a fair value basis, with any excess

purchase consideration representing goodwill. Goodwill arising on acquisitions also includes amounts corresponding to deferred tax liabilities recognised in respect of acquired intangible assets.

Goodwill is recognised as an asset and reviewed for impairment at least annually. Any impairment is recognised immediately in the income statement and not subsequently reversed.

On disposal of a subsidiary or business, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

**Intangible assets**

Intangible assets acquired as part of a business combination are stated in the balance sheet at their fair value as at the date of acquisition, less accumulated amortisation. Internally generated intangible assets are stated in the balance sheet at the directly attributable cost of creation of the asset, less accumulated amortisation.

Intangible assets acquired as part of business combinations comprise: market related assets (e.g. trade marks, imprints, brands); customer related assets (e.g. subscription bases, customer lists, customer relationships); editorial content; software and systems (e.g. application infrastructure, product delivery platforms, in-process research and development); contract based assets (e.g. publishing rights, exhibition rights, supply contracts); and other intangible assets. Internally generated intangible assets typically comprise software and systems development where an identifiable asset is created that is probable to generate future economic benefits.

Intangible assets, other than brands and imprints determined to have indefinite lives, are amortised systematically over their estimated useful lives. The estimated useful lives of intangible assets with finite lives are as follows: market and customer related assets – 3 to 40 years; content, software and other acquired intangible assets – 3 to 20 years; and internally developed intangible assets – 3 to 10 years. Brands and imprints determined to have indefinite lives are not amortised and are subject to impairment review at least annually.

**Property, plant and equipment**

Property, plant and equipment are stated in the balance sheet at cost less accumulated depreciation. No depreciation is provided on freehold land. Freehold buildings and long leases are depreciated over their estimated useful lives up to a maximum of 50 years. Short leases are written off over the duration of the lease. Depreciation is provided on other assets on a straight line basis over their estimated useful lives as follows: leasehold improvements – shorter of life of lease and 10 years; plant – 3 to 20 years; office furniture, fixtures and fittings – 5 to 10 years; computer systems, communication networks and equipment – 3 to 7 years.

## Accounting policies

### Investments

Investments, other than investments in joint ventures and associates, are stated in the balance sheet at fair value. Investments held as part of the venture capital portfolio are classified as held for trading, with changes in fair value reported through the income statement. All other investments are classified as available for sale with changes in fair value recognised directly in equity until the investment is disposed of or is determined to be impaired, at which time the cumulative gain or loss previously recognised in equity is brought into the net profit or loss for the period. All items recognised in the income statement relating to investments, other than investments in joint ventures and associates, are reported as non operating items.

Available for sale investments and venture capital investments held for trading represent investments in listed and unlisted securities. The fair value of listed securities is determined based on quoted market prices, and of unlisted securities on management's estimate of fair value based on standard valuation techniques.

Investments in joint ventures and associates are accounted for under the equity method and stated in the balance sheet at cost as adjusted for post-acquisition changes in Reed Elsevier's share of net assets, less any impairment in value.

### Impairment

At each balance sheet date, reviews are carried out of the carrying amounts of tangible and intangible assets and goodwill to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent, if any, of the impairment loss. Where the asset does not generate cash flows that are independent from other assets, estimates are made based on the cash flows of the cash generating unit to which the asset belongs. Intangible assets with an indefinite useful life are tested for impairment at least annually and whenever there is any indication that the asset may be impaired.

If the recoverable amount of an asset or cash generating unit is estimated to be less than its net carrying amount, the net carrying amount of the asset or cash generating unit is reduced to its recoverable amount. Impairment losses are recognised immediately in the income statement.

### Inventories and pre-publication costs

Inventories and pre-publication costs are stated at the lower of cost, including appropriate attributable overhead, and estimated net realisable value. Pre-publication costs, representing costs incurred in the origination of content prior to publication, are expensed systematically reflecting the expected sales profile over the estimated economic lives of the related products, generally up to five years.

### Leases

Assets held under leases which confer rights and obligations similar to those attaching to owned assets are classified as assets held under finance leases and capitalised within

property, plant and equipment and the corresponding liability to pay rentals is shown net of interest in the balance sheet as obligations under finance leases. The capitalised value of the assets is depreciated on a straight line basis over the shorter of the periods of the leases or the useful lives of the assets concerned. The interest element of the lease payments is allocated so as to produce a constant periodic rate of charge.

Operating lease rentals are charged to the income statement on a straight line basis over the period of the leases. Rental income from operating leases is recognised on a straight line basis over the term of the relevant lease.

### Cash and cash equivalents

Cash and cash equivalents comprise cash balances, call deposits and other short term highly liquid investments and are held in the balance sheet at fair value.

### Assets held for sale

Assets of businesses that are held for sale, rather than for continuing use by Reed Elsevier, are classified as assets held for sale. Such assets are carried at the lower of amortised cost and fair value less costs to sell. Similarly, liabilities of businesses held for sale are also separately classified on the balance sheet.

### Financial instruments

Financial instruments comprise investments (other than investments in joint ventures or associates), trade receivables, cash and cash equivalents, payables and accruals, provisions, borrowings and derivative financial instruments.

Investments (other than investments in joint ventures and associates) are classified as either held for trading or available for sale, as described above.

Trade receivables are carried in the balance sheet at invoiced value less allowance for estimated irrecoverable amounts. Irrecoverable amounts are estimated based on the ageing of trade receivables, experience and circumstance.

Borrowings (other than fixed rate borrowings in designated hedging relationships and for which the carrying value is adjusted to reflect changes in the fair value of the hedged risk), payables, accruals and provisions are recorded at nominal value.

Derivative financial instruments are used to hedge interest rate and foreign exchange risks. Changes in the fair value of derivative financial instruments that are designated and effective as hedges of future cash flows are recognised (net of tax) directly in equity in the hedge reserve. If a hedged firm commitment or forecasted transaction results in the recognition of a non financial asset or liability, then, at the time that the asset or liability is recognised, the associated gains or losses on the derivative that had previously been recognised in equity are included in the initial measurement of the asset or liability. For hedges that do not result in the recognition of an asset or a liability, amounts deferred in equity are recognised in the income statement in the same

period in which the hedged item affects net profit or loss. Any ineffective portion of hedges is recognised immediately in the income statement.

Derivative financial instruments that are not designated as hedging instruments are classified as held for trading and recorded in the balance sheet at fair value, with changes in fair value recognised in the income statement.

Where an effective hedge is in place against changes in the fair value of fixed rate borrowings, the hedged borrowings are adjusted for changes in fair value attributable to the risk being hedged with a corresponding income or expense included in the income statement. The offsetting gains or losses from remeasuring the fair value of the related derivatives are also recognised in the income statement.

The fair values of interest rate swaps, interest rate options, forward rate agreements and forward foreign exchange contracts represent the replacement costs calculated using market rates of interest and exchange. The fair value of long term borrowings is calculated by discounting expected future cash flows at market rates.

Hedge accounting is discontinued when a hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. At that time, any cumulative gain or loss on the hedging instrument recognised in equity is either retained in equity until the firm commitment or forecasted transaction occurs, or, where a hedged transaction is no longer expected to occur, is immediately credited or expensed in the income statement.

On adoption of IAS39 – Financial Instruments, adjustments were made either to the carrying value of hedged items or to equity, as appropriate, to reflect the differences between the previous UK GAAP carrying values of financial instruments and their carrying values required to be reported under IAS39. Any transition gains or losses on financial instruments that qualified for hedge accounting were reflected in equity and remain in equity until either the forecasted transaction occurs or is no longer expected to occur.

#### **Shares held in treasury**

Shares of Reed Elsevier PLC and Reed Elsevier NV that are repurchased by the respective parent companies and not cancelled are classified as shares held in treasury. The consideration paid, including directly attributable costs, is recognised as a deduction from equity. Shares of the parent companies that are purchased by the Reed Elsevier Group plc Employee Benefit Trust are also classified as shares held in treasury, with the cost recognised as a deduction from equity.

#### **Critical judgments and key sources of estimation uncertainty**

The most significant accounting policies in determining the financial condition and results of the Reed Elsevier combined businesses, and those requiring the most subjective or complex judgment, relate to the valuation of goodwill and intangible assets, share based remuneration, pensions and taxation. The carrying amounts of goodwill and intangible

assets are reviewed at least twice a year, the key areas of judgment being in relation to the forecast long term growth rates and the appropriate discount rates to be applied to forecast cash flows. The charge for share based remuneration is determined based on the fair value of awards at the date of grant by use of binomial or Monte Carlo simulation models as appropriate, which require judgments to be made regarding share price volatility, dividend yield, risk free rates of return and expected option lives. Key estimates in accounting for defined benefit pension schemes are determined in conjunction with independent actuaries and include the life expectancy of members, expected salary and pension increases, inflation, the return on scheme assets and the rate at which future pension payments are discounted. Reed Elsevier's policy is to make provision for tax uncertainties where it is considered probable that tax payments may arise.

#### **Standards, amendments and interpretations not yet effective**

New accounting standards and amendments and their expected impact on the future accounting policies and reporting of Reed Elsevier are set out below.

IFRS7 – Financial Instruments: Disclosures (effective for financial years beginning on or after 1 January 2007). IFRS7 requires discussion of the significance of financial instruments for an entity's financial position and performance and introduces new qualitative and quantitative disclosures about exposure to risks arising from their use. Adoption of this standard is not expected to change significantly the disclosures related to financial instruments.

Amendment to IAS1 – Presentation of Financial Statements – Capital Disclosures (effective for financial years beginning on or after 1 January 2007). The amendment introduces disclosures about an entity's capital and how it manages capital. Adoption of this amendment is not expected to change significantly the presentation of the combined financial statements.

IFRS8 – Operating Segments (effective for financial years beginning on or after 1 January 2009). IFRS8 sets out requirements for disclosure of information about an entity's operating segments, its products and services, the geographical areas in which it operates, and its major customers. IFRS8 replaces IAS14 – Segment Reporting. Adoption of this standard is not expected to change significantly the disclosure of information in respect of Reed Elsevier's operating segments.

Additionally, a number of interpretations have been issued which are not expected to have any significant impact on Reed Elsevier's accounting policies and reporting.

## Notes to the combined financial statements

For the year ended 31 December 2006

### 1 Segment analysis

Reed Elsevier is a publisher and information provider organised as four business segments: Elsevier, comprising scientific, technical and medical publishing businesses; LexisNexis, providing legal, tax, regulatory, risk management, information analytics and business information solutions to professional, business and government customers; Harcourt Education, publishing school textbooks and related instructional and assessment materials; and Reed Business, providing information and marketing solutions to business professionals. Internal reporting is consistent with this organisational structure.

Adjusted operating profit figures are presented as an additional performance measure. They are stated before the amortisation of acquired intangible assets, acquisition integration costs and the equity share of taxes in joint ventures. Adjusted operating profit is reconciled to operating profit in note 9.

	Revenue		Operating profit		Adjusted operating profit	
	2006 €m	2005 €m	2006 €m	2005 €m	2006 €m	2005 €m
<b>Business segment</b>						
Elsevier	2,236	2,097	581	578	683	655
LexisNexis	2,308	2,140	388	318	559	493
Harcourt Education	1,307	1,315	63	127	190	235
Reed Business	2,084	1,990	269	231	354	313
Sub-total	7,935	7,542	1,301	1,254	1,786	1,696
Corporate costs	-	-	(57)	(47)	(57)	(47)
Unallocated net pension credit	-	-	50	18	50	18
<b>Total</b>	<b>7,935</b>	<b>7,542</b>	<b>1,294</b>	<b>1,225</b>	<b>1,779</b>	<b>1,667</b>
<b>Geographical origin</b>						
North America	4,379	4,216	535	531	885	869
United Kingdom	1,320	1,270	244	231	293	271
The Netherlands	739	730	254	235	259	242
Rest of Europe	1,007	878	177	155	253	206
Rest of world	490	448	84	73	89	79
<b>Total</b>	<b>7,935</b>	<b>7,542</b>	<b>1,294</b>	<b>1,225</b>	<b>1,779</b>	<b>1,667</b>

Revenue is analysed before the €159m (2005: €133m) share of joint ventures' revenue, of which €30m (2005: €29m) relates to LexisNexis, principally to Giuffrè, and €129m (2005: €104m) relates to Reed Business, principally to exhibition joint ventures.

Share of post-tax results of joint ventures of €27m (2005: €23m) included in operating profit comprises €5m (2005: €4m) relating to LexisNexis and €22m (2005: €19m) relating to Reed Business. The unallocated net pension credit of €50m (2005: €18m) comprises the expected return on pension scheme assets of €262m (2005: €218m) less interest on pension scheme liabilities of €212m (2005: €200m).

#### Analysis of revenue by geographical market

	2006 €m	2005 €m
North America	4,531	4,342
United Kingdom	870	829
The Netherlands	297	295
Rest of Europe	1,294	1,174
Rest of world	943	902
<b>Total</b>	<b>7,935</b>	<b>7,542</b>

## 1 Segment analysis continued

	Expenditure on acquired goodwill and intangible assets		Capital expenditure		Amortisation of acquired intangible assets		Depreciation and other amortisation	
	2006 €m	2005 €m	2006 €m	2005 €m	2006 €m	2005 €m	2006 €m	2005 €m
<b>Business segment</b>								
Elsevier	78	322	75	88	84	71	69	55
LexisNexis	116	85	139	139	153	149	103	95
Harcourt Education	9	10	43	32	126	107	22	20
Reed Business	75	67	44	39	73	76	40	37
Sub-total	278	484	301	298	436	403	234	207
Corporate	-	-	3	4	-	-	4	3
<b>Total</b>	<b>278</b>	<b>484</b>	<b>304</b>	<b>302</b>	<b>436</b>	<b>403</b>	<b>238</b>	<b>210</b>
<b>Geographical location</b>								
North America	152	141	198	191				
United Kingdom	80	23	53	51				
The Netherlands	-	13	26	26				
Rest of Europe	24	292	15	19				
Rest of world	22	15	12	15				
<b>Total</b>	<b>278</b>	<b>484</b>	<b>304</b>	<b>302</b>				

Capital expenditure comprises additions to property, plant and equipment and internally developed intangible assets. Other than the depreciation and amortisation above, non cash items of €72m (2005: €83m) relate to the recognition of share based remuneration and comprise €14m (2005: €16m) in Elsevier, €18m (2005: €23m) in LexisNexis, €7m (2005: €13m) in Harcourt Education, €21m (2005: €21m) in Reed Business and €12m (2005: €10m) in Corporate.

	Total assets		Total liabilities		Net assets/(liabilities)	
	2006 €m	2005 €m	2006 €m	2005 €m	2006 €m	2005 €m
<b>Business segment</b>						
Elsevier	3,504	3,716	1,081	1,108	2,423	2,608
LexisNexis	3,864	4,206	571	563	3,293	3,643
Harcourt Education	2,208	2,434	256	264	1,952	2,170
Reed Business	1,708	1,788	795	795	913	993
Sub-total	11,284	12,144	2,703	2,730	8,581	9,414
Taxation	253	388	1,980	2,244	(1,727)	(1,856)
Cash/borrowings	774	432	4,479	4,619	(3,705)	(4,187)
Net pension assets/obligations	30	-	381	591	(351)	(591)
Other assets and liabilities	372	361	221	243	151	118
<b>Total</b>	<b>12,713</b>	<b>13,325</b>	<b>9,764</b>	<b>10,427</b>	<b>2,949</b>	<b>2,898</b>
<b>Geographical location</b>						
North America	8,353	9,391	4,936	5,948	3,417	3,443
United Kingdom	1,541	1,313	1,674	893	(133)	420
The Netherlands	854	749	690	950	164	(201)
Rest of Europe	1,634	1,590	2,251	2,405	(617)	(815)
Rest of world	331	282	213	231	118	51
<b>Total</b>	<b>12,713</b>	<b>13,325</b>	<b>9,764</b>	<b>10,427</b>	<b>2,949</b>	<b>2,898</b>

Investments in joint ventures of €108m (2005: €104m) included in segment assets above comprise €40m (2005: €41m) relating to LexisNexis and €68m (2005: €63m) relating to Reed Business.

## Notes to the combined financial statements

For the year ended 31 December 2006

### 2 Operating profit

Operating profit is stated after charging/(crediting) the following:

	Note	2006 €m	2005 €m
<b>Staff costs</b>			
Wages and salaries		2,033	1,924
Social security costs		215	199
Pensions	4	117	146
Share based remuneration	5	72	83
<b>Total staff costs</b>		<b>2,437</b>	<b>2,352</b>
<b>Depreciation and amortisation</b>			
Amortisation of acquired intangible assets	14	436	403
Amortisation of internally developed intangible assets	14	104	83
Depreciation of property, plant and equipment	16	134	127
<b>Total depreciation and amortisation</b>		<b>674</b>	<b>613</b>
<b>Auditors' remuneration</b>			
For audit services		6.9	4.7
For non audit services		1.8	2.3
<b>Total auditors' remuneration</b>		<b>8.7</b>	<b>7.0</b>
<b>Other expenses and income</b>			
Pre-publication costs, inventory expenses and other cost of sales		2,915	2,759
Operating lease rentals expense		176	168
Operating lease rentals income		(25)	(20)

Depreciation and amortisation charges are included within administration and other expenses.

Auditors' remuneration for audit services comprises €0.6m (2005: €0.6m) payable to the auditors of the parent companies and €6.3m (2005: €4.1m) payable to the auditors of the parent companies and their associates for the audit of the financial statements of the operating and financing businesses, including for 2006 the review and testing of internal controls over financial reporting in accordance with the US Sarbanes-Oxley Act. Auditors' remuneration for non audit services comprises: €0.9m (2005: €1.0m) for taxation services, €0.4m (2005: €0.6m) for due diligence and other transaction related services, nil (2005: €0.1m) for the audit of associated pension schemes and €0.5m (2005: €0.6m) for other non audit services.

### 3 Personnel

Number of people employed	At 31 December		Average during the year	
	2006	2005	2006	2005
<b>Business segment</b>				
Elsevier	7,200	7,300	7,300	7,100
LexisNexis	13,800	13,400	13,700	13,200
Harcourt Education	5,300	5,400	5,300	5,400
Reed Business	10,300	10,200	10,300	10,200
Sub-total	36,600	36,300	36,600	35,900
Corporate/shared functions	200	200	200	200
<b>Total</b>	<b>36,800</b>	<b>36,500</b>	<b>36,800</b>	<b>36,100</b>
<b>Geographical location</b>				
North America	19,800	20,200	20,000	20,100
United Kingdom	6,000	5,800	5,900	5,800
The Netherlands	2,500	2,500	2,500	2,500
Rest of Europe	4,700	4,600	4,600	4,300
Rest of world	3,800	3,400	3,800	3,400
<b>Total</b>	<b>36,800</b>	<b>36,500</b>	<b>36,800</b>	<b>36,100</b>

## 4 Pension schemes

A number of pension schemes are operated around the world. The major schemes are of the defined benefit type with assets held in separate trustee administered funds. The largest schemes, which cover the majority of employees, are in the UK, the US and the Netherlands. Under these plans, employees are entitled to retirement benefits dependent on the number of years service provided.

The principal assumptions, for the purpose of valuation under IAS19 – Employee Benefits, are determined for each scheme in conjunction with the respective schemes' independent actuaries and are presented below as the weighted average of the various defined benefit pension schemes:

	2006	2005
Discount rate	5.3%	4.9%
Expected rate of return on scheme assets	7.0%	7.0%
Expected rate of salary increases	4.2%	4.0%
Inflation	2.9%	2.7%
Future pension increases	2.9%	2.8%

The expected rates of return on individual categories of scheme assets are determined by reference to relevant market indices. The overall expected rate of return on scheme assets is based on the weighted average of each asset category.

Mortality assumptions used in assessing defined benefit obligations make allowance for future improvements in longevity and have been determined by reference to applicable mortality statistics and the actuaries' expectations for each scheme. The average life expectancies assumed in the valuation of the defined benefit obligations are set out below.

Average life expectancy (at 31 December)	2006		2005	
	Male (years)	Female (years)	Male (years)	Female (years)
Member currently aged 60	86	87	83	86
Member currently aged 45	86	87	83	86

The increase in average life expectancies since 2005 follows the triennial actuarial valuation of the UK pension scheme.

The defined benefit pension expense recognised within operating expenses in the income statement comprises:

	2006 €m	2005 €m
Service cost (including curtailment credits of €16m (2005: nil))	138	133
Interest on pension scheme liabilities	212	200
Expected return on scheme assets	(262)	(218)
<b>Net defined benefit pension expense</b>	<b>88</b>	115

A total of €29m (2005: €31m) was recognised as an expense in relation to defined contribution pension schemes.

## Notes to the combined financial statements

For the year ended 31 December 2006

### 4 Pension schemes continued

The amount recognised in the balance sheet in respect of defined benefit pension schemes at the start and end of the year and the movements during the year were as follows:

	2006			2005		
	Defined benefit obligations €m	Fair value of scheme assets €m	Net pension obligations €m	Defined benefit obligations €m	Fair value of scheme assets €m	Net pension obligations €m
At start of year	(4,349)	3,758	(591)	(3,561)	3,108	(453)
Service cost (including curtailment credits of €16m (2005: nil))	(138)	–	(138)	(133)	–	(133)
Interest on pension scheme liabilities	(212)	–	(212)	(200)	–	(200)
Expected return on scheme assets	–	262	262	–	218	218
Actuarial gain/(loss)	59	145	204	(390)	336	(54)
Contributions by employer	–	90	90	–	68	68
Contributions by employees	(19)	19	–	(19)	19	–
Benefits paid	156	(150)	6	137	(137)	–
Exchange translation differences	21	7	28	(183)	146	(37)
<b>At end of year</b>	<b>(4,482)</b>	<b>4,131</b>	<b>(351)</b>	<b>(4,349)</b>	<b>3,758</b>	<b>(591)</b>

The net pension obligations of €351m at 31 December 2006 comprise schemes in surplus with net pension assets of €30m (2005: nil) and schemes in deficit with net pension obligations of €381m (2005: €591m).

As at 31 December 2006 the defined benefit obligations comprise €4,352m (2005: €4,218m) in relation to funded schemes and €130m (2005: €131m) in relation to unfunded schemes. The weighted average duration of defined benefit scheme liabilities is 19 years (2005: 19 years). Deferred tax assets of €137m (2005: €194m) and deferred tax liabilities of €9m (2005: nil) are recognised in respect of the net pension obligations.

The fair value of scheme assets held as equities, bonds and other assets, and their expected rates of return, is shown below:

	2006			2005		
	Expected rate of return on scheme assets	Fair value of scheme assets €m	Proportion of total scheme assets	Expected rate of return on scheme assets	Fair value of scheme assets €m	Proportion of total scheme assets
Equities	8.0%	2,767	67%	8.1%	2,493	66%
Bonds	4.4%	1,158	28%	4.3%	1,105	30%
Other	5.0%	206	5%	5.7%	160	4%
<b>Total</b>	<b>7.0%</b>	<b>4,131</b>	<b>100%</b>	<b>7.0%</b>	<b>3,758</b>	<b>100%</b>

The actual return on scheme assets for the year ended 31 December 2006 was €407m (2005: €553m).

A summary of pension balances for the three years ended 31 December 2006 is set out below.

	2006 €m	2005 €m	2004 €m
Fair value of scheme assets	4,131	3,758	3,108
Defined benefit obligations	(4,482)	(4,349)	(3,561)
<b>Net pension obligations</b>	<b>(351)</b>	<b>(591)</b>	<b>(453)</b>

## 4 Pension schemes continued

Gains and losses arising on the revaluation of pension scheme assets and liabilities that have been recognised in the statement of recognised income and expense are set out below:

	2006 €m	2005 €m	2004 €m
Gains and losses arising during the year:			
Experience losses on scheme liabilities	(44)	(37)	(26)
Experience gains on scheme assets	146	336	97
Actuarial gains/(losses) arising on the present value of scheme liabilities due to changes in:			
– discount rates	291	(317)	(166)
– inflation	(113)	–	–
– life expectancy and other actuarial assumptions	(75)	(36)	(14)
Net cumulative losses at start of year	205 (163)	(54) (109)	(109) –
<b>Net cumulative gains/(losses) at end of year</b>	<b>42</b>	<b>(163)</b>	<b>(109)</b>

The combined businesses expect to contribute approximately €97m to their defined benefit pension schemes in 2007.

### Sensitivity analysis

Valuation of Reed Elsevier's pension scheme liabilities involves judgments about uncertain events, including the life expectancy of the members, salary and pension increases, inflation and the rate at which the future pension payments are discounted. Estimates are used for each of these factors, determined in conjunction with independent actuaries. Differences arising from actual experience or future changes in assumptions may materially affect future pension charges. In particular, changes in assumptions for discount rates, inflation and life expectancies would have the following approximate effects on the annual net pension expense and the defined benefit pension obligations:

	€m
Increase/decrease of 0.25% in discount rate:	
Decrease/increase in annual net pension expense	10
Decrease/increase in defined benefit pension obligations	209
Increase/decrease of one year in assumed life expectancy:	
Increase/decrease in annual net pension expense	10
Increase/decrease in defined benefit pension obligations	134
Increase/decrease of 0.25% in the expected inflation rate:	
Increase/decrease in annual net pension expense	6
Increase/decrease in defined benefit pension obligations	149

Additionally, the annual net pension expense includes an expected return on scheme assets. A 5% increase/decrease in the market value of equity investments held by the defined benefit pension schemes would, absent any change in their expected long term rate of return, increase/decrease the amount of the expected return on scheme assets by €10m and would decrease/increase the amount of the net pension deficit by €134m.

## Notes to the combined financial statements

For the year ended 31 December 2006

### 5 Share based remuneration

Reed Elsevier provides a number of share based remuneration schemes to directors and employees. The principal share based remuneration schemes are the Executive Share Option Schemes (ESOS), the Long Term Incentive Scheme (LTIS), the Retention Share Plan (RSP) and the Bonus Investment Plan (BIP). Share options granted under ESOS and LTIS are exercisable after three years and up to ten years from the date of grant at a price equivalent to the market value of the respective shares at the date of grant. Conditional shares granted under ESOS, LTIS, RSP and BIP are exercisable after three years for nil consideration if conditions are met. Other awards principally relate to all employee share saving schemes in the UK and the Netherlands.

Share based remuneration awards are, other than in exceptional circumstances, subject to the condition that the employee remains in employment at the time of exercise. Share options and conditional shares granted under LTIS, RSP and BIP are subject to the achievement of growth targets of Reed Elsevier PLC and Reed Elsevier NV adjusted earnings per share measured at constant exchange rates. LTIS grants made in 2006 are variable subject to the achievement of an additional total shareholder return performance target. The numbers of share options and conditional shares included in the tables below are calculated on the basis that 100% of the awards will vest. Further details of performance conditions are given in the Directors' Remuneration Report on pages 34 to 51 of the Reed Elsevier Annual Reports and Financial Statements 2006.

The estimated fair value of grants made in the two years ended 31 December 2006 are set out below. The fair values of grants are recognised in the income statement over the vesting period, typically 3 years.

	In respect of Reed Elsevier PLC ordinary shares			In respect of Reed Elsevier NV ordinary shares			Total fair value
	Number of shares '000	Weighted average fair value per award €	Fair value €m	Number of shares '000	Weighted average fair value per award €	Fair value €m	€m
<b>2006 grants</b>							
Share options							
- ESOS	4,731	1.47	6	3,169	1.87	6	12
- LTIS	3	1.47	-	2	1.91	-	-
- Other	1,168	2.18	3	243	2.17	-	3
<b>Total share options</b>	<b>5,902</b>	<b>1.60</b>	<b>9</b>	<b>3,414</b>	<b>1.89</b>	<b>6</b>	<b>15</b>
Conditional shares							
- ESOS	1,202	7.23	9	806	10.51	9	18
- LTIS	2,003	7.98	16	1,318	11.96	16	32
- BIP	683	7.45	6	280	10.71	3	9
<b>Total conditional shares</b>	<b>3,888</b>	<b>7.66</b>	<b>31</b>	<b>2,404</b>	<b>11.33</b>	<b>28</b>	<b>59</b>
<b>Total</b>			<b>40</b>			<b>34</b>	<b>74</b>

	In respect of Reed Elsevier PLC ordinary shares			In respect of Reed Elsevier NV ordinary shares			Total fair value
	Number of shares '000	Weighted average fair value per award €	Fair value €m	Number of shares '000	Weighted average fair value per award €	Fair value €m	€m
<b>2005 grants</b>							
Share options							
- ESOS	10,346	1.51	16	7,049	1.90	13	29
- LTIS	234	1.45	-	159	1.87	-	-
- Other	940	2.25	2	263	2.01	1	3
<b>Total share options</b>	<b>11,520</b>	<b>1.53</b>	<b>18</b>	<b>7,471</b>	<b>1.91</b>	<b>14</b>	<b>32</b>
Conditional shares							
- LTIS	107	6.76	-	74	9.76	-	-
- RSP	152	6.85	1	103	10.18	2	3
- BIP	692	7.23	6	229	10.48	2	8
<b>Total conditional shares</b>	<b>951</b>	<b>7.11</b>	<b>7</b>	<b>406</b>	<b>10.27</b>	<b>4</b>	<b>11</b>
<b>Total</b>			<b>25</b>			<b>18</b>	<b>43</b>

## 5 Share based remuneration continued

The main assumptions used to determine the fair values, which have been established with advice from and data provided by independent actuaries, are set out below.

Assumptions for grants made during the year	In respect of Reed Elsevier PLC ordinary shares		In respect of Reed Elsevier NV ordinary shares	
	2006	2005	2006	2005
Weighted average share price at date of grant				
– ESOS	£5.32	£5.33	€11.51	€11.31
– LTIS	£5.36	£5.12	€11.81	€11.01
– RSP		£4.94		€10.71
– BIP	£5.48	£5.37	€11.74	€11.35
– Other	£5.30	£5.30	€12.05	€11.19
Expected share price volatility	22%	22%	22%	22%
Expected option life	4 years	4 years	4 years	4 years
Expected dividend yield	2.6%	2.6%	3.1%	2.6%
Risk free interest rate	4.6%	5.1%	3.5%	3.4%
Expected lapse rate	3-5%	3-5%	3-5%	3-5%

Expected share price volatility has been estimated based on relevant historic data in respect of the Reed Elsevier PLC and Reed Elsevier NV ordinary share prices. Expected share option life has been estimated based on historical exercise patterns in respect of Reed Elsevier PLC and Reed Elsevier NV share options.

The share based remuneration awards outstanding as at 31 December 2006, in respect of both Reed Elsevier PLC and Reed Elsevier NV ordinary shares, are set out below.

	ESOS		LTIS		Other		Total	
	Number of shares '000	Weighted average exercise price (pence)	Number of shares '000	Weighted average exercise price (pence)	Number of shares '000	Weighted average exercise price (pence)	Number of shares '000	Weighted average exercise price (pence)
<b>Share options: Reed Elsevier PLC</b>								
Outstanding at 1 January 2005	54,641	508	5,138	487	3,876	408	63,655	500
Granted	10,346	533	234	516	940	424	11,520	524
Exercised	(3,027)	441	–	–	(602)	348	(3,629)	426
Forfeited	(4,146)	532	(91)	487	(678)	442	(4,915)	519
Expired	(74)	443	–	–	(18)	423	(92)	439
Outstanding at 1 January 2006	<b>57,740</b>	<b>514</b>	<b>5,281</b>	<b>488</b>	<b>3,518</b>	<b>416</b>	<b>66,539</b>	<b>507</b>
Granted	4,731	532	3	535	1,168	424	5,902	510
Exercised	(9,691)	461	–	–	(792)	411	(10,483)	457
Forfeited	(4,088)	543	(267)	487	(299)	413	(4,654)	532
Expired	(500)	584	–	–	(222)	507	(722)	561
<b>Outstanding at 31 December 2006</b>	<b>48,192</b>	<b>523</b>	<b>5,017</b>	<b>488</b>	<b>3,373</b>	<b>414</b>	<b>56,582</b>	<b>513</b>
Exercisable at 31 December 2005	22,471	552	65	487	211	506	22,747	552
<b>Exercisable at 31 December 2006</b>	<b>22,121</b>	<b>537</b>	<b>105</b>	<b>487</b>	<b>91</b>	<b>425</b>	<b>22,317</b>	<b>537</b>

## Notes to the combined financial statements

For the year ended 31 December 2006

### 5 Share based remuneration continued

	ESOS		LTIS		Other		Total	
	Number of shares '000	Weighted average exercise price (€)	Number of shares '000	Weighted average exercise price (€)	Number of shares '000	Weighted average exercise price (€)	Number of shares '000	Weighted average exercise price (€)
<b>Share options: Reed Elsevier NV</b>								
Outstanding at 1 January 2005	36,770	11.33	3,529	10.55	1,804	12.07	42,103	11.30
Granted	7,049	11.31	159	11.21	263	11.19	7,471	11.30
Exercised	(1,817)	10.29	–	–	(75)	12.26	(1,892)	10.37
Forfeited	(2,750)	11.88	(62)	10.57	–	–	(2,812)	11.85
Expired	–	–	–	–	(111)	10.16	(111)	10.16
Outstanding at 1 January 2006	<b>39,252</b>	<b>11.33</b>	<b>3,626</b>	<b>10.58</b>	<b>1,881</b>	<b>12.05</b>	<b>44,759</b>	<b>11.30</b>
Granted	3,169	11.51	2	11.76	243	12.05	3,414	11.55
Exercised	(6,666)	9.98	–	–	(243)	10.76	(6,909)	10.01
Forfeited	(2,799)	12.13	(183)	10.57	(35)	12.83	(3,017)	12.04
<b>Outstanding at 31 December 2006</b>	<b>32,956</b>	<b>11.55</b>	<b>3,445</b>	<b>10.58</b>	<b>1,846</b>	<b>12.21</b>	<b>38,247</b>	<b>11.50</b>
Exercisable at 31 December 2005	14,631	12.91	45	10.57	1,881	12.05	16,557	12.81
<b>Exercisable at 31 December 2006</b>	<b>15,055</b>	<b>12.24</b>	<b>72</b>	<b>10.57</b>	<b>1,846</b>	<b>12.21</b>	<b>16,973</b>	<b>12.23</b>

Conditional shares: Reed Elsevier PLC	Number of shares '000				
	ESOS	LTIS	RSP	BIP	Total
Outstanding at 1 January 2005	–	2,346	2,285	710	5,341
Granted	–	107	152	692	951
Exercised	–	–	(46)	(5)	(51)
Forfeited	–	(40)	(259)	(18)	(317)
Outstanding at 1 January 2006	–	<b>2,413</b>	<b>2,132</b>	<b>1,379</b>	<b>5,924</b>
Granted	1,202	2,003	–	683	3,888
Exercised	(4)	–	(54)	(221)	(279)
Forfeited	(49)	(172)	(246)	(108)	(575)
<b>Outstanding at 31 December 2006</b>	<b>1,149</b>	<b>4,244</b>	<b>1,832</b>	<b>1,733</b>	<b>8,958</b>

Conditional shares: Reed Elsevier NV	Number of shares '000				
	ESOS	LTIS	RSP	BIP	Total
Outstanding at 1 January 2005	–	1,611	1,568	304	3,483
Granted	–	74	103	229	406
Exercised	–	–	(32)	–	(32)
Forfeited	–	(28)	(176)	(18)	(222)
Outstanding at 1 January 2006	–	<b>1,657</b>	<b>1,463</b>	<b>515</b>	<b>3,635</b>
Granted	806	1,318	–	280	2,404
Exercised	(3)	–	(36)	(101)	(140)
Forfeited	(33)	(117)	(149)	(45)	(344)
<b>Outstanding at 31 December 2006</b>	<b>770</b>	<b>2,858</b>	<b>1,278</b>	<b>649</b>	<b>5,555</b>

The weighted average share price at the date of exercise of share options and conditional shares during 2006 was 564p (2005: 533p) for Reed Elsevier PLC ordinary shares and €12.34 (2005: €11.31) for Reed Elsevier NV ordinary shares.

5 Share based remuneration continued

	2006		2005	
	Number of shares under option '000	Weighted average remaining period until expiry (years)	Number of shares under option '000	Weighted average remaining period until expiry (years)
<b>Range of exercise prices for outstanding share options</b>				
<b>Reed Elsevier PLC ordinary shares (pence)</b>				
301-350	-	-	38	0.1
351-400	1,345	1.4	2,161	2.3
401-450	4,733	3.0	6,110	4.0
451-500	23,953	5.5	31,858	6.6
501-550	15,462	7.8	12,981	8.1
551-600	6,639	4.7	8,283	5.2
601-650	852	2.8	1,019	3.6
651-700	3,598	4.1	4,089	5.1
<b>Total</b>	<b>56,582</b>	<b>5.6</b>	<b>66,539</b>	<b>6.2</b>
<b>Reed Elsevier NV ordinary shares (euro)</b>				
8.01-9.00	-	-	9	7.2
9.01-10.00	4,146	6.2	8,034	7.0
10.01-11.00	14,595	5.1	17,919	5.9
11.01-12.00	10,589	8.0	8,774	8.0
12.01-13.00	307	5.6	356	3.3
13.01-14.00	5,163	4.8	5,808	5.4
14.01-15.00	2,896	4.2	3,223	4.7
15.01-16.00	551	2.7	636	2.6
<b>Total</b>	<b>38,247</b>	<b>5.9</b>	<b>44,759</b>	<b>6.3</b>

Share options are expected, upon exercise, to be met principally by the issue of new ordinary shares but may also be met from shares held by the Reed Elsevier Group plc Employee Benefit Trust (EBT) (see note 28). Conditional shares will be met from shares held by the EBT.

## Notes to the combined financial statements

For the year ended 31 December 2006

### 6 Net finance costs

	2006 €m	2005 €m
Interest on bank loans, overdrafts and commercial paper	(65)	(64)
Interest on other loans	(188)	(153)
Interest on obligations under finance leases	(2)	(1)
Total borrowing costs	(255)	(218)
Losses on derivatives not designated as hedges	(5)	(29)
Fair value losses on interest rate derivatives formerly designated as cash flow hedges transferred from equity	(4)	(9)
<b>Finance costs</b>	<b>(264)</b>	<b>(256)</b>
Interest on bank deposits	21	14
Gains on loans and derivatives not designated as hedges	10	38
<b>Finance income</b>	<b>31</b>	<b>52</b>
<b>Net finance costs</b>	<b>(233)</b>	<b>(204)</b>

Finance costs include €8m (2005: €16m) transferred from the hedge reserve. A net gain of €2m (2005: €16m) on interest rate derivatives designated as cash flow hedges was recognised directly in equity in the hedge reserve.

### 7 Disposals and other non operating items

	2006 €m	2005 €m
Revaluation of held for trading investments	2	4
Loss on disposal of businesses and other assets	(3)	(2)
<b>Net (loss)/gain on disposals and other non operating items</b>	<b>(1)</b>	<b>2</b>

### 8 Taxation

	2006 €m	2005 €m
Current tax		
United Kingdom	87	124
The Netherlands	73	70
Rest of world	6	121
Total current tax	166	315
Deferred tax		
Origination and reversal of timing differences	(25)	31
<b>Total</b>	<b>141</b>	<b>346</b>

The current tax charge includes credits of €96m (2005: nil) in respect of prior year disposals.

## 8 Taxation continued

A reconciliation of the notional tax charge based on average applicable rates of tax (weighted in proportion to accounting profits) to the actual total tax expense is set out below.

	2006 €m	2005 €m
Profit before tax	1,060	1,023
Tax at average applicable rates	250	225
Tax on share of results of joint ventures	(9)	(9)
Deferred tax on unrealised exchange differences on long term inter-affiliate lending	(32)	64
Adjustments relating to prior year disposals	(96)	–
Non deductible amounts and other items	28	66
<b>Tax expense</b>	<b>141</b>	<b>346</b>
<b>Tax expense as a percentage of profit before tax</b>	<b>13%</b>	<b>34%</b>

The following tax has been recognised directly in equity during the year.

	2006 €m	2005 €m
Tax on actuarial movements on defined benefit pension schemes	(66)	15
Tax on fair value movements on cash flow hedges	(26)	(19)
Deferred tax credits on share based remuneration	4	–
<b>Net tax charge recognised directly in equity</b>	<b>(88)</b>	<b>(4)</b>

During 2006, a tax charge of €4m was transferred to net profit from the hedge reserve (2005: nil). Current taxation liabilities as at 31 December 2005 include €420m previously reported within non-current liabilities.

## 9 Adjusted figures

Reed Elsevier uses adjusted figures as additional performance measures. Adjusted figures are stated before amortisation of acquired intangible assets, acquisition integration costs, disposals and other non operating items, related tax effects and movements in deferred taxation assets and liabilities that are not expected to crystallise in the near term. Adjusted operating profit is also grossed up to exclude the equity share of taxes in joint ventures.

Adjusted operating cash flow is measured after net capital expenditure and dividends from joint ventures but before payments in relation to acquisition integration costs.

	2006 €m	2005 €m
Operating profit	1,294	1,225
Adjustments:		
Amortisation of acquired intangible assets	436	403
Acquisition integration costs	34	30
Reclassification of tax in joint ventures	15	9
<b>Adjusted operating profit</b>	<b>1,779</b>	<b>1,667</b>
Profit before tax	1,060	1,023
Adjustments:		
Amortisation of acquired intangible assets	436	403
Acquisition integration costs	34	30
Reclassification of tax in joint ventures	15	9
Disposals and other non operating items	1	(2)
<b>Adjusted profit before tax</b>	<b>1,546</b>	<b>1,463</b>

## Notes to the combined financial statements

For the year ended 31 December 2006

### 9 Adjusted figures continued

	2006 €m	2005 €m
Profit attributable to parent companies' shareholders	916	675
Adjustments (post tax):		
Amortisation of acquired intangible assets	476	452
Acquisition integration costs	24	24
Disposals and other non operating items	(95)	(2)
Deferred tax not expected to crystallise in the near term:		
Unrealised exchange differences on long term inter affiliate lending	(32)	64
Acquired intangible assets	(128)	(95)
Other	9	(17)
<b>Adjusted profit attributable to parent companies' shareholders</b>	<b>1,170</b>	<b>1,101</b>
Cash generated from operations	1,917	1,786
Dividends received from joint ventures	24	23
Purchases of property, plant and equipment	(129)	(136)
Proceeds on disposals of property, plant and equipment	3	12
Expenditure on internally developed intangible assets	(159)	(149)
Payments in relation to acquisition integration costs	37	41
<b>Adjusted operating cash flow</b>	<b>1,693</b>	<b>1,577</b>

### 10 Cash flow statement

Reconciliation of operating profit before joint ventures to cash generated from operations	Note	2006 €m	2005 €m
Operating profit before joint ventures		1,267	1,202
Amortisation of acquired intangible assets	14	436	403
Amortisation of internally developed intangible assets	14	104	83
Depreciation of property, plant and equipment	16	134	127
Share based remuneration		72	83
<b>Total non cash items</b>		<b>746</b>	<b>696</b>
Increase in inventories and pre-publication costs		(75)	(82)
Increase in receivables		(95)	(134)
Increase in payables		74	104
<b>Increase in working capital</b>		<b>(96)</b>	<b>(112)</b>
<b>Cash generated from operations</b>		<b>1,917</b>	<b>1,786</b>

Cash flow on acquisitions	Note	2006 €m	2005 €m
Purchase of businesses	11	(219)	(428)
Investment in joint ventures		(2)	(22)
Deferred payments relating to prior year acquisitions		(19)	(13)
<b>Total</b>		<b>(240)</b>	<b>(463)</b>

## 10 Cash flow statement continued

	Cash & cash equivalents €m	Borrowings €m	Related derivative financial instruments €m	2006 €m	2005 €m
<b>Reconciliation of net borrowings</b>					
At start of year	432	(4,619)	254	(3,933)	(3,578)
Increase in cash and cash equivalents	351	-	-	351	96
Net movement in bank loans, overdrafts and commercial paper	-	(105)	-	(105)	718
Issuance of other loans	-	(598)	-	(598)	(794)
Repayment of other loans	-	495	-	495	132
Repayment of finance leases	-	18	-	18	19
<b>Change in net borrowings resulting from cash flows</b>	<b>351</b>	<b>(190)</b>	<b>-</b>	<b>161</b>	<b>171</b>
Inception of finance leases	-	(14)	-	(14)	(15)
Fair value adjustments to borrowings and related derivatives	-	(26)	31	5	7
Exchange translation differences	(9)	370	(28)	333	(518)
<b>At end of year</b>	<b>774</b>	<b>(4,479)</b>	<b>257</b>	<b>(3,448)</b>	<b>(3,933)</b>

Net borrowings comprise cash and cash equivalents, loan capital, finance leases, promissory notes, bank and other loans, and those derivative financial instruments that are used to hedge the fair value of fixed rate borrowings.

## 11 Acquisitions

During the year a number of acquisitions were made for a total consideration amounting to €251m, after taking account of net cash acquired of €10m.

The net assets of the businesses acquired are incorporated at their fair value to the combined businesses. The fair values of the consideration given and the assets and liabilities acquired are summarised below.

	Note	Book value on acquisition €m	Fair value adjustments €m	Fair value €m
Goodwill	13	-	150	150
Intangible assets	14	2	126	128
Property, plant and equipment	16	1	-	1
Current assets		13	-	13
Current liabilities		(25)	-	(25)
Deferred tax		-	(16)	(16)
<b>Net assets acquired</b>		<b>(9)</b>	<b>260</b>	<b>251</b>
<b>Consideration (after taking account of €10m net cash acquired)</b>				<b>251</b>
Less: consideration deferred to future years				(32)
<b>Net cash flow</b>				<b>219</b>

The fair value adjustments in relation to the acquisitions made in 2006 relate principally to the valuation of intangible assets. Goodwill, being the excess of the consideration over the net tangible and intangible assets acquired, represents benefits which do not qualify for recognition as intangible assets, including skilled workforces and acquisition synergies that are specific to Reed Elsevier. In addition, goodwill arises on the recognition of deferred tax liabilities in respect of intangible assets for which amortisation does not qualify for tax deductions.

The businesses acquired in 2006 contributed €47m to revenue, €9m to adjusted operating profit, reduced net profit by €13m and contributed €10m to net cash inflow from operating activities for the part year under Reed Elsevier ownership. Had the businesses been acquired at the beginning of the year, on a proforma basis the Reed Elsevier revenues, adjusted operating profit and net profit for the year would have been €7,972m, €1,788m and €917m respectively.

## Notes to the combined financial statements

For the year ended 31 December 2006

### 12 Equity dividends

	2006 €m	2005 €m
<b>Dividends declared in the year</b>		
Reed Elsevier PLC	273	246
Reed Elsevier NV	272	245
<b>Total</b>	<b>545</b>	491

Dividends declared in the year, in amounts per ordinary share, comprise: a 2005 final dividend of 10.7p and 2006 interim dividend of 4.1p giving a total of 14.8p (2005: 13.3p) for Reed Elsevier PLC; and a 2005 final dividend of €0.267 and 2006 interim dividend of €0.102 giving a total of €0.369 (2005: €0.332) for Reed Elsevier NV.

The directors of Reed Elsevier PLC have proposed a final dividend of 11.8p (2005: 10.7p). The directors of Reed Elsevier NV have proposed a final dividend of €0.304 (2005: €0.267). The total cost of funding the proposed final dividends is expected to be €444m, for which no liability has been recognised at the date of the balance sheet.

	2006 €m	2005 €m
<b>Dividends paid and proposed relating to the financial year</b>		
Reed Elsevier PLC	293	267
Reed Elsevier NV	298	265
<b>Total</b>	<b>591</b>	532

Dividends paid to Reed Elsevier PLC and Reed Elsevier NV shareholders are, other than in special circumstances, equalised at the gross level inclusive of the UK tax credit of 10% received by certain Reed Elsevier PLC shareholders. The cost of funding the Reed Elsevier PLC dividends is therefore similar to that of Reed Elsevier NV.

### 13 Goodwill

	2006 €m	2005 €m
At start of year	4,424	3,682
Acquisitions	150	266
Disposals	(29)	(21)
Exchange translation differences	(370)	497
<b>At end of year</b>	<b>4,175</b>	4,424

The carrying amount of goodwill includes cumulative amortisation of €2,450m (2005: €2,697m), which was charged prior to the adoption of IFRS.

## 13 Goodwill continued

For the purposes of impairment testing, goodwill is recorded in the cash generating units that are expected to benefit from each acquisition. The carrying value of goodwill recorded in the major groups of cash generating units is set out below.

<b>Goodwill</b>	2006 €m	2005 €m
Elsevier	1,109	1,199
LexisNexis US	1,605	1,753
LexisNexis International	179	150
Harcourt Schools US	450	504
Reed Exhibitions	393	390
Other	439	428
<b>Total</b>	<b>4,175</b>	<b>4,424</b>

The carrying value of each cash generating unit is compared with its estimated value in use, which is determined to be its recoverable amount. Value in use is calculated based on estimated future cash flows, discounted to their present value. The pre-tax discount rates used are between 10-12%, including a risk premium appropriate to the unit being reviewed. Estimated future cash flows are determined by reference to latest budgets and forecasts for the next five years, with a 3% long term nominal growth rate assumed thereafter.

## 14 Intangible assets

	Market and customer related €m	Content, software and other €m	Total acquired intangible assets €m	Internally developed intangible assets €m	Total €m
<b>Cost</b>					
At 1 January 2005	1,766	4,038	5,804	721	6,525
Acquisitions	129	89	218	–	218
Additions	–	–	–	149	149
Disposals	–	(43)	(43)	–	(43)
Exchange translation differences	279	417	696	75	771
At 1 January 2006	<b>2,174</b>	<b>4,501</b>	<b>6,675</b>	<b>945</b>	<b>7,620</b>
Acquisitions	63	65	128	–	128
Additions	–	–	–	159	159
Disposals	(3)	(23)	(26)	(108)	(134)
Exchange translation differences	(215)	(265)	(480)	(53)	(533)
<b>At 31 December 2006</b>	<b>2,019</b>	<b>4,278</b>	<b>6,297</b>	<b>943</b>	<b>7,240</b>
<b>Amortisation</b>					
At 1 January 2005	142	1,985	2,127	401	2,528
Charge for the year	124	279	403	83	486
Disposals	–	(13)	(13)	–	(13)
Exchange translation differences	27	205	232	38	270
At 1 January 2006	<b>293</b>	<b>2,456</b>	<b>2,749</b>	<b>522</b>	<b>3,271</b>
Charge for the year	156	280	436	104	540
Disposals	(2)	(23)	(25)	(96)	(121)
Exchange translation differences	(36)	(150)	(186)	(25)	(211)
<b>At 31 December 2006</b>	<b>411</b>	<b>2,563</b>	<b>2,974</b>	<b>505</b>	<b>3,479</b>
<b>Net book amount</b>					
At 31 December 2005	1,881	2,045	3,926	423	4,349
<b>At 31 December 2006</b>	<b>1,608</b>	<b>1,715</b>	<b>3,323</b>	<b>438</b>	<b>3,761</b>

## Notes to the combined financial statements

For the year ended 31 December 2006

### 14 Intangible assets *continued*

Intangible assets acquired as part of business combinations comprise: market related assets (e.g. trade marks, imprints, brands); customer related assets (e.g. subscription bases, customer lists, customer relationships); and content, software and other intangible assets (e.g. editorial content, software and product delivery systems, other publishing rights, exhibition rights and supply contracts). Included in content, software and other acquired intangible assets are assets with a net book value of €1,393m (2005: €1,685m) that arose on acquisitions completed prior to the adoption of IFRS that have not been allocated to specific categories of intangible assets. Internally developed intangible assets typically comprise software and systems development where an identifiable asset is created that is probable to generate future economic benefits.

Included in market and customer related intangible assets are €437m (2005: €486m) of brands and imprints relating to Elsevier determined to have indefinite lives based on an assessment of their historical longevity and stable market positions.

### 15 Investments

	2006 €m	2005 €m
Investments in joint ventures	108	104
Available for sale investments	37	32
Venture capital investments held for trading	38	32
<b>Total</b>	<b>183</b>	168

An analysis of changes in the carrying value of investments in joint ventures is set out below.

	2006 €m	2005 €m
At start of year	104	86
Share of results of joint ventures	27	23
Dividends received from joint ventures	(24)	(23)
Additions	1	22
Transfers	–	(4)
Exchange translation differences	–	–
<b>At end of year</b>	<b>108</b>	104

The principal joint ventures at 31 December 2006 are exhibition joint ventures within Reed Business and Giuffrè (an Italian legal publisher in which Reed Elsevier has a 40% shareholding).

Summarised aggregate information in respect of joint ventures and Reed Elsevier's share is set out below.

	Total joint ventures		Reed Elsevier share	
	2006 €m	2005 €m	2006 €m	2005 €m
Revenue	326	283	159	133
Net profit for the year	53	48	27	23
Total assets	320	321	147	151
Total liabilities	(180)	(200)	(82)	(92)
<b>Net assets</b>	<b>140</b>	121	<b>65</b>	59
Goodwill			43	45
<b>Total</b>			<b>108</b>	104

## 16 Property, plant and equipment

	2006			2005		
	Land and buildings €m	Fixtures and equipment €m	Total €m	Land and buildings €m	Fixtures and equipment €m	Total €m
<b>Cost</b>						
At start of year	280	1,015	1,295	257	884	1,141
Acquisitions	–	3	3	–	9	9
Capital expenditure	13	131	144	7	143	150
Disposals	(4)	(81)	(85)	(15)	(125)	(140)
Exchange translation differences	(22)	(74)	(96)	31	104	135
<b>At end of year</b>	<b>267</b>	<b>994</b>	<b>1,261</b>	<b>280</b>	<b>1,015</b>	<b>1,295</b>
<b>Accumulated depreciation</b>						
At start of year	122	715	837	102	627	729
Acquisitions	–	2	2	–	6	6
Disposals	(4)	(81)	(85)	(4)	(111)	(115)
Charge for the year	12	122	134	12	115	127
Exchange translation differences	(6)	(65)	(71)	12	78	90
<b>At end of year</b>	<b>124</b>	<b>693</b>	<b>817</b>	<b>122</b>	<b>715</b>	<b>837</b>
<b>Net book amount</b>	<b>143</b>	<b>301</b>	<b>444</b>	<b>158</b>	<b>300</b>	<b>458</b>

No depreciation is provided on freehold land. The net book amount of property, plant and equipment at 31 December 2006 includes €24m (2005: €29m) in respect of assets held under finance leases relating to fixtures and equipment.

## Notes to the combined financial statements

For the year ended 31 December 2006

### 17 Financial instruments

Details of the objectives, policies and strategies pursued by Reed Elsevier in relation to financial instruments are set out on pages 18 and 19 of the Operating and Financial Review. The main financial risks faced by Reed Elsevier are liquidity risk, market risk – comprising interest rate risk and foreign exchange risk – and credit risk. Financial instruments are used to finance the Reed Elsevier businesses and to hedge interest rate and foreign exchange risks. Reed Elsevier's businesses do not enter into speculative derivative transactions. Details of financial instruments subject to liquidity, market and credit risks are described below.

#### Liquidity risk

Reed Elsevier maintains a range of borrowing facilities and debt programmes to fund its requirements, at short notice and at competitive rates. The remaining contractual maturities for borrowings and derivative financial instruments are shown in the table below. The table shows undiscounted principal and interest cash flows and includes contractual gross cash flows to be exchanged as part of cross currency interest rate swaps and forward foreign exchange contracts where there is a legal right of set off.

At 31 December 2006	Carrying amount €m	Contractual cash flow						Total €m
		Within 1 year €m	1-2 years €m	2-3 years €m	3-4 years €m	4-5 years €m	More than 5 years €m	
<b>Borrowings</b>								
Fixed rate borrowings	(3,113)	(605)	(663)	(133)	(132)	(550)	(2,653)	(4,736)
Floating rate borrowings	(1,366)	(982)	(19)	(19)	(419)	–	(3)	(1,442)
<b>Derivative financial liabilities</b>								
Interest rate derivatives	(10)	(10)	(6)	(1)	(1)	(1)	(12)	(31)
Cross currency interest rate swaps	–	(256)	(355)	–	–	–	–	(611)
Forward foreign exchange contracts	(4)	(754)	(316)	(143)	–	–	–	(1,213)
<b>Derivative financial assets</b>								
Interest rate derivatives	12	14	7	1	1	1	4	28
Cross currency interest rate swaps	259	353	529	–	–	–	–	882
Forward foreign exchange contracts	55	787	339	149	–	–	–	1,275
<b>Total</b>	<b>(4,167)</b>	<b>(1,453)</b>	<b>(484)</b>	<b>(146)</b>	<b>(551)</b>	<b>(550)</b>	<b>(2,664)</b>	<b>(5,848)</b>

At 31 December 2005	Carrying amount €m	Contractual cash flow						Total €m
		Within 1 year €m	1-2 years €m	2-3 years €m	3-4 years €m	4-5 years €m	More than 5 years €m	
<b>Borrowings</b>								
Fixed rate borrowings	(3,245)	(669)	(603)	(635)	(106)	(111)	(2,681)	(4,805)
Floating rate borrowings	(1,374)	(851)	(123)	(19)	(20)	(454)	(3)	(1,470)
<b>Derivative financial liabilities</b>								
Interest rate derivatives	(17)	(13)	(9)	(6)	(2)	(1)	(4)	(35)
Cross currency interest rate swaps	–	(34)	(282)	(394)	–	–	–	(710)
Forward foreign exchange contracts	(13)	(750)	(346)	(158)	–	–	–	(1,254)
<b>Derivative financial assets</b>								
Interest rate derivatives	38	19	12	6	1	1	22	61
Cross currency interest rate swaps	233	42	365	530	–	–	–	937
Forward foreign exchange contracts	21	761	348	155	–	–	–	1,264
<b>Total</b>	<b>(4,357)</b>	<b>(1,495)</b>	<b>(638)</b>	<b>(521)</b>	<b>(127)</b>	<b>(565)</b>	<b>(2,666)</b>	<b>(6,012)</b>

The carrying amount of derivative financial liabilities comprises €5m (2005: nil) in relation to fair value hedges, €6m (2005: €23m) in relation to cash flow hedges and €3m (2005: €7m) held for trading. The carrying amount of derivative financial assets comprises €262m (2005: €254m) in relation to fair value hedges, €63m (2005: €31m) in relation to cash flow hedges and €1m (2005: €7m) held for trading. Derivative financial assets and liabilities held for trading comprise interest rate derivatives that were not designated as hedging instruments on adoption of IAS39 – Financial Instruments.

## 17 Financial instruments *continued*

At 31 December 2006, Reed Elsevier had access to €2,278m (2005: €2,539m) of committed bank facilities that expire in two to three years, of which €58m (2005: €98m) was drawn. These facilities principally provide back up for short term borrowings.

After taking account of the maturity of committed bank facilities that back short term borrowings at 31 December 2006, and after utilising available cash resources, no borrowings mature in the next two years (2005: nil); 25% of borrowings mature in the third year (2005: 46%); 24% in the fourth and fifth years (2005: 11%); 37% in the sixth to tenth years (2005: 29%); and 14% beyond the tenth year (2005: 14%).

### Market Risk

Reed Elsevier's primary market risks are to interest rate fluctuations and exchange rate movements. Derivatives are used to hedge or reduce the risks of interest rate and exchange rate movements and are not entered into unless such risks exist. Derivatives used by Reed Elsevier for hedging a particular risk are not specialised and are generally available from numerous sources.

#### *Interest rate risk*

Reed Elsevier's interest rate exposure management policy is aimed at reducing the exposure of the combined businesses to changes in interest rates.

At 31 December 2006, 88% of net borrowings are either fixed rate or have been fixed through the use of interest rate swaps, forward rate agreements and options. A 100 basis point reduction in interest rates would result in an estimated decrease in net finance costs of €4m (2005: €7m), based on the composition of financial instruments including cash, cash equivalents, bank loans and commercial paper borrowings at 31 December 2006. A 100 basis point rise in interest rates would result in an estimated increase in net finance costs of €4m (2005: €7m). The range of changes represents Reed Elsevier's view of the changes that are reasonably possible over a one year period.

The impact on net equity of a theoretical change in interest rates as at 31 December 2006 is restricted to the change in carrying value of floating rate to fixed rate interest rate derivatives in a designated cash flow hedge relationship and undesignated interest rate derivatives. A 100 basis point reduction in interest rates would result in an estimated reduction in net equity of €13m (2005: €23m) and a 100 basis point increase in interest rates would increase net equity by an estimated €12m (2005: €23m). The impact of a change in interest rates on the carrying value of fixed rate borrowings in a designated fair value hedge relationship would be offset by the change in carrying value of the related interest rate derivative. Fixed rate borrowings not in a designated hedging relationship are carried at amortised cost.

#### *Foreign exchange rate risk*

Translation exposures arise on the earnings and net assets of business operations in countries with currencies other than sterling, most particularly in respect of the US businesses. These exposures are hedged, to a significant extent, by a policy of denominating borrowings in currencies where significant translation exposures exist, most notably US dollars (see note 22).

A theoretical weakening of all currencies by 10% against euros at 31 December 2006 would decrease the carrying value of net assets, excluding net borrowings, by €506m (2005: €567m). This would be offset to a large degree by a decrease in net borrowings of €269m (2005: €310m). A strengthening of all currencies by 10% against euros at 31 December 2006 would increase the carrying value of net assets, excluding borrowings, by €621m (2005: €696m) and increase net borrowings by €329m (2005: €378m).

A retranslation of the combined businesses' net profit for the year assuming a 10% weakening of all foreign currencies against euros but excluding transactional exposures would reduce net profit by €53m (2005: €41m). A 10% strengthening of all foreign currencies against euros on this basis would increase net profit for the year by €65m (2005: €50m).

## Notes to the combined financial statements

For the year ended 31 December 2006

### 17 Financial instruments *continued*

#### **Credit risk**

Reed Elsevier seeks to limit interest rate and foreign exchange risks described above by the use of financial instruments and as a result has a credit risk from the potential non performance by the counterparties to these financial instruments, which are unsecured. The amount of this credit risk is normally restricted to the amounts of any hedge gain and not the principal amount being hedged. Reed Elsevier also has a credit exposure to counterparties for the full principal amount of cash and cash equivalents. Credit risks are controlled by monitoring the credit quality of these counterparties, principally licensed commercial banks and investment banks with strong long term credit ratings, and the amounts outstanding with each of them.

Reed Elsevier has treasury policies in place which do not allow concentrations of risk with individual counterparties and do not allow significant treasury exposures with counterparties which are rated lower than A by Standard and Poor's, Moody's or Fitch.

Reed Elsevier also has credit risk with respect to trade receivables due from its customers that include national and state governments, academic institutions, schools, and large and small enterprises including law firms, book stores and wholesalers. The concentration of credit risk from trade receivables is limited due to the large and broad customer base. Trade receivable exposures are managed locally in the business units where they arise. Where appropriate, business units seek to minimise this exposure by taking payment in advance and through management of credit terms. Allowance is made for bad and doubtful debts based on management's assessment of the risk taking into account the ageing profile, experience and circumstance.

The maximum exposure to credit risk is represented by the carrying amount of each financial asset, including derivative financial instruments, recorded in the balance sheet.

#### **Hedge accounting**

The hedging relationships that are designated under IAS39 – Financial Instruments are described below:

#### **Fair value hedges**

Reed Elsevier has entered into interest rate swaps and cross currency interest rate swaps to hedge the exposure to changes in the fair value of fixed rate borrowings due to interest rate and foreign currency movements which could affect the income statement.

Interest rate derivatives (including cross currency interest rate swaps) with a principal amount of €1,250m were in place at 31 December 2006 (2005: €1,393m) swapping fixed rate term debt issues denominated in US dollars (USD), euros and Swiss francs (CHF) to floating rate USD debt for the whole or part of their term.

## 17 Financial instruments continued

The gains and losses on the borrowings and related derivatives designated as fair value hedges, which are included in the income statement, for the two years ended 31 December 2006 were as follows:

Gains/(losses) on borrowings and related derivatives	1 January 2005 €m	Fair value movement gain/(loss) €m	Exchange gain/(loss) €m	1 January 2006 €m	Fair value movement gain/(loss) €m	Exchange gain/(loss) €m	31 December 2006 €m
USD debt	(7)	(13)	(1)	(21)	22	-	1
Related interest rate swaps	7	13	1	21	(22)	(1)	(2)
	-	-	-	-	-	(1)	(1)
Euro debt	(213)	90	(29)	(152)	(38)	17	(173)
Related Euro to USD cross currency interest rate swaps	214	(90)	30	154	38	(18)	174
	1	-	1	2	-	(1)	1
CHF debt	(121)	60	(17)	(78)	(15)	10	(83)
Related CHF to USD cross currency interest rate swaps	123	(60)	16	79	15	(9)	85
	2	-	(1)	1	-	1	2
Total USD, Euro and CHF debt	(341)	137	(47)	(251)	(31)	27	(255)
Total related interest rate derivatives	344	(137)	47	254	31	(28)	257
<b>Net gain</b>	<b>3</b>	<b>-</b>	<b>-</b>	<b>3</b>	<b>-</b>	<b>(1)</b>	<b>2</b>

All fair value hedges were highly effective throughout the two years ended 31 December 2006.

At 31 December 2006 there were fair value losses of nil (2005: €4m) included within borrowings which relate to debt de-designated from a fair value hedge relationship. During 2006, €4m (2005: €7m) of fair value losses recognised on adoption of IAS39 – Financial Instruments were included in finance income.

### Cash flow hedges

Reed Elsevier enters into two types of cash flow hedge:

- (1) Interest rate derivatives which fix the interest expense on a portion of forecast floating rate denominated debt (including commercial paper, short term bank loans and floating rate term debt).
- (2) Foreign exchange derivatives which fix the exchange rate on a portion of future foreign currency subscription revenues forecast by the Elsevier science and medical businesses for up to 50 months.

## Notes to the combined financial statements

For the year ended 31 December 2006

### 17 Financial instruments *continued*

Movements in the hedge reserve (pre-tax) in 2006 and 2005, including gains and losses on cash flow hedging instruments, were as follows:

	Transition loss €m	Interest rate hedges €m	Foreign exchange hedges €m	Total hedge reserve pre-tax €m
Hedge reserve at 1 January 2005: gains/(losses) deferred	(15)	(22)	95	58
Gains/(losses) arising in 2005	–	16	(31)	(15)
Amounts recognised in income statement	9	7	(44)	(28)
Exchange translation differences	(1)	(1)	(3)	(5)
Hedge reserve at 1 January 2006: gains/(losses) deferred	<b>(7)</b>	<b>–</b>	<b>17</b>	<b>10</b>
Gains arising in 2006	–	2	78	80
Amounts recognised in income statement	4	4	(20)	(12)
Exchange translation differences	–	–	–	–
<b>Hedge reserve at 31 December 2006: gains/(losses) deferred</b>	<b>(3)</b>	<b>6</b>	<b>75</b>	<b>78</b>

All cash flow hedges were highly effective throughout the two years ended 31 December 2006.

A deferred tax charge of €22m (2005: nil) in respect of the above gains and losses deferred in the hedge reserve at 31 December 2006 was also deferred in the hedge reserve.

Of the amounts recognised in the income statement in the year, gains of €20m (2005: €44m) were recognised in revenue, and losses of €8m (2005: €16m) were recognised in finance costs. A deferred tax charge of €4m (2005: nil) was recognised in relation to these items.

The transition loss relates to interest rate derivatives which were not designated as hedging instruments on adoption of IAS39 – Financial Instruments.

The deferred gains and losses on cash flow hedges at 31 December 2006 are currently expected to be recognised in the income statement in future years as follows:

	Transition loss €m	Interest rate hedges €m	Foreign exchange hedges €m	Total hedge reserve pre-tax €m
2007	(3)	5	40	42
2008	–	1	23	24
2009	–	–	11	11
2010	–	–	1	1
<b>Gains/(losses) deferred in hedge reserve at end of year</b>	<b>(3)</b>	<b>6</b>	<b>75</b>	<b>78</b>

The cash flows for these hedges are expected to occur in line with the recognition of the gains and losses in the income statement, other than in respect of certain forward foreign exchange hedges on subscriptions, where cash flows may be expected to occur in advance of the subscription year.

## 18 Deferred tax

	2006 €m	2005 €m
Deferred tax assets	253	388
Deferred tax liabilities	(1,266)	(1,431)
<b>Total</b>	<b>(1,013)</b>	<b>(1,043)</b>

Movements in deferred tax liabilities and assets are summarised as follows:

	Deferred tax liabilities				Deferred tax assets			Total €m
	Excess of tax allowances over amortisation €m	Acquired intangible assets €m	Pensions assets €m	Other temporary differences-liabilities €m	Tax losses carried forward €m	Pensions liabilities €m	Other temporary differences-assets €m	
Deferred tax asset/(liability) at 1 January 2005	(100)	(1,107)	-	(1)	83	154	103	(868)
(Charge)/credit to profit	(49)	95	-	(77)	(9)	12	(3)	(31)
(Charge)/credit to equity	-	-	-	-	-	15	(19)	(4)
Transfers	-	-	-	(7)	-	-	19	12
Acquisitions	-	(16)	-	(4)	-	-	4	(16)
Exchange translation differences	(19)	(139)	-	(7)	5	13	11	(136)
Deferred tax asset/(liability) at 1 January 2006	(168)	(1,167)	-	(96)	79	194	115	(1,043)
(Charge)/credit to profit	(40)	128	(6)	10	(69)	7	(5)	25
(Charge)/credit to equity	-	-	(9)	(26)	-	(57)	4	(88)
Transfers	(6)	7	6	(1)	4	3	(6)	7
Acquisitions	-	(16)	-	-	-	-	-	(16)
Exchange translation differences	16	92	-	10	(4)	(10)	(2)	102
<b>Deferred tax asset/(liability) at 31 December 2006</b>	<b>(198)</b>	<b>(956)</b>	<b>(9)</b>	<b>(103)</b>	<b>10</b>	<b>137</b>	<b>106</b>	<b>(1,013)</b>

At 31 December 2006, potential deferred tax assets not recognised due to uncertainties over availability and timing of relevant taxable income amounted to €288m (2005: €308m) in relation to tax deductions carried forward of €720m (2005: €769m). No time limitation currently applies on utilisation of the tax deductions.

## 19 Inventories and pre-publication costs

	2006 €m	2005 €m
Raw materials	24	18
Pre-publication costs	600	575
Finished goods	319	327
<b>Total</b>	<b>943</b>	<b>920</b>

## 20 Trade and other receivables

	2006 €m	2005 €m
Trade receivables	1,572	1,586
Prepayments and accrued income	252	220
Derivative financial instruments	326	292
<b>Total</b>	<b>2,150</b>	<b>2,098</b>

Trade receivables are predominantly non-interest bearing and their carrying amounts approximate to their fair value.

## Notes to the combined financial statements

For the year ended 31 December 2006

### 21 Trade and other payables

	2006 €m	2005 €m
Payables and accruals	1,424	1,434
Deferred income	1,444	1,429
Derivative financial instruments	14	30
<b>Total</b>	<b>2,882</b>	<b>2,893</b>

### 22 Borrowings

	2006			2005		
	Falling due within 1 year €m	Falling due in more than 1 year €m	Total €m	Falling due within 1 year €m	Falling due in more than 1 year €m	Total €m
Financial liabilities measured at amortised cost:						
Bank loans, overdrafts and commercial paper	855	–	855	782	–	782
Finance leases	9	9	18	16	6	22
Other loans	195	1,906	2,101	516	1,655	2,171
Other loans in fair value hedging relationships	313	1,192	1,505	–	1,644	1,644
<b>Total</b>	<b>1,372</b>	<b>3,107</b>	<b>4,479</b>	<b>1,314</b>	<b>3,305</b>	<b>4,619</b>

The total fair value of financial liabilities measured at amortised cost is €3,043m (2005: €3,059m). The total fair value of other loans in fair value hedging relationships is €1,599m (2005: €1,497m).

#### Analysis by year of repayment

	2006				2005			
	Bank loans, overdrafts and commercial paper €m	Other loans €m	Finance leases €m	Total €m	Bank loans, overdrafts and commercial paper €m	Other loans €m	Finance leases €m	Total €m
Within 1 year	855	508	9	1,372	782	516	16	1,314
Within 1 to 2 years	–	507	4	511	–	538	5	543
Within 2 to 3 years	–	–	3	3	–	524	–	524
Within 3 to 4 years	–	410	2	412	–	–	–	–
Within 4 to 5 years	–	420	–	420	–	444	1	445
After 5 years	–	1,761	–	1,761	–	1,793	–	1,793
	–	3,098	9	3,107	–	3,299	6	3,305
<b>Total</b>	<b>855</b>	<b>3,606</b>	<b>18</b>	<b>4,479</b>	<b>782</b>	<b>3,815</b>	<b>22</b>	<b>4,619</b>

#### Analysis by currency

	2006				2005			
	Bank loans, overdrafts and commercial paper €m	Other loans €m	Finance leases €m	Total €m	Bank loans, overdrafts and commercial paper €m	Other loans €m	Finance leases €m	Total €m
US Dollars	487	2,797	18	3,302	216	3,557	22	3,795
£ Sterling	30	596	–	626	–	–	–	–
Euro	268	213	–	481	456	258	–	714
Other currencies	70	–	–	70	110	–	–	110
<b>Total</b>	<b>855</b>	<b>3,606</b>	<b>18</b>	<b>4,479</b>	<b>782</b>	<b>3,815</b>	<b>22</b>	<b>4,619</b>

Included in the US dollar amounts for other loans above is €820m (2005: €856m) of debt denominated in euros (€500m) and Swiss francs (CHF 500m) that was swapped into US dollars on issuance and against which there are related derivative financial instruments included within trade and other receivables, which, as at 31 December 2006, had a fair value of €259m (2005: €233m).

## 23 Lease arrangements

### Finance leases

At 31 December 2006 future finance lease obligations fall due as follows:

	2006 €m	2005 €m
Within one year	9	16
In the second to fifth years inclusive	10	7
	19	23
Less future finance charges	(1)	(1)
<b>Total</b>	<b>18</b>	<b>22</b>
Present value of future finance lease obligations payable:		
Within one year	9	16
In the second to fifth years inclusive	9	6
<b>Total</b>	<b>18</b>	<b>22</b>

### Operating leases

Reed Elsevier leases various properties, principally offices and warehouses, which have varying terms and renewal rights that are typical to the territory in which they are located.

At 31 December 2006 outstanding commitments under non-cancellable operating leases fall due as follows:

	2006 €m	2005 €m
Within one year	171	165
In the second to fifth years inclusive	527	489
After five years	534	514
<b>Total</b>	<b>1,232</b>	<b>1,168</b>

Of the above outstanding commitments, €1,196m (2005: €1,143m) relate to land and buildings.

Reed Elsevier has a number of properties that are sub-leased. The future lease receivables contracted with sub-tenants fall as follows:

	2006 €m	2005 €m
Within one year	23	18
In the second to fifth years inclusive	70	57
After five years	31	30
<b>Total</b>	<b>124</b>	<b>105</b>

## 24 Provisions

	2006 €m	2005 €m
At start of year	64	73
Utilised	(16)	(19)
Exchange translation differences	(6)	10
<b>At end of year</b>	<b>42</b>	<b>64</b>

The provisions are for property lease obligations which relate to estimated sub-lease shortfalls and guarantees given in respect of certain property leases for various periods up to 2016.

## Notes to the combined financial statements

For the year ended 31 December 2006

### 25 Contingent liabilities and capital commitments

There are contingent liabilities amounting to €54m (2005: €67m) in respect of property lease guarantees.

At 31 December 2006, there were capital commitments of €259m in relation to acquisitions, conditional on regulatory and other approvals.

### 26 Combined share capitals

	2006 €m	2005 €m
At start of year	277	269
Issue of ordinary shares	3	2
Exchange translation differences	5	6
<b>At end of year</b>	<b>285</b>	<b>277</b>

Combined share capitals exclude the shares of Reed Elsevier NV held by a subsidiary of Reed Elsevier PLC.

### 27 Combined share premiums

	2006 €m	2005 €m
At start of year	2,635	2,545
Issue of ordinary shares, net of expenses	134	35
Exchange translation differences	31	55
<b>At end of year</b>	<b>2,800</b>	<b>2,635</b>

Combined share premiums exclude the share premium in respect of shares of Reed Elsevier NV held by a subsidiary of Reed Elsevier PLC.

### 28 Combined shares held in treasury

	Shares held by EBT €m	Shares held by parent companies €m	Total €m
At 1 January 2005	93	–	93
Purchase of shares	39	–	39
Exchange translation differences	4	–	4
At 1 January 2006	136	–	136
Purchase of shares	100	319	419
Exchange translation differences	4	3	7
<b>At 31 December 2006</b>	<b>240</b>	<b>322</b>	<b>562</b>

At 31 December 2006, shares held in treasury related to 17,167,145 (2005: 10,780,776) Reed Elsevier PLC ordinary shares and 9,242,214 (2005: 5,539,922) Reed Elsevier NV ordinary shares held by the Reed Elsevier Group plc Employee Benefit Trust (EBT); and 20,593,500 (2005: nil) Reed Elsevier PLC ordinary shares and 13,381,500 (2005: nil) Reed Elsevier NV ordinary shares held by the respective parent companies.

The EBT purchases Reed Elsevier PLC and Reed Elsevier NV shares which, at the trustees' discretion, can be used in respect of the exercise of share options and to meet commitments under conditional share awards.

## 29 Translation reserve

	2006 €m	2005 €m
At start of year	130	(175)
Exchange differences on translation of foreign operations	(300)	346
Other exchange translation differences	(31)	(41)
<b>At end of year</b>	<b>(201)</b>	<b>130</b>

## 30 Other combined reserves

	Hedge reserve 2006 €m	Other reserves 2006 €m	Total 2006 €m	Total 2005 €m
At start of year	10	(40)	(30)	(184)
Profit attributable to parent companies' shareholders	–	916	916	675
Dividends declared	–	(545)	(545)	(491)
Actuarial gains/(losses) on defined benefit pension schemes	–	204	204	(54)
Fair value movements on available for sale investments	–	4	4	4
Fair value movements on cash flow hedges	80	–	80	(15)
Tax recognised directly in equity	(26)	(62)	(88)	(4)
Increase in share based remuneration reserve	–	72	72	83
Transfers from hedge reserve to net profit (net of tax)	(8)	–	(8)	(28)
Exchange translation differences	(1)	3	2	(16)
<b>At end of year</b>	<b>55</b>	<b>552</b>	<b>607</b>	<b>(30)</b>

## 31 Related party transactions

Transactions between the Reed Elsevier combined businesses have been eliminated within the combined financial statements. Transactions with joint ventures were made on normal market terms of trading and comprise sales of goods and services of €9m (2005: €8m). As at 31 December 2006, amounts owed by joint ventures were €4m (2005: €4m). Key management personnel are also related parties and comprise the executive directors of Reed Elsevier PLC and Reed Elsevier NV. Transactions with key management personnel are set out below.

	2006 €m	2005 €m
Salaries and other short term employee benefits	10	10
Post employment benefits	2	1
Share based remuneration	10	15
<b>Total</b>	<b>22</b>	<b>26</b>

Post employment benefits represent the service cost under IAS19 – Employee Benefits in relation to defined benefit schemes, together with any contributions made to defined contribution schemes. Share based remuneration is the amount charged in respect of executive directors under IFRS2 – Share Based Payment.

## 32 Exchange rates

The following exchange rates have been applied in preparing these combined financial statements presented in euros:

	Income statement		Balance sheet	
	2006	2005	2006	2005
Sterling to euro	0.68	0.68	0.67	0.68
US dollar to euro	1.25	1.25	1.32	1.18

## Notes to the combined financial statements

For the year ended 31 December 2006

### 33 Post balance sheet event

On 14 February 2007, Reed Elsevier approved a plan to sell the Harcourt Education division and to return the net proceeds to shareholders by way of a special distribution in the equalisation ratio. It is expected that the sale will be completed during 2007.

### 34 Approval of financial statements

The combined financial statements were approved and authorised for issue by the boards of directors of Reed Elsevier PLC and Reed Elsevier NV on 14 February 2007. The supplemental combined financial statements presented in euros were approved for publication on the Reed Elsevier website, [www.reedelsevier.com](http://www.reedelsevier.com), on 22 March 2007.

## Independent auditors' report to the members of Reed Elsevier PLC and shareholders of Reed Elsevier NV

### Report on the combined financial statements presented in euros

We have audited the combined financial statements presented in euros of Reed Elsevier PLC (registered in England and Wales), Reed Elsevier NV (registered in Amsterdam), Reed Elsevier Group plc (registered in England and Wales), Elsevier Reed Finance BV (registered in Amsterdam) and their respective subsidiaries, associates and joint ventures (together "the combined businesses"), for the year ended 31 December 2006 ("the combined financial statements presented in euros"), which comprise the combined income statement, the combined cash flow statement, the combined balance sheet, the combined statement of recognised income and expenses, the combined shareholders' equity reconciliation, the accounting policies and the related notes 1 to 34 and have been prepared on the basis set out in the accounting policies. As set out in the accounting policies, the combined financial statements presented in euros are supplementary to the combined financial statements dated 14 February 2007 included in the Reed Elsevier Annual Reports and Financial Statements 2006.

Our audit work has been undertaken so that we might state to the members of Reed Elsevier PLC and shareholders of Reed Elsevier NV those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than Reed Elsevier PLC and Reed Elsevier NV, and the members of Reed Elsevier PLC as a body and the shareholders of Reed Elsevier NV as a body, for our audit work, for this report, or for the opinions we have formed.

### Directors' responsibility

The directors are responsible for the preparation and fair presentation of the combined financial statements presented in euros in accordance with International Financial Reporting Standards as adopted by the European Union. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of the combined financial statements presented in euros that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the given circumstances.

### Auditors' responsibility

Our responsibility is to express an opinion on the combined financial statements presented in euros, based on our audit. We conducted our audit in accordance with relevant legal and regulatory requirements, International Standards on Auditing (UK and Ireland) issued by the United Kingdom Auditing Practices Board and Dutch Law. This requires that we comply with our respective professions' ethical requirements and plan and perform the audit to obtain reasonable assurance whether the combined financial statements presented in euros are free from material misstatement.

We also read other information contained in this document, as described in the contents section, including the operating and financial review presented in euros, and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the combined financial statements presented in euros.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the combined financial statements presented in euros. The procedures selected depend on our judgement, including the assessment of the risks of material misstatement of the combined financial statements presented in euros, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the combined businesses' preparation and fair presentation of the combined financial statements presented in euros in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the combined businesses' internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the combined financial statements presented in euros.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### Opinion

In our opinion, the combined financial statements presented in euros give a true and fair view of the financial position of the combined businesses as at 31 December 2006, and of their profits and cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

**Deloitte & Touche LLP**  
Chartered Accountants  
and Registered Auditors  
London  
United Kingdom  
22 March 2007

**Deloitte Accountants B.V.**  
J P M Hopmans  
Amsterdam  
The Netherlands  
22 March 2007

## Directors' remuneration report

This report provides Reed Elsevier's statement of how it has applied the principles of good governance relating to Directors' remuneration and communicates its policies and practices on executive remuneration to shareholders. It has been prepared by the Remuneration Committee (the "Committee") of Reed Elsevier Group plc and approved by the boards of Reed Elsevier Group plc, Reed Elsevier PLC and Reed Elsevier NV.

In accordance with the UK Directors' Remuneration Report Regulations 2002 (the UK Regulations) and the Dutch Corporate Governance Code issued in December 2003 (the Dutch Code), resolutions will be submitted to the respective Annual General Meetings of Reed Elsevier PLC and Reed Elsevier NV to approve this report and the remuneration policy as set out below.

### Membership of the Remuneration Committee

Throughout 2006, the Committee consisted wholly of independent non-executive directors: Rolf Stomberg ("Chairman"), Mark Elliott, Cees van Lede and, with effect from 24 July 2006, the Chairman of Reed Elsevier, Jan Hommen, whose appointment is in line with the revision to the Combined Code. At the invitation of the Chairman, the Chief Executive Officer attends the meetings of the Committee except when his own remuneration is under consideration.

### The contents of this report

For greater clarity, the main body of this report (Sections A and B) is focused on pay policy and practice for executive directors (pages 62 to 69) and non-executive directors (pages 69 and 70). Section C (pages 70 to 79 forming part of this report) deals with the auditable disclosures and other regulatory requirements. The framework of the report is as follows:

#### Section A Executive directors

- a. Remuneration policy and objectives
- b. Remuneration in practice
- c. 2006 payments
- d. 2006 awards
- e. Shareholding requirement
- f. Service contracts
- g. Policy on external appointments

#### Section B Non-executive directors

- a. Policy
- b. Fee levels

#### Section C Statutory disclosures

### A. Executive directors

#### (a) Remuneration policy and objectives

Our remuneration policy has been designed to meet the needs of a group of global business divisions, each of which operates internationally by line of business. In order to support this business structure, it is essential to have a remuneration policy which:

- aids the attraction and retention of the best executive talent from anywhere in the world; and
- underpins Reed Elsevier's demanding performance standards.

The challenges and demands created by the need for global market competitiveness as well as for internal consistency have led the Committee to apply a common and consistent set of standards to the design and operation of its incentive plans, including the level of incentive opportunity.

The Committee believes that in order to meet its remuneration objectives, the remuneration of executive directors should comprise a balance between fixed and variable (performance-related) pay elements with the greater proportion of potential reward being linked to performance. For superior performance, some 60% of each director's total target remuneration is performance-related.

The Committee regularly reviews remuneration policy to ensure that it is sufficiently flexible to take account both of future changes in Reed Elsevier's business operations and environment and of key developments in remuneration practice. Consequently, the policy set out in this report has applied during 2006 and will apply in 2007 subject to any necessary changes. Any changes will be described in full in future reports.

#### Remuneration objectives

The principal objectives of the policy are to attract and motivate executives of the highest calibre and experience, who are capable of shaping and executing strategy and delivering shareholder value in a competitive and increasingly global employment market. The Committee believes that this requires the following:

- A pay and benefits package which is competitive with packages offered by other leading multinational companies operating in global markets, i.e. one which provides upper quartile total remuneration for the sustained delivery of superior levels of performance.
- A reward structure that links individual performance, company performance and parent company share price performance so as to align the interests of the directors with those of the group as a whole and its shareholders.
- An approach to performance management that stimulates enhanced performance by directors, recognises their individual contribution to the attainment of our short- and longer-term results and also encourages the teamwork which is essential to achieve the long term strategic objectives.

Base salary and the Annual Incentive Plan (AIP) aim to position the executive within the relevant market for executive talent and to provide a focus on the delivery of our shorter term strategic objectives.

The Executive Share Option Scheme (ESOS) and Long Term Incentive Scheme (LTIS) encourage a focus on longer term earnings growth and total shareholder return and increase executives' alignment with shareholders' interests.

The Committee believes that the main driver of long term shareholder value is sustained growth in profitability. In relation to shareholders, the primary measure of profitability is growth in adjusted earnings per share which is supported, at an operational level, by the measures of revenue growth, profitability, cash generation and return on invested capital. In addition, recognising shareholders' preference for longer term incentive arrangements to include a performance measure based on shareholder return, a further measure of total shareholder return relative to a focused peer group applies to awards made under the LTIS from 2006. These measures are integrated into our reward structure. In all cases, payments are made against a sliding scale of performance achievement, since this is the most direct way to link pay with performance.

#### (b) Remuneration in practice

The Committee's practice is to review the market competitiveness of base salary on the following basis:

- UK-based directors against FTSE 50 companies (excluding financial services); and
- US-based directors (or directors on US-market based reward packages) against US Media Industry companies.

Benefits, including medical and retirement benefits, are positioned to reflect local country practice. UK directors are eligible to participate in the all-employee SAYE (savings related) share option scheme.

Recognising the more global approach to the design of its incentive plans, referred to earlier, the annual and longer term incentive plans for executive directors are operated with common incentive opportunity levels, irrespective of geographical location.

In relation to long term incentives, the performance measures are tested once at the end of the specific performance period and are not subsequently re-tested.

This overall approach is set out in greater detail below with reference to the individual elements of the reward package for executive directors:

#### Base salary

- Salaries are reviewed annually to take account of two factors: firstly, market movement and individual performance during the previous year; secondly, the increased and sustainable contribution of the individual to the group which may position the individual at a higher

value relative to the market. The review of an individual salary does not automatically result in an increase to that salary.

#### Annual Incentive Plan (AIP)

- Based on achievement of financial performance targets set against the critical measures of revenue growth, profit, cash generation and key performance objectives (KPOs).
- Directors have a target bonus opportunity of 90% of salary, which is payable for the achievement of highly stretching financial targets, (which align with the annual budget and the parent companies' minimum 10% constant currency adjusted EPS objective), and for outstanding performance against KPOs. For 2007, a maximum of 150% of salary could be paid for exceptional performance (for 2006 this was 110%). All targets are approved by the Committee at the beginning of the year.
- The target 90% bonus opportunity is allocated as follows, as a percentage of salary:
 

– Revenue	27%
– Profit	27%
– Cash Flow Conversion Rate	9%
– KPOs	27%

The four elements are measured separately, such that there could be a pay-out on one element and not on others.

- For 2007, payment against each financial performance measure will only commence if a threshold of 97.5% of the target is achieved (for 2006 this was 94%).
- Each director is typically set around six KPOs. These represent critical, non-financial priorities, for which they are accountable. Against each objective, a number of measurable "milestone targets" are defined. These must be achieved during the annual performance period for the KPO payout to be made.

#### Bonus Investment Plan (BIP)

- Designed to encourage increased personal shareholding by the participant.
- Directors and other designated key senior executives may invest up to half of any payment they receive under the AIP in shares of Reed Elsevier PLC or Reed Elsevier NV.
- Subject to continued employment, and to their retaining these investment shares during a three-year performance period, they will be awarded an equivalent number of matching shares.
- The award of matching shares is dependent on the achievement of a performance condition. In 2006, this was the achievement of at least 6% per annum compound growth in the average of Reed Elsevier PLC and Reed Elsevier NV adjusted EPS – measured at constant exchange rates over the three year vesting period.

## Directors' remuneration report continued

### Executive Share Options (ESOS)

- Annual grants of options are made over shares in Reed Elsevier PLC and Reed Elsevier NV at the market price at date of grant.
- The level of option grant and the performance conditions are determined and reviewed by the Committee annually.
- The standard performance condition, which governs the size of grant for all participants, relates to the compound annual growth in adjusted EPS (at constant currencies) over the three years prior to grant. The Target Grant Pool for all participants is defined with reference to share usage during the base year of 2003, as follows:

Adjusted EPS Growth (constant currencies) per annum	Target Grant Pool (as a % of 2003 Grant)
Less than 6%	50%
6% or more	75%
8% or more	100%
10% or more	125%
12% or more	150%

- The awards made to executive directors are subject to an annual maximum of three times base salary. The awards are subject to the following three performance criteria:
  - On grant
    - corporate performance as measured by adjusted EPS growth in accordance with the criteria above, and
    - individual performance over the three year period prior to grant;
  - On vesting
    - a further performance condition such that the compound growth in adjusted EPS (at constant currency) during the three years following grant must be at least 6% per annum. There is no retesting of the performance condition.
- The combination of the tests on grant and vesting requires sustained high level profit growth over a continuous six year period in respect of each individual grant to executive directors.
- Options are normally exercisable between three and ten years from the date of grant.

### Long term Incentive (LTIS)

In line with its previous commitment to shareholders the Committee reviewed the operation of the LTIS in 2006 and shareholders approved changes to its operation which apply to awards made from 2006.

- All executive directors will be eligible to receive an annual grant of performance shares with a target value of around 135% of salary. (Lower levels of grant will apply to other senior executives invited to participate in the LTIS).
- Awards consist solely of performance shares.
- In addition to achieving a demanding EPS performance target over a three year performance period, an additional TSR performance target over the same three year period is also applied.

The minimum level of compound adjusted EPS growth (at constant currencies) will continue to be 8% per annum, with maximum vesting (under the EPS measure) being achieved for growth of 12% per annum. Any award earned through EPS performance may then be increased in line with Reed Elsevier's TSR performance against a comparator group over the three year period. No increase will be applied for TSR performance which is below median, and the maximum increase will be applied at upper quartile of TSR achievement. No award will be made to participants if Reed Elsevier fails to achieve the minimum threshold of 8% per annum adjusted EPS growth (at constant currencies), irrespective of the associated TSR performance.

The effect of the combination of these two measures is shown in the following table, which sets out the potential payment as a percentage of the initial target award:

Adjusted EPS Growth (constant currencies) per annum	LTIS Performance Schedule			
	TSR Ranking			
	Below median	Median	62.5 percentile	Upper quartile
Below 8%	0%	0%	0%	0%
8%	28%	35%	42%	49%
10%	80%	100%	120%	140%
12% and over	108%	135%	162%	189%

For executive directors, the target award of 135% of salary could therefore be increased to a maximum of around 255% of salary (135% x 189%). Any shares which vest will be treated as attracting dividends during the performance period. This could increase the maximum to around 270% of salary depending on dividend payments.

The Committee considers this performance condition to be tougher than normal UK practice because the TSR element can improve the reward to participants if, but only if, the adjusted EPS test has first been achieved.

→ Reed Elsevier's TSR will be tested against a selected international group of competitor companies over a three year period. For awards made in 2007, these companies will be as follows:

The Thomson Corporation	United Business Media
McGraw Hill	Fair Isaac
Reuters Group	John Wiley & Sons
Pearson	DMGT
Wolters Kluwer	Lagardere
ChoicePoint	Dun & Bradstreet
EMAP	WPP
Informa	Taylor Nelson
Dow Jones	

Note: VNU became a private company during 2006 and has been removed from the peer group.

The TSR of Reed Elsevier and each of the comparator companies will be calculated in the currency of its primary listing, which the Committee considers to be the fairest test of management's relative performance. Reed Elsevier's TSR will be taken as a simple average of the TSR of Reed Elsevier PLC and Reed Elsevier NV.

→ The Committee continues to have full discretion to reduce or cancel awards granted to participants based on its assessment as to whether the EPS and TSR performance fairly reflects the progress of the business having regard to underlying revenue growth, cash generation, return on capital and any significant changes in inflation as well as individual performance.

### Retirement benefits

→ The Committee reviews retirement benefit provision in the context of the total remuneration package for each director, bearing in mind their age and service and against the background of evolving legislation and practice in the group's major countries of operation.

→ Base salary is the only pensionable element of remuneration.

→ The three UK-based executive directors are provided with conventional UK defined benefit pension arrangements targeting two thirds (Sir Crispin Davis 45%) of salary at a normal retirement age of 60. The targeted pension is provided through a combination of:

- the main UK Reed Elsevier Pension Scheme for salary restricted to a cap, determined annually on the same basis as the pre-April 2006 Inland Revenue earnings cap, and
- Reed Elsevier's unfunded unapproved pension arrangement for salary above the cap.

→ P. Tierney and A. Prozes are covered by a mix of defined benefit and defined contribution arrangements. In accordance with US legislation, these directors have no defined retirement age. Reed Elsevier pays an annual contribution of 19.5% of salary to E. Engstrom's personal pension plan.

→ These arrangements are set out in further detail on page 72.

### (c) 2006 payments

In this section, we set out the base annual salary paid to executive directors during 2006, the annual incentive payment made in respect of 2006, and any gains which they have made during 2006 under any of the long term incentive plans.

#### (i) Base salary for 2006

The annual salary increases made to executive directors with effect from 1 January 2006 were consistent with US and UK norms, respectively, for increases paid to senior executives during 2006. The increases to US-based executives were in a range from 3% to 7%; the increases to UK-based executives were in a range from 4% to 6%, except in the case of Mr. van de Aast, who was given an increase to align him more appropriately to the global market within which he operates, rather than to the UK market, which accounts for less than 20% of his business.

Because of the many countries in which we operate, there is no practical basis on which to compare directors' pay increases with those of other employees. However, the same factors, in terms of market, personal contribution and performance determine the level of increase across all employee populations globally.

## Directors' remuneration report continued

	Annual Salary 2006	Annual Salary 2005
G J A van de Aast	£526,500	£430,000
M H Armour	£561,750	£535,000
Sir Crispin Davis	£1,081,600	£1,040,000
E Engstrom	\$1,092,000	\$1,040,000
A Prozes	\$1,112,800	\$1,040,000
P Tierney	\$1,071,200	\$1,040,000

### (ii) Annual Incentive Plan Payments for 2006

In assessing the level of bonus payments for 2006, the Committee noted the following performances.

Measure	Percentage change over 2005 at constant exchange rates				
	Elsevier	LexisNexis	Harcourt	Reed Business	Reed Elsevier
Revenue	+8%	+8%	0%	+5%	+6%
Adjusted operating profit	+10%	+13%	-19%	+14%	+9%

	Payments made for 2006 (paid in March 2007)	% of salary
G J A van de Aast	£538,862	102.35%
M H Armour	£488,790	87.01%
Sir Crispin Davis	£919,360	85.00%
E Engstrom	\$996,068	91.22%
A Prozes	\$1,052,998	94.63%
P Tierney	\$391,631	36.56%

The 2006 financial results were encouraging, with 6% revenue growth (at constant currencies), improved underlying margins, and adjusted operating profits up 9% (at constant currencies). We have also delivered strong cash generation and higher returns on invested capital. Organic revenue growth was 5%, with good growth in Elsevier, LexisNexis and Reed Business and flat revenues in Harcourt Education in a weaker market. Organic adjusted operating profit growth was 8% with underlying margin improvement in Elsevier, LexisNexis and Reed Business. The revenue growth benefits from a 10% increase in digital revenues representing the payback on the continuing investment in new electronic product, innovative marketing and expanded sales coverage. The 0.7 percentage point improvement in underlying margin reflects the revenue growth and the continuing focus on cost across the business. The quality of the earnings is underpinned by our strong cash flow in 2006, with 95% of adjusted operating profits converting into cash.

In addition, the directors were generally assessed as having delivered a strong performance against their KPOs, resulting in positive business momentum and an overall promising business outlook going into 2007.

### (iii) Gains made under Long term Incentive Plans during 2006

#### ESOS

The following gains were made by executive directors in relation to share options over ordinary shares in Reed Elsevier PLC (PLC) and Reed Elsevier NV (NV) exercised during 2006:

	No. of options exercised	Share type	Option price	Market price	Gain
Gerard van de Aast	81,728	PLC	451.50p	565.00p	£92,761
	58,191	NV	€9.34	€12.11	€161,189
Pat Tierney	25,000	PLC	451.50p	559.00p	£26,875
	16,000	NV	€9.34	€12.90	€56,960

**BIP**

The first cycle under the Bonus Investment Plan (BIP) was launched in 2003 and therefore the first matching shares vested to participants in 2006.

Accordingly, the following numbers of shares were transferred under the terms of the BIP, to the following executive directors.

	No. of matching shares vested	Share type	Market price on date of vesting	Value
Mark Armour	11,327	PLC	545.50p	£61,789
	8,030	NV	€11.70	€93,951
Sir Crispin Davis	22,731	PLC	545.50p	£123,998
	16,115	NV	€11.70	€188,546
Andrew Prozes	20,040	PLC	545.50p	£109,318
	14,552	NV	€11.70	€170,258
Gerard van de Aast	12,057	NV	€11.70	€141,067

**LTIS**

- The 2004–2006 cycle of the LTIS will be tested as at the vesting date of 2 March 2007 and the first awards under this plan will be made in March 2007.
- For the performance period 2004–06, awards to executive directors under the LTIS were made in February 2004 in respect of 5.5 times salary in conventional market price options and 2.5 times salary in performance shares.
- The performance condition governing the vesting of those awards was as follows:
  - at 8% compound annual growth in adjusted EPS (at constant currency), 25% of the awards vest;
  - at 10% growth, 100% vest;
  - at 12% growth, 125% of the awards vest.
 Awards vest on a straight line basis between each of these points. There is no provision for retesting of the performance condition.

The Committee assessed both the earnings growth and the quality of earnings in order to determine whether the performance condition had been achieved. Reed Elsevier's performance throughout the 2004–06 performance period continued to show good revenue growth, continuous margin improvement, strong cash generation and growing returns on capital. On average over the period, Reed Elsevier succeeded in delivering against its targeted adjusted earnings per share growth of a minimum of 10% at constant currencies. Increasing profitability and capital discipline drove the post tax return on capital employed to 9.8% in 2006, which was 0.4 percentage points ahead of 2005. This was the fifth successive year of growth in returns. Acquisitions have continued to accelerate the strategy in e-health, legal solutions, risk management and business online, and are on track to deliver a return on capital in excess of Reed Elsevier's weighted average cost of capital within three years, with good growth in returns expected thereafter. The Remuneration Committee therefore considers that the adjusted EPS growth achieved is a fair reflection of the progress of the business and has approved that the average compound annual growth rate in adjusted EPS at constant exchange rates over the 2004–06 performance period is 10.17%, which means that 102.125% of the target awards will vest.

## Directors' remuneration report continued

Accordingly, the following numbers of options will become exercisable and the following numbers of shares will be transferred on reaching the vesting date, under the terms of the 2004-06 LTIS, to the following executive directors:

	Share Type	No. of Shares	No. of Share Options	Option Price
G J A van de Aast	PLC	106,342	233,955	487.25p
	NV	73,023	160,651	€10.57
M H Armour	PLC	132,036	290,481	487.25p
	NV	90,666	199,467	€10.57
Sir Crispin Davis	PLC	259,825	571,616	487.25p
	NV	178,416	392,516	€10.57
E Engstrom	PLC	147,801	325,163	478.00p
	NV	102,165	224,766	€10.30
A Prozes	PLC	138,435	304,558	487.25p
	NV	95,061	209,133	€10.57
P Tierney	PLC	89,982	197,962	487.25p
	NV	61,789	135,936	€10.57

During 2006, Mr Engstrom received shares to the value of €648,226 on the vesting of restricted shares awarded to him in 2004 as part of his initial recruitment arrangements, which were set out in the Annual Reports and Financial Statements 2004.

### (d) 2006 awards

In this section, we set out the new awards made to executive directors during 2006 under the terms of our long term incentive plans.

LTIS awards, ESOS grants made in the year and executive directors' elections under the Bonus Investment Plan (BIP) are shown in the following table.

	Share Type	LTIS Awards No. of Shares	ESOS Share Options		BIP Matching Shares
			No. of Shares	Option Price	No. of shares
G J A van de Aast	PLC	70,364	127,662	530.50p	18,633
	NV	46,332	85,775	€11.47	12,311
M H Armour	PLC	75,075	158,836	530.50p	21,653
	NV	49,434	106,720	€11.47	14,306
Sir Crispin Davis	PLC	144,550	305,824	530.50p	42,092
	NV	95,181	205,480	€11.47	27,810
E Engstrom	PLC	82,092	178,895	530.50p	–
	NV	54,055	120,198	€11.47	29,442
A Prozes	PLC	83,656	182,303	530.50p	26,400
	NV	55,085	122,487	€11.47	17,636
P Tierney	PLC	80,528	175,488	530.50p	8,124
	NV	53,025	117,908	€11.47	5,426

### (e) Shareholding requirement

Participants in the LTIS are required to build up a significant personal shareholding in Reed Elsevier PLC and/or Reed Elsevier NV. Following shareholders' approval of the revised terms of the LTIS in 2006, the shareholding requirement for the Chief Executive Officer is now three times salary (previously 1.5 times salary) and for other executive directors is two times salary (previously 1.5 times salary). These increased shareholding requirements must be met by February 2009 at the latest.

Details of directors' shareholdings, as at 31 December 2006, are set out on page 79.

**(f) Service contracts**

Executive directors are employed under service contracts which generally provide for one year's notice and neither specify a pre-determined level of severance payment nor contain specific provisions in respect of change in control.

The service contracts for executive directors (and for approximately 130 other senior executives) contain the following provisions:

- covenants which prevent them from working with specified competitors, recruiting Reed Elsevier employees and soliciting Reed Elsevier customers for a period of 12 months after leaving employment;
- in the event of their resigning, they will immediately lose all rights to any outstanding awards under the LTIS, ESOS and BIP granted from 2004 onwards, including any vested but unexercised options; and
- in the event that they were to join a specified competitor within 12 months of termination, any gains made in the six months prior to termination on the exercise or vesting of an LTIS, ESOS and BIP award made from 2004 onwards shall be repayable.

**(g) Policy on external appointments**

The Committee believes that the experience gained by allowing executive directors to serve as non-executive directors on the boards of other organisations is of benefit to Reed Elsevier. Accordingly, executive directors may, subject to the approval of the Chairman and the Chief Executive Officer, serve as non-executive directors on the boards of up to two non-associated companies (of which only one may be to the board of a major company) and they may retain remuneration arising from such appointments.

- Sir Crispin Davis is a non-executive director of GlaxoSmithKline plc and received a fee of £70,000 (€102,900) during 2006.
- Erik Engstrom was a non-executive director of Eniro AB (until 5 April 2006) and received a fee of SEK75,000 (€8,125) during 2006.
- Andrew Prozes is a non-executive director of the Cott Corporation and received a fee of \$56,000 (€44,739) during 2006.
- Gerard van de Aast is a non-executive director of OCE NV (since 1 May 2006) and received a fee of €23,342 during 2006.

**B. Non-executive directors****(a) Policy**

Reed Elsevier seeks to recruit non-executive directors with the experience to contribute to the board of a dual-listed global business and with a balance of personal skills which will make a major contribution to the boards and their committee structures.

With the exception of G J de Boer-Kruyt, who serves only on the supervisory board of Reed Elsevier NV, non-executive directors, including the Chairman, are appointed to the boards of Reed Elsevier Group plc, Reed Elsevier PLC and the supervisory board of Reed Elsevier NV.

Non-executive directors' remuneration is determined by the three boards as appropriate to the director concerned. The primary source for comparative market data is the practice of FTSE50 companies, although reference is also made to AEX companies.

Non-executive directors, including the Chairman, serve under letters of appointment, do not have contracts of service and are not entitled to notice of, or payments following, termination.

In 2005 the Reed Elsevier Group plc board introduced a charity donation matching programme for non-executive directors. Under the policy, where a non-executive director donates all or part of their fees to a registered charity, the Company may, at its sole discretion, make a matching donation to any charity, provided the charity's objectives are judged to be appropriate and are not political or religious in nature. Messrs Reid, Zelnick and van Lede each donated a proportion of their fees in respect of 2006 to charity and, in accordance with the programme, the Company made matching charitable donations of €33,075, €61,836 and €30,000, respectively.

## Directors' remuneration report continued

### (b) Fee levels

Non-executive directors receive one annual fee in respect of their memberships of the boards of Reed Elsevier PLC, Reed Elsevier NV and Reed Elsevier Group plc. The fee paid to G J de Boer-Kruyt, who serves only on the supervisory board of Reed Elsevier NV, reflects her time commitment to that company and to other companies within the Reed Elsevier combined businesses. Non-executive directors are reimbursed for expenses incurred in attending meetings. They do not receive any performance related bonuses, pension provisions, share options or other forms of benefit. Fees may be reviewed annually, although in practice they have changed on a less frequent basis and were last reviewed with effect from 1 May 2003. The fee for Mrs de Boer-Kruyt was last reviewed with effect from 1 January 2004.

Annual fee rates applicable to non-executive directors and to the Chairman are set out in the following table:

	Annual fee 2006	Annual fee 2005
Chairman	€350,000	€350,000
Non-executive directors	£45,000/€65,000	£45,000/€65,000
Chairman of:		
– Audit Committee	£7,000/€12,000	£7,000/€12,000
– Remuneration Committee	£7,000/€12,000	£7,000/€12,000

### C. Statutory disclosures

#### (a) Report authorship

This report has been prepared by the Remuneration Committee of Reed Elsevier Group plc. It has been prepared in accordance with the UK Regulations and the Dutch Code issued in December 2003 in order to meet the requirements of the UK Combined Code of Corporate Governance issued in July 2003, the Dutch Code and the Netherlands Civil code.

#### (b) Remuneration committee constitution and terms of reference

The Committee is responsible for:

- recommending to the boards the remuneration (in all its forms) of the Chairman and the executive directors, including terms of service contracts and all other terms and conditions of employment;
- providing advice to the Board and to the Chief Executive Officer on major policy issues affecting the remuneration of executives at a senior level below the board; and
- the operation of all share-based plans.

A copy of the Terms of Reference of the Committee can be found on the Reed Elsevier website [www.reedelsevier.com](http://www.reedelsevier.com).

The Remuneration Committee met six times during the year. Mr van Lede was unable to attend one meeting, otherwise there was full attendance.

#### (c) Advisors

The Committee has appointed Towers Perrin, an external consultancy which has wide experience of executive remuneration in multinational companies, to advise in developing its performance-related remuneration policy. Towers Perrin also provide actuarial and other Human Resources consultancy services directly to some Reed Elsevier companies.

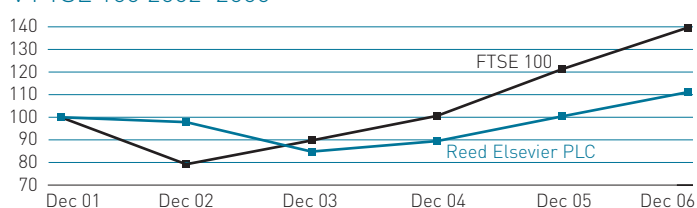
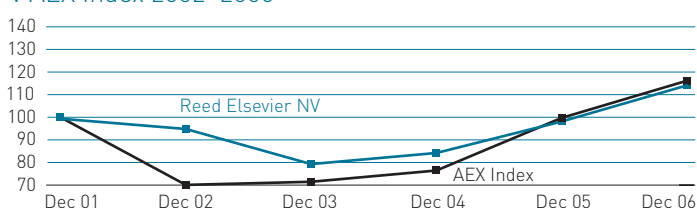
The following individuals also provided material advice or services to the Committee during the year:

- Sir Crispin Davis (Chief Executive Officer);
- Ian Fraser (Group HR Director); and
- Philip Wills (Director, Compensation and Benefits).

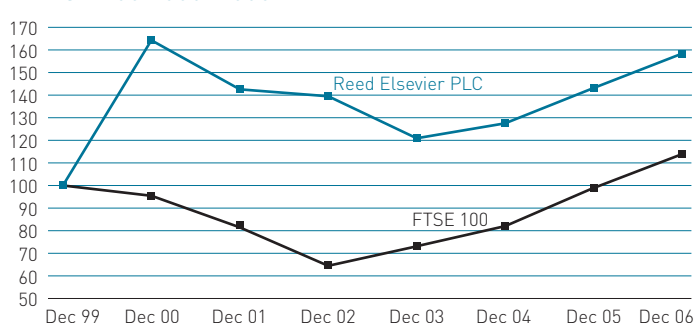
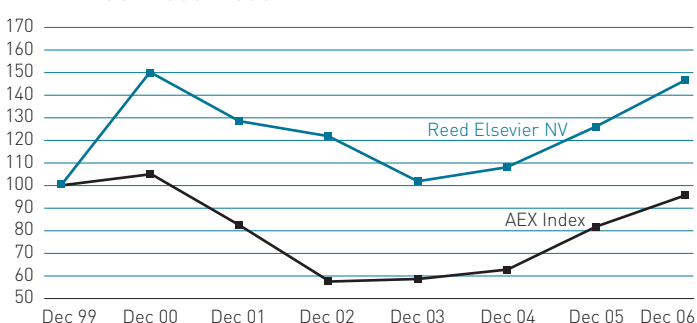
**(d) Total Shareholder Return (TSR)**

As required by the Directors' Remuneration Report Regulations 2002, the following graphs show the Reed Elsevier PLC and Reed Elsevier NV total shareholder return performance, assuming dividends were reinvested. They compare the Reed Elsevier PLC performance with that achieved by the FTSE 100, and the Reed Elsevier NV performance with the performance achieved by the Euronext Amsterdam (AEX) Index, over the five year period from 2002–2006.

For the five year period since 1 January 2002, the TSR for Reed Elsevier PLC was 11%, against a FTSE 100 return of 39%. For Reed Elsevier NV during the same period, TSR was 14%, against an AEX Index return of 16%. As Reed Elsevier PLC and Reed Elsevier NV are members of the FTSE 100 and AEX Index respectively, the Committee considers these indices to be appropriate for comparison purposes.

**Reed Elsevier PLC total shareholder return  
v FTSE 100 2002–2006**

**Reed Elsevier NV total shareholder return  
v AEX Index 2002–2006**


For the seven year period since 1 January 2000, being the period since Reed Elsevier set out its investment led growth strategy, the TSR for Reed Elsevier PLC was 58%, significantly outperforming the FTSE 100 which showed a return of 14%. For Reed Elsevier NV, in the same seven year period TSR was 47%, also significantly outperforming the AEX Index which showed a negative return of 4%.

**Reed Elsevier PLC total shareholder return  
v FTSE 100 2000–2006**

**Reed Elsevier NV total shareholder return  
v AEX Index 2000–2006**


The total shareholder return set out above is calculated on the basis of the average share price in the 30 trading days prior to the respective year ends and on the assumption that dividends were reinvested.

**(e) Service contracts**

Each of the executive directors has a service contract, as summarised below:

	Contract Date	Expiry date (subject to notice period)	Notice period	Subject to:
G J A van de Aast <sup>(i)</sup>	15 November 2000	17 July 2017	12 months	English law
M H Armour <sup>(i)</sup>	7 October 1996	29 July 2014	12 months	English law
Sir Crispin Davis <sup>(i)</sup>	19 July 1999	19 March 2009	12 months	English law
E Engstrom <sup>(i)</sup>	25 June 2004	14 June 2025	12 months	English law
A Prozes <sup>(ii)</sup>	5 July 2000	Indefinite	12 months base salary payable for termination without cause	New York law
P Tierney <sup>(ii)</sup>	19 November 2002	Indefinite	12 months base salary payable for termination without cause	New York law

(i) Employed by Reed Elsevier Group plc

(ii) Employed by Reed Elsevier Inc

## Directors' remuneration report continued

The Committee believes that, as a general rule, notice periods should be twelve months and that the executive directors should, subject to practice within their base country, be required to mitigate their damages in the event of termination. The Committee will, however, note local market conditions so as to ensure that the terms offered are appropriate to attract and retain top executives operating in global businesses.

No loans, advances or guarantees have been provided for the benefit of any director.

### (f) Auditable disclosures

#### (i) Pensions in more detail

The target pension for Sir Crispin Davis at normal retirement age of 60 is 45% of base salary in the 12 months prior to retirement. Other executive directors based in the UK are provided with pension benefits at a normal retirement age of 60, equivalent to two thirds of base salary in the 12 months prior to retirement, provided they have completed 20 years' service with Reed Elsevier or at an accrual rate of 1/30th of pensionable salary per annum if employment is for less than 20 years.

The target pension for A Prozes, a US-based director, after completion of seven years' pensionable service is US\$300,000 per annum. In the event that Mr Prozes completes more than seven years pensionable service, the pension payable will be increased on a pro rata basis by US\$42,857 per annum. The pension will be reduced in amount by the value of any other retirement benefits payable by Reed Elsevier or which become payable by any former employer, other than those attributable to employee contributions. The target pension for P Tierney, a US-based director, after completion of five years' pensionable service is US\$440,000 per annum, inclusive of any other retirement benefits payable by Reed Elsevier or any former employer, other than those attributable to employee contributions. In the event of termination of employment before completion of five years' pensionable service, the pension payable will be reduced proportionately. As US employees Messrs Prozes and Tierney also are eligible to participate in Reed Elsevier's 401k plan, to which Reed Elsevier contributed €5,371 and €5,221 respectively for the year.

The pension arrangements for the above directors include life assurance cover whilst in employment, an entitlement to a pension in the event of ill health or disability and a spouse's and/or dependents' pension on death.

E Engstrom is not a member of a company pension scheme and Reed Elsevier made a contribution to Mr Engstrom's designated retirement account of €170,120, equivalent to 19.5% of his annual salary. In addition, Mr Engstrom is provided with life assurance cover whilst in employment.

The increase in the transfer value of the directors' pensions, after deduction of contributions, is shown below:

	Age 31 December 2006	Directors' contributions €	Transfer value of accrued pension 31 December 2005 €	Transfer value of accrued pension 31 December 2006 €	Increase in transfer value during the period (net of directors' contributions) €	Accrued annual pension 31 December 2006 €	Increase in accrued annual pension during the period €	Increase in accrued annual pension during the period (net of inflation) €	Transfer value of increase in accrued annual pension during the period (net of inflation and directors' contributions) €
G J A van de Aast	49	7,928	1,060,681	1,579,205	510,596	150,258	43,118	40,760	420,469
M H Armour	52	7,928	3,321,930	4,214,200	884,342	327,953	41,827	35,543	448,797
Sir Crispin Davis	57	7,928	8,178,645	10,821,386	2,634,813	549,587	93,191	83,149	1,629,289
A Prozes	60	-	-	-	-	-	-	-	-
P Tierney	61	-	2,506,030	3,131,465	625,435	253,128	32,965	32,965	405,635

Transfer values have been calculated in accordance with the guidance note GN11 published by the UK Institute of Actuaries and Faculty of Actuaries.

The transfer value in respect of individual directors represents a liability in respect of directors' pensions entitlement, and is not an amount paid or payable to the director.

**(ii) Aggregate emoluments**

The emoluments of the directors of Reed Elsevier PLC and Reed Elsevier NV (including any entitlement to fees or emoluments from either Reed Elsevier Group plc or Elsevier Reed Finance BV) were as follows:

	2006 €000	2005 €000
Salaries and fees	6,618	6,182
Benefits	185	162
Annual performance-related bonuses	4,811	4,381
Pension contributions	204	197
Pension to former director	325	326
Payment to former director	–	15
<b>Total</b>	<b>12,143</b>	<b>11,263</b>

No compensation payments have been made for loss of office or termination in 2005 and 2006.

Details of long-term share based incentives exercised by the directors over shares in Reed Elsevier PLC and Reed Elsevier NV during the year are shown on pages 74 to 78. The aggregate notional pre-tax gain made by the directors on the exercise of such incentives during the year was €2,069,866 (2005: €688,364).

**(iii) Individual emoluments of executive directors**

	Salary €	Benefits €	Bonus €	Total 2006 €	Total 2005 €
G J A van de Aast	740,801	27,629	792,127	1,560,557	1,248,596
M H Armour	825,773	31,995	718,521	1,576,289	1,502,867
Sir Crispin Davis	1,589,952	57,401	1,351,459	2,998,812	2,907,614
E Engstrom	872,413	27,432	795,771	1,695,616	1,533,636
A Prozes	889,031	24,780	841,255	1,755,066	1,676,721
P Tierney	855,796	15,354	312,879	1,184,029	1,103,582
<b>Total</b>	<b>5,773,766</b>	<b>184,591</b>	<b>4,812,012</b>	<b>10,770,369</b>	<b>9,973,016</b>

Benefits principally comprise the provision of a company car, medical insurance and life assurance.

Sir Crispin Davis was the highest paid director in 2006. His aggregate notional pre-tax gain on the exercise of share based incentives during the year was €370,822 (2005: €13,981).

**(iv) Individual emoluments of non-executive directors**

	2006 €	2005 €
G J de Boer-Kruyt	33,800	33,800
J F Brock (until 28 April 2005)	–	16,250
M W Elliott	66,150	65,700
J Hommen (from 27 April 2005)	350,000	233,333
L Hook (from 19 April 2006)	44,100	–
C J A van Lede	65,000	65,000
D E Reid	66,150	65,700
Lord Sharman	76,440	75,920
R W H Stomberg	77,000	77,000
M Tabaksblat (until 28 April 2005)	–	70,000
S Zelnick (from 27 April 2005)	66,150	49,275
<b>Total</b>	<b>844,790</b>	<b>751,978</b>

## Directors' remuneration report continued

### (v) Share options and interests in shares

Details of options and restricted shares held by directors in Reed Elsevier PLC and Reed Elsevier NV during the period are shown below.

#### (a) Options in Reed Elsevier PLC

	1 January 2006	Granted during the year	Option price	Exercised/ Lapsed during the year	Market price at exercise date	31 December 2006	Exercisable from	Exercisable until
<b>G J A van de Aast</b>								
- ESOS	50,940		638.00p			50,940	1 Dec 2003	1 Dec 2010
	49,317		659.00p			49,317	23 Feb 2004	23 Feb 2011
	58,000		600.00p			58,000	22 Feb 2005	22 Feb 2012
	81,728		451.50p	81,728 <sup>(i)</sup>	565.00p	-		
	124,956		487.25p			124,956	19 Feb 2007	19 Feb 2014
	120,900		533.50p			120,900	17 Feb 2008	17 Feb 2015
		127,662	530.50p			127,662	13 Mar 2009	13 Mar 2016
- BIP	31,217		Nil			31,217	26 Mar 2007	26 Mar 2007
		18,633	Nil			18,633	4 Apr 2009	4 April 2009
- LTIS (options)	229,087		487.25p			229,087	19 Feb 2007	19 Feb 2014
- LTIS (shares)	104,130		Nil			104,130	19 Feb 2007	19 Feb 2007
		70,364	Nil			70,364	19 Apr 2009	19 April 2009
<b>Total</b>	<b>850,275</b>	<b>216,659</b>		<b>81,728</b>		<b>985,206</b>		
<b>M H Armour</b>								
- ESOS	30,000		585.25p	30,000 <sup>(ii)</sup>		-		
	52,000		565.75p			52,000	21 Apr 2000	21 Apr 2007
	66,900		523.00p			66,900	17 Aug 2001	17 Aug 2008
	33,600		537.50p			33,600	21 Feb 2003	19 Apr 2009
	88,202		436.50p			88,202	2 May 2003	2 May 2010
	62,974		659.00p			62,974	23 Feb 2004	23 Feb 2011
	74,000		600.00p			74,000	22 Feb 2005	22 Feb 2012
	104,319		451.50p			104,319	21 Feb 2006	21 Feb 2013
	155,147		487.25p			155,147	19 Feb 2007	19 Feb 2014
	150,422		533.50p			150,422	17 Feb 2008	17 Feb 2015
		158,836	530.50p			158,836	13 Mar 2009	13 Mar 2016
- BIP	11,327		Nil	11,327	545.50p	-		
	19,225		Nil			19,225	26 Mar 2007	26 Mar 2007
	21,861		Nil			21,861	14 Apr 2008	14 Apr 2008
		21,653	Nil			21,653	4 Apr 2009	4 April 2009
- LTIS (options)	284,437		487.25p			284,437	19 Feb 2007	19 Feb 2014
- LTIS (shares)	129,289		Nil			129,289	19 Feb 2007	19 Feb 2007
		75,075	Nil			75,075	19 Apr 2009	19 Apr 2009
- SAYE	4,329		377.60p			4,329	1 Aug 2009	31 Jan 2010
<b>Total</b>	<b>1,288,032</b>	<b>255,564</b>		<b>41,327</b>		<b>1,502,269</b>		

## (a) Options in Reed Elsevier PLC continued

	1 January 2006	Granted during the year	Option price	Exercised/ Lapsed during the year	Market price at exercise date	31 December 2006	Exercisable from	Exercisable until
<b>Sir Crispin Davis</b>								
- ESOS	160,599		467.00p			160,599	21 Feb 2003	1 Sept 2009
	80,300		467.00p			80,300	1 Sept 2003	1 Sept 2009
	80,300		467.00p			80,300	1 Sept 2004	1 Sept 2009
	171,821		436.50p			171,821	2 May 2003	2 May 2010
	122,914		659.00p			122,914	23 Feb 2004	23 Feb 2011
	148,500		600.00p			148,500	22 Feb 2005	22 Feb 2012
	209,192		451.50p			209,192	21 Feb 2006	21 Feb 2013
	305,303		487.25p			305,303	19 Feb 2007	19 Feb 2014
	292,409		533.50p			292,409	17 Feb 2008	17 Feb 2015
		305,824	530.50p			305,824	13 Mar 2009	13 Mar 2016
- BIP	22,731		Nil	22,731 <sup>(iii)</sup>	545.50p	-		
	39,554		Nil			39,554	26 Mar 2007	26 Mar 2007
	86,042		Nil			86,042	14 Apr 2008	14 Apr 2008
		42,092	Nil			42,092	4 Apr 2009	4 Apr 2009
- LTIS (options)	559,722		487.25p			559,722	19 Feb 2007	19 Feb 2014
- LTIS (shares)	254,419		Nil			254,419	19 Feb 2007	19 Feb 2007
		144,550	Nil			144,550	19 Apr 2009	19 Apr 2009
- SAYE		3,793	424.40p			3,793	1 Aug 2011	31 Jan 2012
<b>Total</b>	<b>2,533,806</b>	<b>496,259</b>		<b>22,731</b>		<b>3,007,334</b>		
<b>E Engstrom</b>								
- ESOS	63,460		478.00p			63,460	23 Aug 2007	23 Aug 2014
	154,517		533.50p			154,517	17 Feb 2008	17 Feb 2015
		178,895	530.50p			178,895	13 Mar 2009	13 Mar 2016
- BIP	14,020		Nil			14,020	14 Apr 2008	14 Apr 2008
- LTIS (options)	318,398		478.00p			318,398	23 Aug 2007	23 Aug 2014
- LTIS (shares)	144,726		Nil			144,726	19 Feb 2007	19 Feb 2007
		82,092	Nil			82,092	19 Apr 2009	19 Apr 2009
- Restricted shares	77,186		Nil	38,593 <sup>(iv)</sup>	560.00p	38,593	23 Aug 2005	23 Aug 2007
<b>Total</b>	<b>772,307</b>	<b>260,987</b>		<b>38,593</b>		<b>994,701</b>		
<b>A Prozes</b>								
- ESOS	188,281		566.00p			188,281	9 Aug 2003	9 Aug 2010
	83,785		659.00p			83,785	23 Feb 2004	23 Feb 2011
	103,722		600.00p			103,722	22 Feb 2005	22 Feb 2012
	132,142		451.50p			132,142	21 Feb 2006	21 Feb 2013
	162,666		487.25p			162,666	19 Feb 2007	19 Feb 2014
	154,517		533.50p			154,517	17 Feb 2008	17 Feb 2015
		182,303	530.50p			182,303	13 Mar 2009	13 Mar 2016
- BIP	20,040		Nil	20,040 <sup>(v)</sup>	545.50p	-		
	20,104		Nil			20,104	26 Mar 2007	26 Mar 2007
	23,756		Nil			23,756	14 Apr 2008	14 Apr 2008
		26,400	Nil			26,400	4 Apr 2009	4 Apr 2009
- LTIS (options)	298,221		487.25p			298,221	19 Feb 2007	19 Feb 2014
- LTIS (shares)	135,555		Nil			135,555	19 Feb 2007	19 Feb 2007
		83,656	Nil			83,656	19 Apr 2009	19 Apr 2009
<b>Total</b>	<b>1,322,789</b>	<b>292,359</b>		<b>20,040</b>		<b>1,595,108</b>		

## Directors' remuneration report continued

### (a) Options in Reed Elsevier PLC continued

	1 January 2006	Granted during the year	Option price	Exercised/ Lapsed during the year	Market price at exercise date	31 December 2006	Exercisable from	Exercisable until
<b>P Tierney</b>								
– ESOS	396,426		451.50p	25,000 <sup>(vi)</sup>	559.00p	371,426	21 Feb 2006	21 Feb 2013
	162,666		487.25p			162,666	19 Feb 2007	19 Feb 2014
	154,517		533.50p			154,517	17 Feb 2008	17 Feb 2015
		175,488	530.50p			175,488	13 Mar 2009	13 Mar 2016
– BIP	19,572		Nil			19,572	26 Mar 2007	26 Mar 2007
	24,156		Nil			24,156	14 Apr 2008	14 Apr 2008
		8,124	Nil			8,124	4 Apr 2009	4 Apr 2009
– LTIS (options)	298,221		487.25p			298,221	19 Feb 2007	19 Feb 2014
– LTIS (shares)	135,555		Nil			135,555	19 Feb 2007	19 Feb 2007
		80,528	Nil			80,528	19 Apr 2009	19 Apr 2009
<b>Total</b>	<b>1,191,113</b>	<b>264,140</b>		<b>25,000</b>		<b>1,430,253</b>		

(i) Retained an interest in 9,652 shares

(ii) Lapsed unexercised

(iii) Retained an interest in 13,666 shares

(iv) Retained an interest in 10,226 shares

(v) Retained an interest in 13,244 shares

(vi) Retained an interest in all of the shares

Awards granted under BIP and ESOS which become exercisable from 2007 onwards are subject to post-grant performance conditions, as set out on pages 63 and 64.

The proportion of the award that may vest in 2007 under LTIS is subject to the annual growth in adjusted EPS during the performance period. The numbers of LTIS options and shares included in the above table are calculated by reference to a target annual growth rate of 10%, which would result in 100% of the award vesting. Based on actual adjusted EPS growth, approximately 102% of the target award will vest, as outlined on page 67.

The proportion of the award that may vest in 2009 under LTIS is subject to the annual growth in adjusted EPS and relative total shareholder return (TSR) measured against a group of competitor companies during the performance period. The numbers of LTIS shares included in the above table are calculated by reference to an assumed achievement of 10% per annum averaged compound growth in adjusted EPS at constant currencies and median TSR, which would result in 100% of the award vesting. Depending on actual adjusted EPS growth and TSR, the proportion of the award that may vest could be lower or higher, as outlined on pages 64 and 65.

Options under the SAYE scheme, in which all eligible UK employees are invited to participate, are granted at a maximum discount of 20% to the market price at time of grant. They are normally exercisable after the expiry of 3 or 5 years from the date of grant. No performance targets are attached to this scheme as it is an all-employee scheme.

The middle market price of a Reed Elsevier PLC ordinary share on the date of the 2006 award under BIP and LTIS was 549.50p and 535.00p, respectively.

The middle market price of a Reed Elsevier PLC ordinary share during the year was in the range 503.50p to 607.50p and at 31 December 2006 was 560.50p.

**(b) Options in Reed Elsevier NV**

	1 January 2006	Granted during the year	Option price	Exercised during the year	Market price at exercise date	31 December 2006	Exercisable from	Exercisable until
<b>G J A van de Aast</b>								
- ESOS	35,866		€14.87			35,866	1 Dec 2003	1 Dec 2010
	35,148		€14.75			35,148	23 Feb 2004	23 Feb 2011
	40,699		€13.94			40,699	22 Feb 2005	22 Feb 2012
	58,191		€9.34	58,191 <sup>(ii)</sup>	€12.11	-		
	85,805		€10.57			85,805	19 Feb 2007	19 Feb 2014
	82,478		€11.31			82,478	17 Feb 2008	17 Feb 2015
		85,775	€11.47			85,775	13 Mar 2009	13 Mar 2016
- BIP	12,057		Nil	12,057 <sup>(iii)</sup>	€11.70	-		
	26,347		Nil			26,347	14 Apr 2008	14 Apr 2008
		12,311	Nil			12,311	4 Apr 2009	4 Apr 2009
- LTIS (options)	157,309		€10.57			157,309	19 Feb 2007	19 Feb 2014
- LTIS (shares)	71,504		Nil			71,504	19 Feb 2007	19 Feb 2007
		46,332	Nil			46,332	19 Apr 2009	19 Apr 2009
<b>Total</b>	<b>605,404</b>	<b>144,418</b>		<b>70,248</b>		<b>679,574</b>		
<b>M H Armour</b>								
- ESOS	20,244		€13.55			20,244	21 Feb 2003	19 Apr 2009
	61,726		€10.73			61,726	2 May 2003	2 May 2010
	44,882		€14.75			44,882	23 Feb 2004	23 Feb 2011
	51,926		€13.94			51,926	22 Feb 2005	22 Feb 2012
	74,276		€9.34			74,276	21 Feb 2006	21 Feb 2013
	106,536		€10.57			106,536	19 Feb 2007	19 Feb 2014
	102,618		€11.31			102,618	17 Feb 2008	17 Feb 2015
		106,720	€11.47			106,720	13 Mar 2009	13 Mar 2016
- BIP	8,030		Nil	8,030	€11.70	-		
	12,842		Nil			12,842	26 Mar 2007	26 Mar 2007
	15,098		Nil			15,098	14 Apr 2008	14 Apr 2008
		14,306	Nil			14,306	4 Apr 2009	4 Apr 2009
- LTIS (options)	195,317		€10.57			195,317	19 Feb 2007	19 Feb 2014
- LTIS (shares)	88,780		Nil			88,780	19 Feb 2007	19 Feb 2007
		49,434	Nil			49,434	19 Apr 2009	19 Apr 2009
<b>Total</b>	<b>782,275</b>	<b>170,460</b>		<b>8,030</b>		<b>944,705</b>		
<b>Sir Crispin Davis</b>								
- ESOS	95,774		€12.00			95,774	21 Feb 2003	1 Sept 2009
	47,888		€12.00			47,888	1 Sept 2003	1 Sept 2009
	47,888		€12.00			47,888	1 Sept 2004	1 Sept 2009
	120,245		€10.73			120,245	2 May 2003	2 May 2010
	87,601		€14.75			87,601	23 Feb 2004	23 Feb 2011
	104,204		€13.94			104,204	22 Feb 2005	22 Feb 2012
	148,946		€9.34			148,946	21 Feb 2006	21 Feb 2013
	209,645		€10.57			209,645	19 Feb 2007	19 Feb 2014
	199,481		€11.31			199,481	17 Feb 2008	17 Feb 2015
		205,480	€11.47			205,480	13 Mar 2009	13 Mar 2016
- BIP	16,115		Nil	16,115 <sup>(iii)</sup>	€11.70	-		
	26,421		Nil			26,421	26 Mar 2007	26 Mar 2007
		27,810	Nil			27,810	4 Apr 2009	4 Apr 2009
- LTIS (options)	384,349		€10.57			384,349	19 Feb 2007	19 Feb 2014
- LTIS (shares)	174,704		Nil			174,704	19 Feb 2007	19 Feb 2007
		95,181	Nil			95,181	19 Apr 2009	19 Apr 2009
<b>Total</b>	<b>1,663,261</b>	<b>328,471</b>		<b>16,115</b>		<b>1,975,617</b>		

## Directors' remuneration report continued

### (b) Options in Reed Elsevier NV continued

	1 January 2006	Granted during the year	Option price	Exercised during the year	Market price at exercise date	31 December 2006	Exercisable from	Exercisable until
<b>E Engstrom</b>								
- ESOS	43,866		€10.30			43,866	23 Aug 2007	23 Aug 2014
	105,412		€11.31			105,412	17 Feb 2008	17 Feb 2015
		120,198	€11.47			120,198	13 Mar 2009	13 Mar 2016
- BIP		29,442	Nil			29,442	4 Apr 2009	4 Apr 2009
- LTIS (options)	220,090		€10.30			220,090	23 Aug 2007	23 Aug 2014
- LTIS (shares)	100,040		Nil			100,040	19 Feb 2007	19 Feb 2007
		54,055	Nil			54,055	19 Apr 2009	19 Apr 2009
- Restricted shares	53,354		Nil	26,677 <sup>(iv)</sup>	€12.39	26,677	23 Aug 2005	23 Aug 2007
<b>Total</b>	<b>522,762</b>	<b>203,695</b>		<b>26,677</b>		<b>699,780</b>		
<b>A Prozes</b>								
- ESOS	131,062		€13.60			131,062	9 Aug 2003	9 Aug 2010
	59,714		€14.75			59,714	23 Feb 2004	23 Feb 2011
	72,783		€13.94			72,783	22 Feb 2005	22 Feb 2012
	94,086		€9.34			94,086	21 Feb 2006	21 Feb 2013
	111,699		€10.57			111,699	19 Feb 2007	19 Feb 2014
	105,412		€11.31			105,412	17 Feb 2008	17 Feb 2015
		122,487	€11.47			122,487	13 Mar 2009	13 Mar 2016
- BIP	14,552		Nil	14,552 <sup>(v)</sup>	€11.70	-		
	13,612		Nil			13,612	26 Mar 2007	26 Mar 2007
	16,522		Nil			16,522	14 Apr 2008	14 Apr 2008
		17,636	Nil			17,636	4 Apr 2009	4 Apr 2009
- LTIS (options)	204,782		€10.57			204,782	19 Feb 2007	19 Feb 2014
- LTIS (shares)	93,083		Nil			93,083	19 Feb 2007	19 Feb 2007
		55,085	Nil			55,085	19 Apr 2009	19 Apr 2009
<b>Total</b>	<b>917,307</b>	<b>195,208</b>		<b>14,552</b>		<b>1,097,963</b>		
<b>P Tierney</b>								
- ESOS	282,258		€9.34	16,000 <sup>(vi)</sup>	€12.90	266,258	21 Feb 2006	21 Feb 2013
	111,699		€10.57			111,699	19 Feb 2007	19 Feb 2014
	105,412		€11.31			105,412	17 Feb 2008	17 Feb 2015
		117,908	€11.47			117,908	13 Mar 2009	13 Mar 2016
- BIP	13,252		Nil			13,252	26 Mar 2007	26 Mar 2007
	16,800		Nil			16,800	14 Apr 2008	14 Apr 2008
		5,426	Nil			5,426	4 Apr 2009	4 Apr 2009
- LTIS (options)	204,782		€10.57			204,782	19 Feb 2007	19 Feb 2014
- LTIS (shares)	93,083		Nil			93,083	19 Feb 2007	19 Feb 2007
		53,025	Nil			53,025	19 Apr 2009	19 Apr 2009
<b>Total</b>	<b>827,286</b>	<b>176,359</b>		<b>16,000</b>		<b>987,645</b>		

(i) Retained an interest in 7,411 shares

(ii) Retained an interest in 7,836 shares

(iii) Retained an interest in 9,708 shares

(iv) Retained an interest in all of the shares

(v) Retained an interest in 9,598 shares

(vi) Retained an interest in all of the shares

Awards granted under BIP and ESOS which become exercisable from 2007 onwards are subject to post-grant performance conditions, as set out on pages 63 and 64.

The proportion of the award that may vest in 2007 under LTIS is subject to the annual growth in adjusted EPS at constant currencies during the performance period. The numbers of LTIS options and shares included in the above table are calculated by reference to a target annual growth rate of 10%, which would result in 100% of the award vesting. Based on actual adjusted EPS growth, approximately 102% of the target award will vest, as outlined on page 67.

The proportion of the award that may vest in 2009 under LTIS is subject to the annual growth in adjusted EPS at constant currencies and relative total shareholder return (TSR) measured against a group of competitor companies during the performance period. The numbers of LTIS shares included in the above table are calculated by reference to an assumed achievement of 10% per annum averaged compound growth in adjusted EPS at constant currencies and median TSR, which would result in 100% of the award vesting. Depending on actual adjusted EPS growth and TSR, the proportion of the award that may vest could be lower or higher, as outlined on pages 64 and 65.

The market price of a Reed Elsevier NV ordinary share on the date of the 2006 award under BIP and LTIS was €11.78 and €11.76, respectively.

The market price of a Reed Elsevier NV ordinary share during the year was in the range €11.08 to €13.72 and at 31 December 2006 was €12.92.

### (c) Shareholdings in Reed Elsevier PLC and Reed Elsevier NV

	Reed Elsevier PLC ordinary shares		Reed Elsevier NV ordinary shares	
	1 January 2006 <sup>(i)</sup>	31 December 2006	1 January 2006 <sup>(i)</sup>	31 December 2006
G J A van de Aast	18,600	39,169	35,445	57,941
M H Armour	99,321	112,007	38,727	47,150
G J de Boer-Kruyt	-	-	-	-
Sir Crispin Davis	528,847	567,174	298,261	324,344
M W Elliott	-	-	-	-
E Engstrom	19,253	29,479	26,678	73,415
J Hommen	-	-	-	-
L Hook	-	-	-	-
C J A van Lede	-	-	11,100	-
A Prozes	91,444	123,740	73,632	95,954
D E Reid	-	-	-	-
Lord Sharman	-	-	-	-
R W H Stomberg	-	-	-	-
P Tierney	42,440	72,212	28,902	48,090
S Zelnick	-	-	-	-

(i) On date of appointment if subsequent to 1 January 2006.

Any ordinary shares required to fulfil entitlements under nil cost restricted share awards are provided by the Employee Benefit Trust (EBT) from market purchases. As a potential beneficiary under the EBT in the same way as other employees of Reed Elsevier, each executive director is deemed to be interested in all the shares held by the EBT which, at 31 December 2006, amounted to 17,167,145 Reed Elsevier PLC ordinary shares and 9,242,214 Reed Elsevier NV ordinary shares.

The Directors' Remuneration Report was approved and authorised for issue by the boards of directors of Reed Elsevier Group plc, Reed Elsevier PLC and Reed Elsevier NV on 14 February 2007. The Directors' Remuneration Report presented in euros was approved for publication on the Reed Elsevier website, [www.reedelsevier.com](http://www.reedelsevier.com), on 22 March 2007.

