

**IBM United Kingdom Limited**  
**Financial Statements**  
**31 December 2007**



# **IBM United Kingdom Limited**

## **Financial Statements**

**Year Ended 31 December 2007**

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# IBM United Kingdom Limited

## Company Information

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<b>The board of directors</b>	B Riley S D Wilson A Creasey B Ross J Granger
<b>Company secretary</b>	I Ferguson (appointed 6 September 2007) N Sayani (resigned 6 September 2007)
<b>Registered office</b>	PO Box 41 North Harbour Portsmouth Hampshire PO6 3AU
<b>Independent auditor</b>	PricewaterhouseCoopers LLP Chartered Accountants & Registered Auditors Savannah House 3 Ocean Way Ocean Village Southampton Hampshire SO14 3TJ
<b>Bankers</b>	National Westminster Bank PLC 69 High Street Cosham PO6 3DA
<b>Solicitors</b>	Ashurst Morris Crisp Broadwalk House 5 Appold Street London EC2A 2HA

# **IBM United Kingdom Limited**

## **The Directors' Report**

**Year Ended 31 December 2007**

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The directors present their report and the audited financial statements of the company for the year ended 31 December 2007

### **PRINCIPAL ACTIVITIES AND BUSINESS REVIEW**

IBM is a globally integrated innovation company, serving the needs of enterprises and institutions worldwide. The company seeks to be a partner in its clients' success by enabling their own capacity to innovate, so that they may differentiate themselves for competitive advantage in a globalised economy.

In the United Kingdom, IBM offers a broad range of hardware and software solutions, technology services and business consulting to clients in all industries, including small and mid-size businesses. We combine broad expertise across industries and business processes with deep technology capability. In this way, we are able to provide complete solutions to our clients' business problems. More than half our employees are engaged in services-related work for large and small enterprises and Government agencies.

In recent years, we have shifted our business mix away from commodity segments, while investing in targeted acquisitions to continue to build capabilities in higher value areas such as our software portfolio and services offerings.

IBM is able to offer unique breadth of capability of business and technology solutions, services and products. We work with a broad and growing range of business partners to deliver and integrate these for our clients.

The software development laboratory at Hursley, Hampshire, develops new products for IBM worldwide and enables us to offer our customers a unique glimpse into information technology's potential and future.

IBM also prides itself as a progressive corporate citizen and proactively engages government organisations, industry bodies, communities and experts on many issues facing business and society, including education, diversity and energy and climate change.

We expect the above activities to continue in the future.

# **IBM United Kingdom Limited**

## **The Directors' Report** *(continued)*

**Year Ended 31 December 2007**

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### **PRINCIPAL RISKS AND UNCERTAINTIES**

The key business risks affecting the company are considered to relate to the economic environment and competition

The company operates in a highly competitive market but it has an ability to innovate and integrate which is considered to be unique to IBM, and sets it apart from its competition.

If overall demand for systems, software and services changes, whether due to general economic conditions or a shift in corporate buying patterns, sales performance could be impacted. IBM's diverse set of products and offerings is designed to provide more consistent results in both strong and weak economic environments. The company accomplishes this by not only having a mix of offerings with long-term cash and income streams, as well as cyclical transaction based sales, but also by continually developing competitive products and solutions and effectively managing a skilled resource base. IBM continues to transform itself to take advantage of shifting demand trends, focusing on open standards and client and industry specific solutions.

### **KEY PERFORMANCE INDICATORS**

IBM United Kingdom Limited is managed by the UK board along with other UK IBM entities. The performance and results for all UK entities are analysed on a worldwide IBM measurement basis, at a business unit and sector level. For this reason the directors of IBM United Kingdom Limited believe that analysis using key performance indicators is not appropriate for an understanding of the development, performance or position of the business shown in these financial statements. The development, performance and position of International Business Machines Corporation, which includes the UK entities, is discussed on pages 23 - 37 of their financial statements, which do not form part of this report.

### **RESULTS AND DIVIDENDS**

The trading results for the year and the company's financial position at the end of the year are shown in the attached financial statements on pages 9 to 12.

The directors have not recommended a dividend (2006 £nil).

### **FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES**

The company is exposed to a variety of financial risks as a result of its operations that include the effects of changes in market prices, credit risk, liquidity risk, interest rate risk and currency risk. The company has a strong risk management programme in place aligned to the worldwide programme of the company's ultimate parent company, International Business Machines Corporation.

#### **Price risk**

The financial risk posed by external vendors is managed and controlled by IBM's central procurement function. Procurement is the only business unit in IBM which is authorised to make financial commitments to external vendors. The unit has responsibility for achieving overall value for IBM in terms of supplier selection at the optimum price. All procurement activities are carried out under worldwide IBM guidelines.

#### **Credit risk**

The company has in place policies that require appropriate credit checks on potential customers before sales are made and regular reviews of credit limits on existing customers are carried out. The company also manages its credit risk by factoring certain trade receivables. Any losses incurred in the collection of the debt sold are not borne by the company.

# **IBM United Kingdom Limited**

## **The Directors' Report** *(continued)*

**Year Ended 31 December 2007**

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### **FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES** *(continued)*

#### **Liquidity and interest rate risk**

The company is funded internally by IBM Treasury Centre in Ireland. There is a letter of support in place from IBM World Trade Corporation confirming that the company can take funding from the Treasury Centre to enable it to meet any liquidity shortfall as the Treasury Centre is ultimately funded by International Business Machines Corporation. Any borrowing is treated as short term debt finance. The company does not have any long term debt finance.

As the company invests or borrows cash balances internally it operates daily in either a cash or overdraft position with no fixed period debt in place. Interest is paid or earned on the daily balance using the variable one month interest rate as the base.

#### **Currency risk**

The company operates a 12 month forward rolling hedging programme to hedge a proportion of its US dollar costs arising from transactions with both related companies and suppliers.

### **RESEARCH AND DEVELOPMENT**

Specific product development projects are carried out at the laboratories in Hursley and Warwick on behalf of International Business Machines Corporation and its subsidiaries. The expenditure on these projects in the year was recharged to International Business Machines Corporation.

### **DIRECTORS**

The directors who served the company during the year and up to the date of signing these financial statements were as follows:

L Hirst	(Resigned 12 May 2008)
B Riley	(Appointed 24 June 2008)
S D Wilson	
A Creasey	
B Ross	(Appointed 25 January 2007)
J Granger	(Appointed 29 June 2007)

### **JOINT VENTURE**

During 2007 International Business Machines Corporation and Ricoh announced the formation of a joint venture company based on IBM's Printing Division. Infoprint Solutions Company was created following IBM's decision that its printing systems division clients and employees would be best served by the creation of a new company which would focus primarily on the output solutions business. Ricoh will initially own 51% of the company and will progressively acquire the remaining 49% from IBM over the next three years. In the UK this involved IBM United Kingdom Limited selling its printing division to Infoprint Solutions United Kingdom Limited, a subsidiary of Infoprint Solutions Company. The gain on sale recognised in these financial statements is £3.0 million.

### **CHANGES TO DEFINED BENEFIT PENSION PLANS**

During 2006 changes were made to the Defined Benefit sections of the Pension Plans to help control and stabilise the future costs of the Plans. Under these changes salary increases received by members who elected to stay in the defined benefit sections may not be fully pensionable, increases to pensions paid to retirees in respect of years of service prior to 1997 were agreed with the Trustee for the next fifteen years, and a number of members of the Defined Benefit sections elected to transfer to an enhanced defined contribution section of the Plan for future service. As a result of these changes a past service credit of £250.5 million was recognised in the prior year.

# **IBM United Kingdom Limited**

## **The Directors' Report** *(continued)*

**Year Ended 31 December 2007**

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### **SALE OF LAND**

On 29 December 2006, the company entered into a transaction to sell the remaining land held at the North Harbour site. A profit of £6.8 million was recognised on the disposal in the prior year.

### **MARKET VALUE OF LAND AND BUILDINGS**

The directors believe that the market value of the land and buildings reported in the accounts is not materially different from the net book value.

### **DONATIONS**

During the year the company made donations in the United Kingdom totalling £0.8 million (2006 £0.8 million) for educational, cultural and social welfare activities. The company made no donations for political purposes.

### **DISABLED EMPLOYEES**

Disabled persons in common with all others are given full consideration in respect of selection, continued employment, training, career development and promotion.

### **EMPLOYEE INVOLVEMENT**

Employees receive information on the financial and economic factors affecting the performance of the business, along with product announcements, details of organisational changes and all other matters of direct concern and interest to them. This information is provided by the internal publication 'Link me', and by their managers. The views of the employees are obtained from opinion surveys, at departmental meetings and through direct contact with their managers.

The company has also established a 'UK Forum' as an additional communication channel with employees. The 'UK Forum' consists of representatives of the employee population who are elected to represent the views of employees and consult with the company on major areas of interest.

The company continues to support employee share ownership through established employee share schemes, membership of which is service related.

In addition, all IBM employees have the opportunity to purchase IBM shares through the IBM Employee Stock Purchase Plan, which is intended to encourage employees to take active ownership in IBM and to be committed to its long term success.

### **SUPPLIER PAYMENT POLICY AND PRACTICE**

The company agrees payment terms with its suppliers when it enters into binding purchase contracts. The company seeks to abide by the payment terms agreed with the suppliers whenever it is satisfied that the supplier has provided the goods and services in accordance with the agreed terms and conditions. The company seeks to treat all its suppliers fairly and has a standard policy which deals specifically with the payment of suppliers. At the year end the company had an average of 63 days (2006 66 days) purchases outstanding in trade creditors, of which 37 days (2006 41 days) represent invoiced goods and services and the balance accrued items.

### **CLOSE COMPANY STATUS**

The company is not a close company within the meaning of the provision of the Income and Corporation Taxes Act 1988.

# IBM United Kingdom Limited

## The Directors' Report *(continued)*

Year Ended 31 December 2007

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### STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). The financial statements are required by law to give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, the directors are required to

select suitable accounting policies and then apply them consistently,

make judgements and estimates that are reasonable and prudent,

state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements,

prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities. The directors confirm that they have complied with the above requirements and responsibilities.

### DISCLOSURE OF INFORMATION TO AUDITORS

In so far as the directors are aware

there is no relevant audit information of which the company's auditor is unaware, and

the directors have taken all steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the auditor is aware of that information.

### AUDITOR

Pursuant to s386 Companies Act 1985, an elective resolution was passed on 28 October 2004 dispensing with the requirement to appoint auditors annually. Therefore PricewaterhouseCoopers LLP are deemed to continue as auditors.

Signed by order of the board



I Ferguson  
Company Secretary

28 July 2008



# **IBM United Kingdom Limited**

## **Independent Auditors' Report to the Members of IBM United Kingdom Limited**

**Year Ended 31 December 2007**

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We have audited the financial statements of IBM United Kingdom Limited for the year ended 31 December 2007 which comprise the Profit and Loss Account, Statement of Total Recognised Gains and Losses, the Balance Sheet, the Cash Flow Statement and the related notes. These financial statements have been prepared under the accounting policies set out therein.

### **RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS**

The directors' responsibilities for preparing the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities.

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

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements.

In addition we report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

### **BASIS OF AUDIT OPINION**

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

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

# **IBM United Kingdom Limited**

## **Independent Auditors' Report to the Members of IBM United Kingdom Limited *(continued)***

**Year Ended 31 December 2007**

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### **OPINION**

In our opinion

the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the company's affairs as at 31 December 2007 and of its profit for the year then ended,

the financial statements have been properly prepared in accordance with the Companies Act 1985, and

the information given in the Directors' Report is consistent with the financial statements



PricewaterhouseCoopers LLP  
Chartered Accountants & Registered Auditors  
Southampton

28 July 2008

# IBM United Kingdom Limited

## Profit and Loss Account

Year Ended 31 December 2007

	Note	2007 £m	2006 (restated) £m
<b>TURNOVER</b>	<b>2</b>	<b>3,674.1</b>	<b>3,659.5</b>
Cost of sales		<u>(3,494.1)</u>	<u>(3,178.7)</u>
<b>GROSS PROFIT</b>		<b>180.0</b>	<b>480.8</b>
Distribution costs		(4.1)	(4.6)
Administrative expenses		(134.8)	(144.7)
Other operating income		<u>4.0</u>	<u>5.8</u>
<b>OPERATING PROFIT</b>	<b>3</b>	<b>45.1</b>	<b>337.3</b>
Profit on disposal of fixed assets	<b>6</b>	–	6.8
Profit on sale of operation	<b>7</b>	<u>3.0</u>	<u>–</u>
		<b>48.1</b>	<b>344.1</b>
Interest receivable and similar income	<b>8</b>	37.2	41.6
Interest payable and similar charges	<b>9</b>	(19.8)	(31.2)
Other finance income	<b>19</b>	<u>103.3</u>	<u>90.0</u>
<b>PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION</b>		<b>168.8</b>	<b>444.5</b>
Tax on profit on ordinary activities	<b>10</b>	16.4	(89.5)
<b>PROFIT FOR THE FINANCIAL YEAR</b>		<u><b>185.2</b></u>	<u><b>355.0</b></u>

All of the activities of the company are classed as continuing

There is no difference between the profit and loss account reported above and its historical cost equivalent

The notes on pages 13 to 40 form part of these financial statements

# IBM United Kingdom Limited

## Statement of Total Recognised Gains and Losses

Year Ended 31 December 2007

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		2007	2006
		£m	(restated) £m
Profit for the financial year	27	185.2	355 0
Actuarial gain in respect of defined benefit pension scheme	19	316.2	177 2
Deferred tax in respect of defined benefit pension scheme	16	(88.5)	(53 2)
		<hr/>	<hr/>
Total recognised gains and losses relating to the year		412.9	479 0
Prior year adjustment	27	49.2	-
		<hr/>	<hr/>
Total gains and losses recognised since the last annual report		462.1	479 0

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The notes on pages 13 to 40 form part of these financial statements.

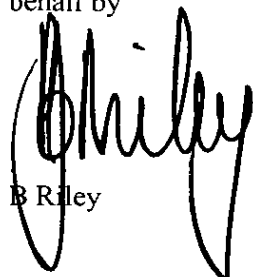
# IBM United Kingdom Limited

## Balance Sheet

31 December 2007

	Note	2007 £m	2006 (restated) £m
<b>FIXED ASSETS</b>			
Intangible assets	11	–	45 8
Tangible assets	12	335.9	354 1
		<u>335.9</u>	<u>399 9</u>
<b>CURRENT ASSETS</b>			
Stock	14	8.0	13 0
Debtors due within one year	15	1,764.7	1,529 1
Debtors due after one year	15	199.1	208 2
Cash at bank		28.6	34 0
		<u>2,000.4</u>	<u>1,784 3</u>
<b>CREDITORS: Amounts falling due within one year</b>	17	<u>(1,350.8)</u>	<u>(1,302 8)</u>
<b>NET CURRENT ASSETS</b>		<u>649.6</u>	<u>481 5</u>
<b>TOTAL ASSETS LESS CURRENT LIABILITIES</b>		<u>985.5</u>	<u>881 4</u>
<b>CREDITORS: Amounts falling due after more than one year</b>	18	<u>(56.8)</u>	<u>(42 5)</u>
		<u>928.7</u>	<u>838 9</u>
<b>PROVISIONS FOR LIABILITIES AND CHARGES</b>	20	<u>(39.4)</u>	<u>(38 1)</u>
<b>NET ASSETS EXCLUDING PENSION SCHEME ASSET</b>		<u>889.3</u>	<u>800 8</u>
Pension scheme asset	19	301.0	17 4
<b>NET ASSETS INCLUDING PENSION SCHEME ASSET</b>		<u>1,190.3</u>	<u>818 2</u>
<b>CAPITAL AND RESERVES</b>			
Called-up equity share capital	26	956.4	956 4
Share premium account	27	277.9	277 9
Share options reserve	27	–	1 9
Profit and loss account	27	(44.0)	(418 0)
<b>TOTAL SHAREHOLDERS' FUNDS</b>	28	<u>1,190.3</u>	<u>818 2</u>

These financial statements were approved by the directors on 28 July 2008 and are signed on their behalf by

  
B Riley

The notes on pages 13 to 40 form part of these financial statements

# IBM United Kingdom Limited

## Cash Flow Statement

Year Ended 31 December 2007

	Note	2007 £m	2006 £m
<b>NET CASH INFLOW/(OUTFLOW) FROM OPERATING ACTIVITIES</b>	<b>29</b>	<b>143.1</b>	<b>(259 1)</b>
<b>RETURNS ON INVESTMENTS AND SERVICING OF FINANCE</b>			
Interest received		2.7	0 3
Interest paid		(17.5)	(27 7)
<b>NET CASH OUTFLOW FROM RETURNS ON INVESTMENTS AND SERVICING OF FINANCE</b>		<b>(14.8)</b>	<b>(27 4)</b>
<b>TAXATION</b>		<b>(1.6)</b>	<b>7 0</b>
<b>CAPITAL EXPENDITURE AND FINANCIAL INVESTMENT</b>			
Payments to acquire tangible fixed assets		(85.2)	(143 7)
Receipts from sale of tangible fixed assets		-	7 2
Issue of loans/repayment of loans made to group undertakings		(3.2)	261 8
<b>NET CASH (OUTFLOW)/INFLOW FROM CAPITAL EXPENDITURE AND FINANCIAL INVESTMENT</b>		<b>(88.4)</b>	<b>125 3</b>
<b>ACQUISITIONS AND DISPOSALS</b>			
Cash acquired with purchase of businesses		16.0	0 2
Receipts from sale of operation		2.3	-
<b>NET CASH INFLOW FROM ACQUISITIONS AND DISPOSALS</b>		<b>18.3</b>	<b>0 2</b>
<b>NET CASH INFLOW/(OUTFLOW) BEFORE MANAGEMENT OF LIQUID RESOURCES</b>		<b>56.6</b>	<b>(154 0)</b>
<b>MANAGEMENT OF LIQUID RESOURCES *</b>			
(Increase)/decrease in amounts placed on deposit		(62.0)	185 4
<b>(DECREASE)/INCREASE IN CASH</b>	<b>29</b>	<b>(5.4)</b>	<b>31 4</b>

\*Management of liquid resources includes amounts held on short term deposit (note 15)

The consideration for the acquisition of trade and assets of fellow subsidiary undertakings has resulted in an increase in amounts owed to fellow subsidiary undertakings (note 17)

Included in the net cash outflow from operating activities is £104 9 million (2006 £640 3 million) relating to cash paid in respect of pension contributions (note 19)

The notes on pages 13 to 40 form part of these financial statements

# **IBM United Kingdom Limited**

## **Notes to the Financial Statements**

**Year Ended 31 December 2007**

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### **1. ACCOUNTING POLICIES**

#### **Basis of accounting**

These financial statements have been prepared on a going concern basis, under the historical cost convention, in accordance with the Companies Act 1985 and applicable accounting standards in the United Kingdom. The principal accounting policies, which have been applied consistently throughout the year, are set out in the note below.

#### **Change in accounting policy**

The prior year results have been restated because of a change in accounting policy in respect of FRS 20 'Share Based Payment'. The treatment of the parent company recharges to IBM United Kingdom Limited on the exercise of share options has been amended and is now offset to equity instead of a charge in the profit and loss account which makes the treatment consistent with other group undertakings. As a result of this change the share options reserve has been reduced by £51.4 million, the profit and loss account reserve has been increased by £49.2 million, deferred tax has been reduced by £2.2 million and shareholders funds reduced overall by £2.2 million.

#### **Turnover**

Turnover is shown net of VAT and other taxes.

The company recognises revenue when it is realised or realisable and earned. The company considers revenue realised or realisable and earned when it has persuasive evidence of an arrangement, the product has been shipped or the services have been provided to the customer, the sales price is fixed or determinable and collectibility is reasonably assured.

Global Services revenue is recognised on a time and materials basis, a percentage of completion method, on a straight line basis over the term of the contract, or on an output basis that reflects the services provided during the period. The methodology used is dependant on the nature of the contract.

Revenue from perpetual (one-time charge) license software is recognised at the inception of the license term if all revenue recognition criteria have been met. Revenue from term (monthly license charge) license software is recognised over the term of the subscription. In addition, the company markets and distributes certain software products under a Commissionaire Agreement and recognises commission earned upon delivery of the licence key.

Revenue from hardware sales is recognised when risk of loss has transferred to the client and there are no unfulfilled company obligations that affect the client's final acceptance of the arrangement.

The company enters into multiple-element revenue arrangements which may include any combination of services, software and hardware. A multiple-element arrangement is separated into more than one unit of accounting if the commercial substance is that the individual components operate independently of each other and a reliable fair value can be attributed to each component. If the components are not deemed to operate independently of each other then the arrangement is accounted for as a whole to reflect the company's right to consideration in exchange for the performance of its obligations.

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

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### 1. ACCOUNTING POLICIES *(continued)*

#### Long term contracts

Work in progress on long term contracts is valued at the lower of cost and net realisable value. Profits are recognised on each contract using the percentage of completion method, on a straight line basis over the term of the contract or as costs are incurred. The methodology used is dependent on the nature of the contract. Amounts receivable under them are included in debtors valued according to the work done at contract prices less payments received on account. Full provision for future anticipated losses and any excess of payments received over amounts recoverable is included in creditors.

#### Goodwill

Goodwill arising on the acquisition of PricewaterhouseCoopers Consulting business is being amortised over its estimated useful economic life of five years. The Directors believe this to be appropriate as the main contracts acquired with this business have term periods ranging between one and five years. Other purchased goodwill arising on the acquisition of a business is amortised through the profit and loss account over five years. If a business is subsequently sold or closed, any goodwill arising on acquisition that was written off directly to reserves or that has not been amortised through the profit and loss account is taken into account in determining the profit or loss on sale or closure.

#### Tangible fixed assets

The cost of a tangible fixed asset comprises its purchase price and any costs directly attributable to bringing it into working condition for its intended use.

The carrying values of tangible fixed assets are reviewed for impairment if events or changes in circumstances indicate that the carrying value may not be recoverable. Impairment reviews are carried out by the associated IBM business division. Any impairment in value is charged to the profit and loss account.

#### Depreciation

Depreciation is calculated on a straight line basis, so as to write off the cost of an asset, less its estimated residual value, over the useful economic life of that asset as follows:

Land and buildings	- 5 - 50 years
Plant and machinery	- 1.5 - 7 years
Fixtures and fittings	- 5 - 15 years

#### Stock

Stock is valued at the lower of cost and net realisable value, after making due allowance for obsolete and slow moving items.

Cost includes all costs incurred in bringing each product to its present location and condition, including a proportion of overheads where appropriate. Net realisable value is based on estimated selling price less further costs expected to be incurred to completion and disposal.



# **IBM United Kingdom Limited**

## **Notes to the Financial Statements**

**Year Ended 31 December 2007**

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### **1. ACCOUNTING POLICIES** *(continued)*

#### **Finance lease agreements**

Assets owned by the company which are leased to customers under finance lease arrangements are not included in fixed assets, as amounts receivable under such agreements are included in debtors

The net investment in finance leases represents the total minimum lease payments receivable less finance charges allocated to future periods excluding amounts already invoiced, which are included in trade debtors

#### **Operating lease agreements**

Assets owned by the company which are leased to customers under operating leases are included in fixed assets and are depreciated at rates intended to write off the cost of the assets less an estimated residual value over their useful economic lives. Rental income is taken to the profit and loss account on a straight line basis

Where the company enters into operating leases as a lessee, the rental charges are charged to the profit and loss account on a straight line basis over the life of the lease

#### **Pensions**

The company contributes to a number of pension plans, which comprise both defined benefit and defined contribution sections

The cost of the defined contribution section of the pension plan is charged to the profit and loss account in the year in which it is incurred

For the defined benefit section pension scheme liabilities are measured on an actuarial basis using a projected unit method and are discounted to their present value. Pension scheme assets are valued at market value as at the balance sheet date. The net pension scheme asset is recognised in full on the balance sheet where there is sufficient evidence that the asset is fully recoverable. The deferred tax relating to the defined benefit asset is offset against the defined benefit asset and not included with other deferred tax assets or liabilities. Operating costs are recognised in the profit and loss account in the year in which they are earned by the employees and finance costs and any other changes in the value of assets and liabilities are recognised in the year in which they arise

Details of the group's pension commitments are shown in note 19

#### **Provisions for liabilities and charges**

The company makes provision for the consolidation of the company's property portfolio and the rebalancing of the workforce, when the company has a present legal or constructive obligation as a result of a past event and it is probable that a transfer of economic benefits, which can be reliably estimated, will be required to settle the obligation

Any adjustment to the provision is charged to the profit and loss account in the year in which it is incurred

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

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### 1. ACCOUNTING POLICIES *(continued)*

#### **Deferred taxation**

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events have occurred at that date that will result in an obligation to pay more, or a right to pay less or to receive more tax, with the following exceptions

- Provision is made for tax on gains arising from the revaluation (and similar fair value adjustments) of fixed assets, and gains on disposal of fixed assets that have been rolled over into replacement assets, only to the extent that, at the balance sheet date, there is a binding agreement to dispose of the assets concerned. However, no provision is made where, on the basis of all available evidence at the balance sheet date, it is more likely than not that the taxable gain will be rolled over into replacement assets and charged to tax only when the replacement assets are sold
- Deferred tax assets are recognised only to the extent that the directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted

Deferred tax is measured on an undiscounted basis at the tax rates that are expected to apply in the periods in which timing differences reverse, based on tax rates and laws enacted or substantively enacted at the balance sheet date

#### **Foreign currencies**

Monetary assets and liabilities denominated in foreign currencies are translated at the rate of exchange ruling at the balance sheet date. Transactions in foreign currencies are translated at the rate of exchange ruling at the transaction date. The company operates a 12 month forward rolling hedging programme to hedge its US dollar costs arising from transactions with both related companies and suppliers. All realised differences are taken to the profit and loss account

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

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### 1. ACCOUNTING POLICIES *(continued)*

#### **Share-based payments**

Equity-settled share-based payments are provided to certain employees (including directors) under the terms of the company's share option plans. All plans are for shares in the company's ultimate parent undertaking, International Business Machines Corporation.

Equity-settled share-based payments are measured at fair value at the date of grant. The fair value determined at the grant date of the equity-settled share-based payments is expensed on an accelerated method over the vesting period, together with a corresponding increase in equity, based upon the company's estimate of the number of shares that will eventually vest.

Fair value is measured using the Black-Scholes option pricing model. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions and behavioural considerations.

As per the terms of the arrangement with International Business Machines Corporation, IBM United Kingdom Limited is required to compensate its ultimate parent undertaking for the difference between the market value of the underlying shares on exercise date and the proceeds from the exercise of the share-based payments. The intercompany charge is first offset to equity against the share option reserve arising on the issue of share-based payments and the excess, if any, is treated as a reduction in retained earnings.

#### **Financial instruments**

Financial instruments are classified and accounted for, according to the substance of the contractual arrangement, as either financial assets, financial liabilities or equity instruments. An equity instrument is any contract that evidences a residual interest in the assets of the company after deducting all of its liabilities.

#### **Research and development**

Costs of product development are recharged to the ultimate parent undertaking in the United States of America.

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 2. TURNOVER

	Home £m	Export £m	Total £m
<b>2007</b>			
Hardware	431.8	-	431.8
Global Services	1,955.8	912.1	2,867.9
Software	374.4	-	374.4
Total	<u>2,762.0</u>	<u>912.1</u>	<u>3,674.1</u>
<b>2006</b>			
Hardware	442.9	0.7	443.6
Global Services	1,899.6	929.5	2,829.1
Software	386.8	-	386.8
Total	<u>2,729.3</u>	<u>930.2</u>	<u>3,659.5</u>

Turnover is supplied from the United Kingdom. Exports are to fellow subsidiary and associated undertakings except for a relatively small amount which is supplied direct to overseas customers. All of these markets are broadly similar.

Hardware includes Servers, from supercomputers to the latest generation Blade servers, Storage and Retail Store Solutions.

IBM Global Services offers customers comprehensive IT services integrated with business insight to reduce costs, improve productivity, and gain competitive advantage. Many client contracts in the UK begin with engagement with the Global Business Services division, where consultants and industry experts provide deep industry knowledge. This division also provides Application Development and Maintenance services. The Global Technology Services division provides a full range of IT services, including managing and operating entire information technology systems, consulting on the best use of technology infrastructure, maintaining systems and Business Continuity and Recovery Services. The Managed Business Process Services unit runs and transforms business processes such as HR or finance and administration for customers.

Software comprises operating systems and middleware which connects operating systems, business processes, and applications seamlessly. UK companies are increasingly seeking to dissolve barriers that impede the flow of information within the enterprise, by deploying open standards-based middleware to integrate their IT systems. Key middleware brands include Tivoli, Lotus, Rational, DB2 and Websphere.

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 3. OPERATING PROFIT

Operating profit is stated after charging/(crediting)

	2007	2006 (restated)
	£m	£m
Amortisation of intangible fixed assets	45.8	61.7
Depreciation of owned fixed assets	100.4	99.3
Loss on disposal of fixed assets	3.6	2.4
Operating lease costs		
Land and buildings	54.9	59.5
Plant and equipment	18.8	19.0
Operating lease income	(18.3)	(13.3)
Finance lease interest income	(1.6)	(2.9)
Exchange differences arising on foreign currency transactions	2.9	(10.7)

#### Audit services

	2007 £000	2006 £000
Audit services in respect of the company's annual accounts	487	477
Other services relating to taxation	87	-
All other services	1,506	1,461
	<u>2,080</u>	<u>1,938</u>
 Audit services in respect of the company's associated pension scheme	 67	 54

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 4. PARTICULARS OF EMPLOYEES

The average number of staff including directors employed by the company during the financial year amounted to

	2007 No	2006 No
Number of services and marketing staff	16,745	16,953
Number of product development staff	1,639	1,590
	<u>18,384</u>	<u>18,543</u>

The aggregate payroll costs of the above were

	2007 £m	2006 £m
Wages and salaries	1,162.8	1,127.4
Social security costs	127.3	120.0
Pension costs (note 19)	131.2	(110.1)
Cost of employee share schemes	13.8	15.0
	<u>1,435.1</u>	<u>1,152.3</u>

Pension costs include £70.6 million (2006 credit £157.7 million) in respect of defined benefit pension schemes, representing amounts charged to operating profit. These amounts do not include amounts credited to finance income (see note 19) and amounts recognised in the statement of total recognised gains and losses in respect of defined benefit pension schemes.

These totals include employees who have fixed-term contracts with the company. They also include 235 employees (2006 242 employees) whose duties were carried out mainly outside the United Kingdom.

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 5. DIRECTORS' EMOLUMENTS

The emoluments of, and the number of stock options and stock appreciation rights, in International Business Machines Corporation, exercised by the directors in respect of their services as directors or otherwise in connection with the management of the company, are shown in the following sections of this note. Those directors whose emoluments, stock options and stock appreciation rights are received exclusively in respect of other duties performed for other subsidiaries of International Business Machines Corporation are accordingly excluded.

The directors' aggregate emoluments in respect of qualifying services were

	2007 £	2006 £
Aggregate emoluments	1,688,605	1,325,440
Contributions to defined contribution schemes	99,520	59,413

	2007 No	2006 No
Number of directors who exercised share options	4	1
Number of directors who received shares in respect of qualifying service under a long term incentive scheme	5	3
Number of directors who accrued benefits under defined benefit scheme	2	4
Number of directors who accrued benefits under defined contribution schemes	3	2

Two directors were appointed during the year and one resigned in the prior year

Aggregate emoluments receivable under long term incentive schemes were £nil (2006 £nil)

#### Emoluments of highest paid director:

	2007 £	2006 £
Aggregate emoluments	459,460	391,250
Accrued pension at the year end in the defined benefit pension scheme	138,865	7,622
Amounts paid, or treated as paid, to a defined contribution scheme in respect of qualifying services	55,194	–

The highest paid director received shares in respect of qualifying service under a long term incentive scheme during 2007 and 2006

The highest paid director exercised share options during 2007 and 2006

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 6. PROFIT ON DISPOSAL OF FIXED ASSETS

	2007 £m	2006 £m
Profit on disposal of land and buildings	<u>-</u>	<u>6.8</u>

The profit on disposal in 2006 relates to the sale of land at the North Harbour site

### 7. PROFIT ON SALE OF OPERATION

	2007 £m	2006 £m
Profit on sale of operation	<u>3.0</u>	<u>-</u>

During the year IBM United Kingdom Limited sold its printing division to Infoprint Solutions United Kingdom Limited. The total value of net liabilities transferred was £0.7 million and the related cash consideration was £3.6 million. Costs incurred in the sale of the division were £1.3 million. This sale is not considered material to the financial statements and therefore has not been disclosed as a discontinued operation.

### 8. INTEREST RECEIVABLE AND SIMILAR INCOME

	2007 £m	2006 £m
Fellow subsidiary undertakings	2.1	0.1
Parent undertaking	34.5	41.3
Other interest receivable	0.6	0.2
	<u>37.2</u>	<u>41.6</u>

Interest on amounts owed by parent undertaking and interest bearing amounts owed by fellow subsidiary undertakings are charged at rates based on LIBOR.

### 9. INTEREST PAYABLE AND SIMILAR CHARGES

	2007 £m	2006 £m
Fellow subsidiary undertakings	19.7	29.5
Other interest payable	0.1	1.7
	<u>19.8</u>	<u>31.2</u>

Interest on loans from fellow subsidiary and external undertakings is charged at rates based on LIBOR.

Interest payable and similar charges to fellow subsidiary undertakings include £15.8 million (2006: £13.4 million) of factoring charges.



# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 10. TAXATION ON ORDINARY ACTIVITIES

#### (a) Analysis of charge in the year

	2007 £m	2006 (restated) £m
Current tax		
UK Corporation tax based on the results for the year at 30% (2006 30%)	5.9	-
Adjustments relating to prior years	(2.9)	3 5
Total current tax	3.0	3 5
Deferred tax (note 16)		
Origination and reversal of timing differences	(14.1)	95 8
Adjustments relating to prior years	(5.3)	(9 8)
Total deferred tax	(19.4)	86 0
Tax (credit)/charge on profit on ordinary activities	(16.4)	89 5

#### (b) Factors affecting current tax charge

The tax assessed on the profit on ordinary activities for the year is lower (2006 lower) than the standard rate of corporation tax in the UK of 30% (2006 30%)

	2007 £m	2006 (restated) £m
Profit on ordinary activities before taxation	168.8	444 5
Profit on ordinary activities multiplied by the standard rate of tax of 30% (2006 30%)	50.6	133 3
Effects of		
Expenses not deductible for tax purposes	4.9	3 7
Accelerated capital allowances	27.0	28 3
Other timing differences	(76.6)	(165 3)
Adjustments to tax charge in respect of previous periods	(2.9)	3 5
Total current tax (note 10(a))	3.0	3 5

#### (c) Factors that may affect future tax charges

The standard rate of Corporation Tax in the UK was changed to 28% with effect from 1 April 2008

During the year as a result of the change in UK Corporation Tax rates deferred tax balances have been re-measured. Deferred tax relating to temporary differences which are expected to reverse prior to 1 April 2008 is measured at 30% and deferred tax relating to temporary differences expected to reverse after 1 April 2008 is measured at the tax rate of 28% as these are the tax rates that will apply on reversal.

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

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### 11. INTANGIBLE FIXED ASSETS

	Goodwill £m
<b>COST</b>	
At 1 January 2007 and 31 December 2007	<u>310.9</u>
<b>AMORTISATION</b>	
At 1 January 2007	265.1
Charge for the year	<u>45.8</u>
At 31 December 2007	<u>310.9</u>
<b>NET BOOK VALUE</b>	
At 31 December 2007	<u>-</u>
At 31 December 2006	<u>45.8</u>

Goodwill on the acquisition of the Informix database software business and the PricewaterhouseCoopers Consulting business was being amortised evenly over the directors' estimate of its useful economic life of five years

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 12. TANGIBLE FIXED ASSETS

	Land and buildings £m	Plant and machinery £m	Fixtures and fittings £m	Total £m
<b>COST</b>				
At 1 January 2007	123.7	604.1	184.9	912.7
Additions	8.3	62.0	15.5	85.8
Disposals	—	(47.7)	(5.2)	(52.9)
Reclassification	(27.0)	—	27.0	—
Transfers	—	(11.0)	—	(11.0)
<b>At 31 December 2007</b>	<b><u>105.0</u></b>	<b><u>607.4</u></b>	<b><u>222.2</u></b>	<b><u>934.6</u></b>
<b>DEPRECIATION</b>				
At 1 January 2007	57.6	401.7	99.3	558.6
Charge for the year	5.0	82.2	13.2	100.4
On disposals	(0.5)	(46.6)	(5.2)	(52.3)
Transfers	—	(8.0)	—	(8.0)
<b>At 31 December 2007</b>	<b><u>62.1</u></b>	<b><u>429.3</u></b>	<b><u>107.3</u></b>	<b><u>598.7</u></b>
<b>NET BOOK VALUE</b>				
<b>At 31 December 2007</b>	<b><u>42.9</u></b>	<b><u>178.1</u></b>	<b><u>114.9</u></b>	<b><u>335.9</u></b>
At 31 December 2006	<u>66.1</u>	<u>202.4</u>	<u>85.6</u>	<u>354.1</u>

Transfers relate to assets transferred to and from fellow subsidiary undertakings

Reclassification relates to building improvements which were included in land and buildings during work in progress and transferred to fixtures and fittings when capitalised

The net book value of land and buildings relates entirely to freehold assets

Plant and machinery includes assets rented to lessees under operating leases. The capital value of these assets is £38.2 million (2006: £43.2 million) and the accumulated depreciation is £20.8 million (2006: £18.5 million).

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 13. PURCHASE OF BUSINESS

During the year the company acquired the trade and associated assets and liabilities of fellow subsidiary undertakings MRO Software UK Limited, FileNet Limited, Softek Storage Systems UK Limited, Vallent Software Systems UK, Internet Security Systems Limited and Watchfire Limited. The transfers of assets and liabilities were at net book value.

The impact of this is set out in the table below

	£m
Tangible fixed assets	0.6
Debtors due within one year	20.0
Cash	16.0
Creditors due within year	(32.2)
Corporation tax	(0.8)
Creditors due more than one year	(0.9)
Provisions for liabilities	(0.3)
Total net assets acquired at book value	<u>2.4</u>

### 14. STOCK

	2007 £m	2006 £m
Raw materials and consumables	–	0.2
Finished goods and goods for resale	8.0	12.8
	<u>8.0</u>	<u>13.0</u>

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 15. DEBTORS

Debtors due within one year

	2007	2006
	£m	£m
Trade debtors	8.3	47.0
Amounts owed by parent undertakings	625.1	585.8
Amounts owed by fellow subsidiary undertakings	694.7	574.8
Amounts recoverable on contracts	26.4	17.5
Deferred tax (note 16)	47.3	-
Net investment in finance leases	13.0	11.6
Other debtors	86.7	76.2
Prepayments and accrued income	263.2	216.2
	<u>1,764.7</u>	<u>1,529.1</u>

Debtors due after more than one year

	2007	2006 (restated)
	£m	£m
Deferred tax (note 16)	187.6	194.4
Net investment in finance leases	11.5	13.8
	<u>199.1</u>	<u>208.2</u>

Amounts owed by parent undertakings are interest bearing (note 8)

Included within amounts owed by fellow subsidiary undertakings is £96.3 million (2006 £34.3 million) of amounts held on short term deposit. This is shown within management of liquid resources in the cash flow statement and the notes to the statement of cash flows (note 29).

IBM United Kingdom Limited has entered into an agreement under which it sells for cash certain of its trade receivables to IBM United Kingdom Financial Services Limited ("the factor"), a fellow subsidiary undertaking, based in Portsmouth, of International Business Machines Corporation. The terms of the agreement preclude the repurchase of any trade receivables which have been sold to the factor. Any losses incurred in the collection of the debt sold under this agreement are not borne by the company. These trade receivables totalling £200.0 million (2006 £187.1 million) have been excluded from the balance sheet in accordance with FRS 5 Reporting the Substance of Transactions.

Assets purchased by the company for supply to customers under finance leases totalled £6.1 million in the year (2006 £9.3 million).

The 2006 deferred tax has been restated to reflect the change in accounting policy for FRS 20 Share Based Payments.

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 16. DEFERRED TAXATION

The deferred tax asset comprises

	2007	2006 (restated)
	£m	£m
Capital allowances	142.1	109.5
Other timing differences	92.8	84.9
Total asset (note 15)	234.9	194.4
Deferred tax liability on pension asset (note 19)	(117.0)	(7.4)
	<u>117.9</u>	<u>187.0</u>

	2007 £m
At 1 January 2007 as previously reported	189.2
Prior year adjustment – FRS 20	(2.2)
At 1 January 2007 as restated	187.0
Profit and loss account movement arising during the year	19.4
Amount charged to statement of total recognised gains and losses	(88.5)
Provision at end of year including deferred tax on pension asset	<u>117.9</u>

Deferred taxation not recognised in the financial statements amounts to £nil (2006 £60.1 million)

### 17. CREDITORS: Amounts falling due within one year

	2007 £m	2006 £m
Trade creditors	167.0	194.5
Amounts owed to fellow subsidiary undertakings	566.0	517.1
Corporation tax	18.9	17.0
Other taxation and social security	152.9	141.7
Accruals and deferred income	446.0	432.5
	<u>1,350.8</u>	<u>1,302.8</u>

Included in amounts owed to fellow subsidiary undertakings is £31.6 million (2006 £43.6 million) which is interest bearing (note 9)

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 18. CREDITORS: Amounts falling due after more than one year

	2007	2006
	£m	£m
Accruals and deferred income	<u>56.8</u>	<u>42.5</u>

### 19. PENSIONS

#### Details and Valuation of Pension Plans

Employees of the company are eligible to join one of the IBM contributory pension plans that are administered separately from the company. The assets of the plans, which comprise both defined benefit and defined contribution sections, are held in trust funds. The cost of the defined benefit sections of the Plans is assessed in accordance with the advice of an independent qualified actuary. Employees who have joined the company after January 1997 are eligible to become members of the defined contribution section of the main plan.

Actuarial valuations of the IBM Pension Plan ('Main Plan') and the IBM IT Solutions Pension Scheme ('I Plan') are carried out every three years. The most recent valuations as at 31 December 2006 were carried out by an independent qualified actuary during 2007 using the projected unit credit method. The market value of the assets of the defined benefit sections of these plans as at this date was £5,590 million which was expected to cover 105.3% of the accrued liabilities after allowing for future increases in salaries.

The Trustees of the Main and I Plans have agreed with the company a schedule of contributions for each of the Plans that sets out the amount of the company's annual contributions from January 2008, following the formal valuations of the Plans at 31 December 2006. Under the agreed schedules the company is making contributions at a rate of 20.6% of pensionable earnings to the Defined Benefit section of the Main Plan, and 16.4% of pensionable earnings and £0.5 million per month to the I Plan. The Trustee and International Business Machines Corporation have signed a deed whereby International Business Machines Corporation has agreed to pay or procure payment of the contributions shown in the schedules in the event that the company fails to do so.

The main assumptions used for this valuation were as follows:

Return on investments	
- pre-retirement	7.30%
- post-retirement	5.10%
Salary increases	3.90%
Pension increases	
- service after 5 April 2005	2.20%
- service between 6 April 1997 and 5 April 2005	2.90%
- service before 6 April 1997 (up to 6 April 2010)	1.74%
- service before 6 April 1997 (from 6 April 2011)	1.45%
Price inflation	2.90%

Changes were made to the Defined Benefit sections of the Pension Plans in 2006 to help control and stabilise the future costs of the Plans. Under these changes, salary increases received by members who elected to stay in the defined benefit sections may not be fully pensionable, increases to pensions paid to retirees in respect of years of service prior to 1997 were agreed with the Trustee for the next fifteen years, and a number of members of the Defined Benefit sections elected to transfer to an enhanced defined contribution section of the Plan for future service.

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 19. PENSIONS *(continued)*

FRS 17 Retirement Benefits requires the recognition of the costs of providing pension benefits in the period in which they are earned, and the recognition of the finance costs and changes in the values of assets and liabilities in the period in which they arise

The operating charge/(credit) in the accounts on this basis is as follows

	2007 £m	2006 £m
Defined Benefit Sections	(32.7)	(247.7)
Defined Contribution Sections	60.6	47.6
Operating charge/(credit)	<u>27.9</u>	<u>(200.1)</u>

The current service cost of the closed defined benefit sections will increase under the projected unit credit method as members of these sections approach retirement, although this increase will be limited by the fact that the number of active members of these sections is declining and their share of the total salary roll is falling

The company contributed a total of £104.9 million (2006 £640.3 million) to all the Pension and Post-Retirement Benefits Plans to which its employees and retirees belonged in 2007

A qualified independent actuary carried out a review of the Main and I Plans based on the following assumptions

	2007	2006	2005
Rate of increase in salaries	4.20%	3.90%	3.70%
Rate of increase to pensions in payments			
- accrued before 6 April 1997	1.92%	1.74%	1.89%
- accrued between 5 April 1997 and 5 April 2005	3.20%	2.90%	2.70%
- accrued after 5 April 2005	2.30%	2.50%	2.50%
Rate of increase to pensions in deferment	3.20%	2.90%	2.70%
Discount rate	5.75%	5.00%	4.75%
Inflation assumption	3.20%	2.90%	2.70%



# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 19. PENSIONS *(continued)*

The value of the assets and liabilities and the long term expected rates of return applied in this review were as follows

	2007 Rate of return	2007 Value £m	2006 Rate of return	2006 Value £m	2005 Rate of return	2005 Value £m
Equities	8.0%	3,559.1	7.8%	3,704.1	7.9%	3,202.8
Bonds	5.1%	1,934.8	4.6%	1,520.7	4.2%	1,197.2
Property	6.6%	332.3	6.1%	352.9	6.2%	272.0
Other	5.1%	(5.1)	4.4%	9.6	4.2%	26.4
Total market value of assets		5,821.1		5,587.3		4,698.4
Present value of scheme liabilities		(5,403.1)		(5,562.5)		(5,691.2)
Surplus/(deficit) in scheme		418.0		24.8		(992.8)
Related deferred tax		(117.0)		(7.4)		297.9
Net pension asset/(liability)		301.0		17.4		(694.9)

The deferred tax asset that arose on the deficit in the scheme in 2005 was recognised to the extent that there was persuasive and reliable evidence that it could be realised

The following charges relating to the defined benefit sections of the pension plans have been recognised in the financial statements

#### Analysis of amounts charged to operating profit in respect of defined benefit schemes:

	2007 £m	2006 £m
Current service cost	68.8	92.8
Past service cost/(credit)	1.8	(250.5)
Total operating charge/(credit)	70.6	(157.7)

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 19. PENSIONS *(continued)*

#### Analysis of the amount credited to other finance income:

	2007 £m	2006 £m
Expected return on pension scheme assets	(378.6)	(349.4)
Interest on pension scheme liabilities	275.3	259.4
Net gain	<u>(103.3)</u>	<u>(90.0)</u>

#### Statement of total recognised gains and losses

	2007 £m	2006 £m
Actual less expected return on pension scheme assets	(1.4)	121.1
Experience gains and (losses) arising on the scheme liabilities	74.7	(3.8)
Gain on change in assumptions underlying the scheme liabilities	242.9	59.9
Gain recognised in statement of total recognised gains and losses	<u>316.2</u>	<u>177.2</u>

#### Movements in surplus/(deficit) during the year

	2007 £m	2006 £m
Surplus/(deficit) in scheme at beginning of year	24.8	(992.8)
Movement in year		
Current service cost	(68.8)	(92.8)
Defined Benefit contributions	44.3	592.7
Past service (costs)/credit	(1.8)	250.5
Other finance income	103.3	90.0
Actuarial gain	316.2	177.2
Surplus in scheme at the end of the year	<u>418.0</u>	<u>24.8</u>

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 19. PENSIONS *(continued)*

#### Details of experience gains and losses:

	2007	2006	2005	2004	2003
Actual less expected return on pension scheme assets (£m)	(1.4)	121.1	473.1	153.4	288.8
Percentage of scheme assets	0%	2.2%	10.1%	3.9%	8.0%
Experience gain/(loss) on scheme liabilities (£m)	74.7	(3.8)	91.5	(115.4)	(21.8)
Percentage of scheme liabilities	1.4%	(0.1)%	1.6%	(2.0)%	0%
Total gain/(loss) recognised in statement of recognised gains and losses (£m)	316.2	177.2	159.0	(272.3)	133.3
Percentage of scheme liabilities	5.9%	3.2%	2.8%	(5.0)%	3.0%

### 20. OTHER PROVISIONS

#### Restructuring provision

	£m
At 1 January 2007	38.1
Transfer to/from profit and loss account	16.0
Acquired during the year	0.3
Increase due to acquired leases	14.3
Utilised during the year	(29.3)
At 31 December 2007	<u>39.4</u>

Provision has been made for the consolidation of the company's property portfolio and the rebalancing of the workforce. These provisions are expected to be utilised over the next three years.

During the year IBM United Kingdom Limited increased its restructuring provision by £14.3 million in respect of the Woking and Windsor sites which were acquired as part of the purchase of business of MRO Software UK Limited and Internet Security Systems Limited respectively. This has been charged directly to a related undertaking under the terms of the purchase of business agreement.

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 21. SHARE-BASED PAYMENTS

Share-based incentive awards are provided to employees under the terms of the company's plans. All plans are for shares in the company's ultimate parent undertaking, International Business Machines Corporation.

During the year the company recognised total expenses, excluding deferred tax, of £13.8 million (2006: £15.0 million) related to equity-settled share-based payment transactions.

#### Share options

Share Options are awards which allow the employee to purchase shares of International Business Machines Corporation at a fixed price. They are granted at an exercise price equal to or greater than the company stock price at the date of the grant. These awards, which generally vest 25 percent per year, are fully vested four years from the date of grant and have a contractual term of 10 years.

Details of the number of share options and the weighted average exercise price outstanding during the year are as follows:

	2007		2006	
	Number	Weighted average exercise price	Number	Weighted average exercise price
	('000)	£	('000)	£
Outstanding at the beginning of the year	10,225	47.27	11,606	53.02
Granted during the year	46	51.39	77	45.14
Forfeited during the year	(81)	48.44	(248)	46.90
Exercised during the year	(2,478)	38.76	(1,015)	31.83
Expired during the year	(221)	49.95	(353)	54.73
Transferred during the year	10	45.66	158	42.33
Outstanding at the end of the year	<u>7,501</u>	<u>48.72</u>	<u>10,225</u>	<u>47.27</u>
Exercisable at the end of the year	<u>6,840</u>	<u>48.73</u>	<u>8,528</u>	<u>47.30</u>

Options transferred during the year relate to employees assigned to and from other countries.

The weighted average share price at the date of exercise for share options exercised during the year was £52.88 (2006: £45.45).

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 21. SHARE-BASED PAYMENTS *(continued)*

Range of exercise prices	Weighted average exercise price	2007		Weighted average exercise price	2006	
		Number of shares ('000)	Weighted average remaining life: contractual		Number of shares ('000)	Weighted average remaining life: contractual
£10-£30	£25.78	129	0.18	£24.31	441	0.93
£31-£40	£36.95	1,859	5.01	£37.06	3,132	5.90
£41-£50	£48.32	2,927	5.41	£48.13	3,799	6.06
£51+	£58.78	2,586	2.68	£59.61	2,853	3.69
		<u>7,501</u>			<u>10,225</u>	

Share options are granted at various intervals throughout the course of the financial year. The grant date fair value of share options is calculated using the Black Scholes option pricing model. Key inputs and assumptions used to estimate the fair value of share options include the grant price of the award, the expected option term, volatility of the ultimate parent's shares, the risk-free rate and the company's dividend yield. Where relevant, the expected life used in the model has been adjusted based on management's best estimate of the effects of non-transferability, exercise restrictions and behavioural considerations. Expected volatility is based on the historical volatility of the ultimate parent entity's share price. The inputs into the pricing model were as follows:

	2007	2006
Weighted average share price	£51.39	£45.14
Weighted average exercise price	£51.39	£48.93
Expected volatility	23.15%	26.39%
Expected life - years	5	5
Risk free rate	4.51%	4.87%
Expected dividends	<u>0.20</u>	<u>-</u>

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 21. SHARE-BASED PAYMENTS *(continued)*

#### Share awards

In addition to share options the company grants its employees share awards. These awards are made in the form of Restricted Stock Units (RSUs). RSUs are share awards that are granted to employees and entitle the holder to shares of International Business Machines Corporation's common stock as the award vests, typically over a two-to-five year period. The fair value of the award is determined and fixed on the grant date based on the company's share price.

Details of the number of RSU's outstanding during the year are as follows:

	2007 Number (‘000)	2006 Number (‘000)
Outstanding at the beginning of the year	630	554
Granted during the year	262	246
Forfeited during the year	(38)	(57)
Exercised during the year	(243)	(124)
Transferred during the year	30	11
Outstanding at the end of the year	<u>641</u>	<u>630</u>

RSU's transferred during the year relate to employees assigned to and from other countries. The weighted average fair value of RSU's granted during the year was £51.72 (2006: £43.54).

#### Employees Stock Purchase Plan

The company maintains an Employees Stock Purchase Plan (ESPP). The ESPP enables eligible participants to purchase full or fractional shares of International Business Machines Corporation through payroll deductions at a 5% deduction off fair value.

The company incurs recharges from International Business Machines Corporation in respect of share based payments which are settled on a cash basis. There is an intercompany liability of £49.8 million (2006: £49.9 million) recognised in creditors falling due within one year to reflect the amount estimated that IBM United Kingdom Limited will pay on the exercise of share options. This is calculated as the difference between the exercise price and market price for shares at the balance sheet date on the options which have vested and are exercisable and in the money at that date.

### 22. FINANCIAL COMMITMENT

In October 2006 IBM United Kingdom Limited introduced a 12 month forward rolling hedging programme to hedge a proportion of its US dollar costs arising from transactions with both related companies and suppliers. At the year end the fair value of the liability was £1.9 million (2006: £1.4 million). The amount recognised in the profit and loss account in the year on the closed foreign currency forward exchange contracts was a loss of £5.2 million (2006: £nil).

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 23. COMMITMENTS UNDER OPERATING LEASES

At 31 December 2007 the company had annual commitments set out below

	2007		2006	
	Land & Buildings £m	Other Items £m	Land & Buildings £m	Other Items £m
Operating leases which expire				
Within 1 year	2.6	2.7	1.9	1.9
Within 2 to 5 years	20.3	12.1	16.0	12.8
After more than 5 years	35.1	-	42.0	-
	<u>58.0</u>	<u>14.8</u>	<u>59.9</u>	<u>14.7</u>

### 24. CONTINGENT LIABILITIES

The company has contingent liabilities in respect of bank and contractual performance guarantees and other matters arising in the normal course of business. No material liability is expected to arise in respect of these arrangements.

### 25. RELATED PARTY TRANSACTIONS

Transactions with other companies within the group are not disclosed in accordance with FRS 8 'Related Party Disclosures' as the consolidated accounts of International Business Machines Corporation in which the company is included are available at the address shown in note 30.

### 26. SHARE CAPITAL

#### Authorised share capital:

	2007 £m	2006 £m
1,000,000,000 Ordinary shares of £1 each	<u>1,000.0</u>	<u>1,000.0</u>

#### Allotted and called up:

	2007		2006	
	No	£m	No	£m
Ordinary shares of £1 each	<u>956,427,000</u>	<u>956.4</u>	<u>956,427,000</u>	<u>956.4</u>

# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 27. RESERVES

	Share premium account £m	Share options reserve £m	Profit and loss account £m
At 1 January 2007 as previously reported	277.9	53.3	(467.2)
Prior year adjustment FRS 20	—	(51.4)	49.2
At 1 January 2007 as restated	277.9	1.9	(418.0)
Retained profit for the financial year	—	—	185.2
Actuarial gain on pension scheme	—	—	316.2
Movement on deferred tax relating to pension asset	—	—	(88.5)
Adjustment in respect of employee share schemes	—	(40.8)	—
Transfer to profit and loss reserve	—	38.9	(38.9)
At 31 December 2007	277.9	—	(44.0)

Included within the adjustment in respect of employee share schemes is a £54.5 million recharge from International Business Machines Corporation on the exercise of options in the year, £13.8 million charge for share based payments and £0.1 million movement in the intercompany liability for share options

### 28. RECONCILIATION OF MOVEMENTS IN SHAREHOLDERS' FUNDS

	2007 £m	2006 (restated) £m
Retained profit for the financial year	185.2	355.0
Actuarial gain on pension scheme	316.2	177.2
Movement on deferred tax relating to pension asset	(88.5)	(53.2)
Adjustment in respect of employee share schemes	(40.8)	(25.5)
Net addition to shareholders' funds	372.1	453.5
Opening shareholders' funds as previously reported	820.4	355.6
Prior year adjustment FRS 20	(2.2)	9.1
Opening shareholders' funds as restated	818.2	364.7
Shareholders' funds as at 31 December 2007	1,190.3	818.2



# IBM United Kingdom Limited

## Notes to the Financial Statements

Year Ended 31 December 2007

### 29. NOTES TO THE STATEMENT OF CASH FLOWS

#### RECONCILIATION OF OPERATING PROFIT TO NET CASH INFLOW/(OUTFLOW) FROM OPERATING ACTIVITIES

	2007	2006 (restated)
	£m	£m
Operating profit	45.1	337.3
Amortisation	45.8	61.7
Depreciation	100.4	99.3
Loss on disposal of fixed assets	3.6	2.4
Difference between pension charge and contributions	26.3	(750.4)
Decrease/(increase) in stocks	4.8	(2.9)
(Increase)/decrease in debtors	(38.6)	64.1
Decrease in creditors	(4.5)	(25.0)
Increase/(decrease) in provisions	1.0	(20.1)
Movement on share option reserve (FRS 20)	(40.8)	(25.5)
Net cash inflow/(outflow) from operating activities	<u>143.1</u>	<u>(259.1)</u>

Included in net cash inflow/(outflow) from operating activities is £104.9 million (2006 £640.3 million) relating to cash paid in respect of pension contributions (note 19)

#### RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET DEBT

	2007	2006
	£m	£m
(Decrease)/increase in cash in the period	(5.4)	31.4
Increase/(decrease) in liquid resources	<u>62.0</u>	<u>(185.4)</u>
Change in net debt	<u>56.6</u>	<u>(154.0)</u>
Net debt at 1 January 2007	<u>68.3</u>	<u>222.3</u>
Net debt at 31 December 2007	<u>124.9</u>	<u>68.3</u>

#### ANALYSIS OF CHANGES IN NET DEBT

	Cash	Liquid resources	Net funds
	£m	£m	£m
At 1 January 2007	34.0	34.3	68.3
Movements in liquid resources	–	62.0	62.0
Cash acquired with purchase of businesses	16.0	–	16.0
Cash utilised by the business	(21.4)	–	(21.4)
At 31 December 2007	<u>28.6</u>	<u>96.3</u>	<u>124.9</u>

# **IBM United Kingdom Limited**

## **Notes to the Financial Statements**

**Year Ended 31 December 2007**

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### **30. ULTIMATE PARENT COMPANY**

The company's immediate parent undertaking is IBM United Kingdom Holdings Limited which holds 89% of the shares and is registered in Great Britain

The company's ultimate parent undertaking and controlling party is International Business Machines Corporation which is incorporated in the United States of America and is the parent undertaking of the smallest and largest group to consolidate these financial statements. Copies of the accounts of this undertaking may be obtained from IBM Corporate Headquarters, New Orchard Road, Armonk, New York 10504