

**In 2007, ARM
was at the
heart of around
a quarter of
all electronic
devices sold
in the world**



ARM – The Architecture for the Digital World®

ARM provided microprocessor and physical IP designs that were used in around a quarter of all electronic devices* sold in 2007. Because our designs offer better performance, better energy efficiency and can increase design reliability, ARM has become the architecture of choice for silicon chips. The familiarity of chip and software engineers in ARM technology combined with ARM's investment in software, tools and an ecosystem of developers, has fuelled the growth of ARM® technology-based designs.

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*"Electronic devices" includes any device which may contain digital chips with an embedded microprocessor such as audio headsets, automotive vehicles, digital still cameras, digital storage devices such as USB memory sticks, digital TVs, discrete microcontrollers, DVD recorders and players, IP network routers and switches, mobile phones such as smartphones, feature phones and low-cost voice phones, portable media players, printers, set-top boxes, smartcards, desk-top PCs, laptops and mobile computers, some programmable whitegoods such as washing machines and dishwashers, and also video recorders. We do not include simple electrical devices that are unlikely to contain digital chips with an embedded microprocessor such as analogue telephones, lawn mowers, light-bulbs, powered hand-tools, torches, and some whitegoods such as ovens and fridges. Nor do we include digital storage such as optical media, or discrete memory chips.

But this is just the beginning of our journey...

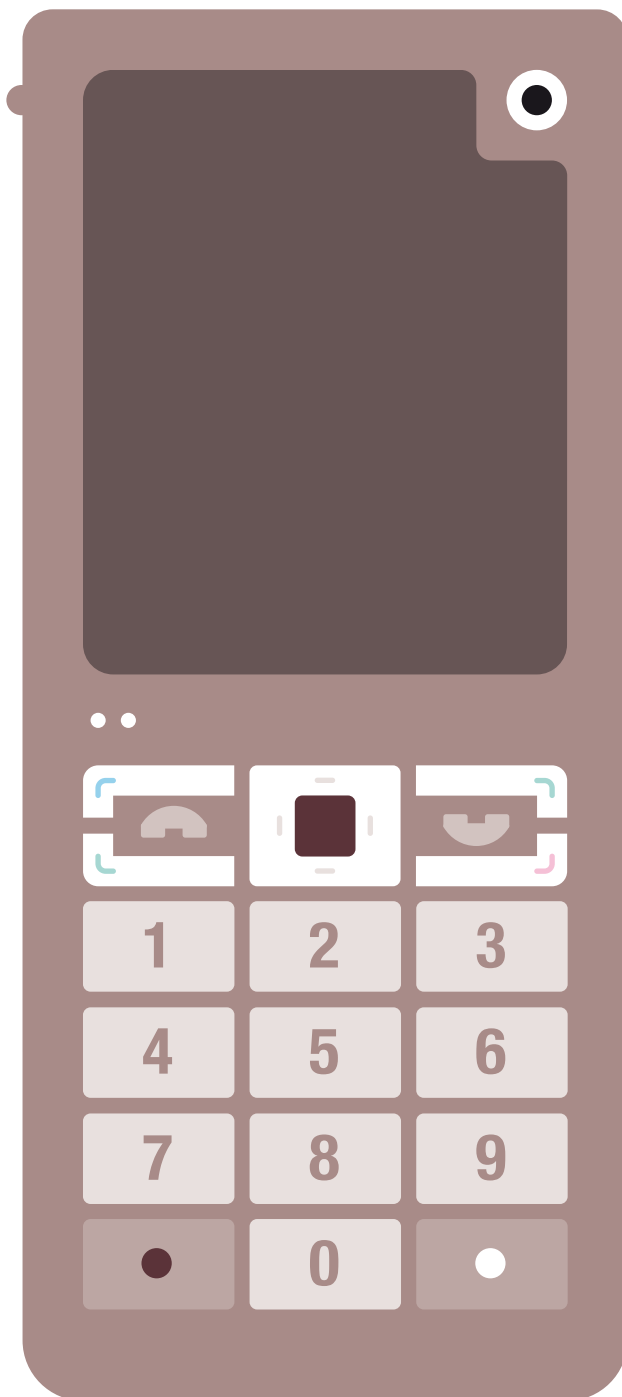
Business highlights

- Dollar revenue growth at twice the semiconductor industry rate
- Strong licensing and royalty momentum in the Processor Division; units shipped up 18%
- Cortex™ family uptake has been the fastest in ARM's history; 37 licenses since launch in 2005
- Physical IP business better positioned to capitalise on long-term growth opportunities; started 32nm R&D
- Record bookings quarter in Q4; backlog at highest ever level up 24%
- £147 million cash returned to shareholders
- 100% increase recommended to 2007 total dividend to 2.0 pence per share

**Because most
new mobile
phones need
more than one
microprocessor...**

**We are increasing ARM's value
in every new mobile phone.**

In 2007, two billion ARM technology-based chips were shipped in mobile phones – that's an average of 1.7 per phone. Since 2003, the ARM value per mobile phone has increased by nearly 50% and continues to rise as all phones become more and more sophisticated.



Functionality



Camera



Text



Browse



Music



Games



Headphones



GPS

**Because fewer
than 25% of
the world's
processors are in
mobile phones...**

**And the growth in “intelligent”
products is growing rapidly to
meet consumer demand.**

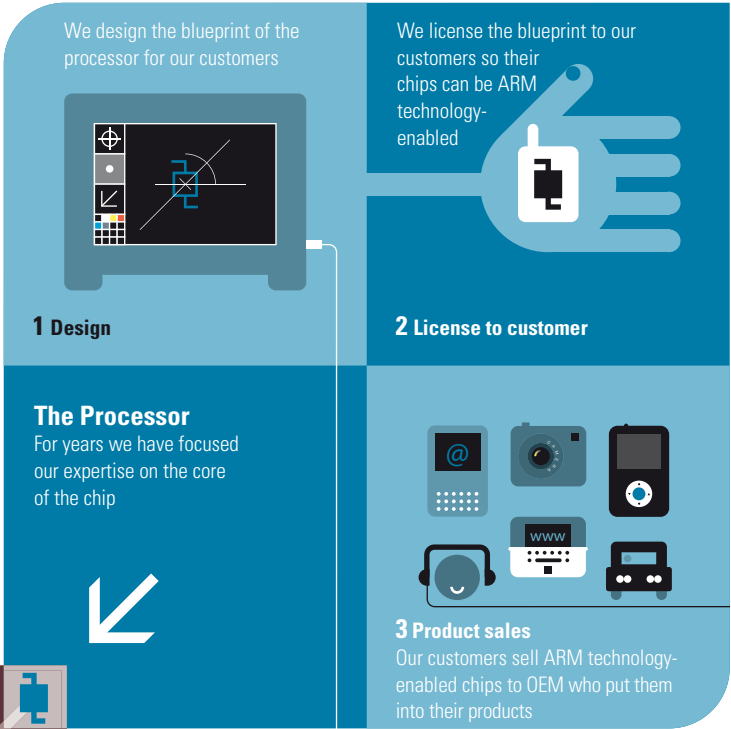
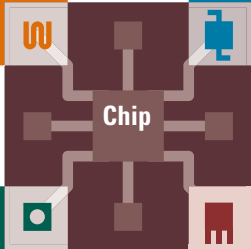
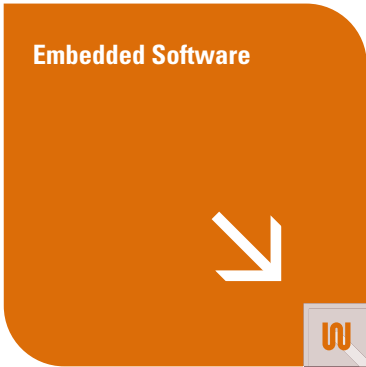
For consumer products to be easier to use, safer and more energy efficient, they need to become smarter. Washing machines, airbags, televisions, toys, cameras, printers, etc., all need advanced chips to make them smart. Many of these products are already using ARM technology-based chips and we believe that this trend will be a source of future royalty revenue.



Because we plan to grow our share of the chip...

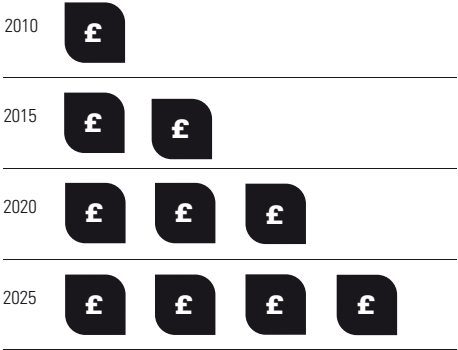
We are recreating our successful processor business model in other aspects of chip design.

As the design of computer chips becomes more complex, semiconductor companies are looking to out-source more of their design work. The next trend is for physical IP to be out-sourced. ARM is well placed to provide advanced physical IP designs on the latest manufacturing processes.

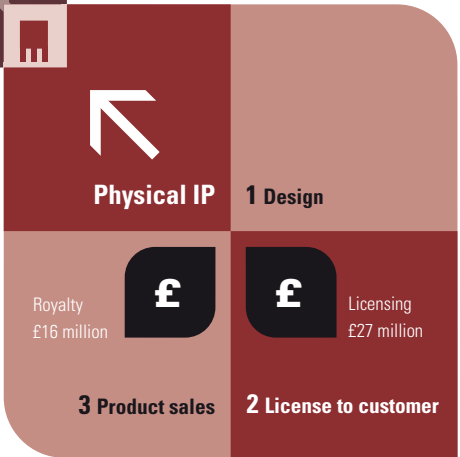


Last year we received £83 million in processor license fees

4 Royalty income
We receive a royalty payment every time one of these products is sold. Last year we received £88 million in processor royalty fees

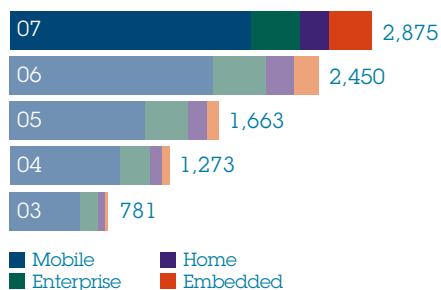


5 Ongoing growth
Each processor design can have a life of 25 years so we receive ongoing royalties

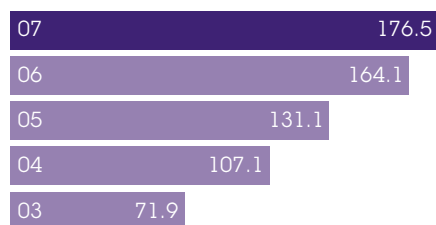


Business highlights

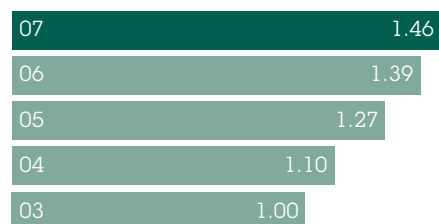
Royalty unit split (millions of units)



Processor Division royalty revenue (\$m)



ARM value in mobile phone market* (indexed to 2003 levels)



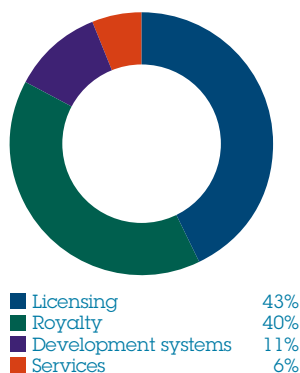
* Source: Gartner, ARM estimates
ARM Value = Average ARM royalties per handset/Average selling price per handset

Physical IP licensing per node (%)

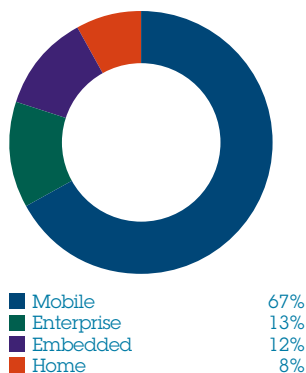


ARM acquired Artisan and established Physical IP Division in late 2004.

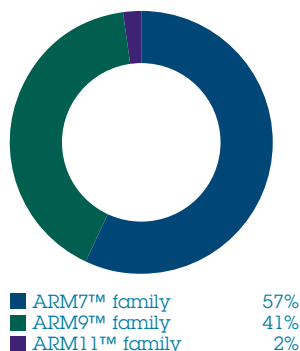
Revenue analysis (%)



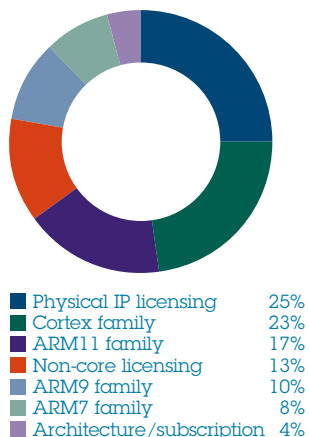
Processor Division royalty units (%)



Royalty units by family (%)



License revenues by product (%)





2007 was another successful year for ARM and we entered 2008 with the Group order backlog at its highest-ever level, the physical IP business better positioned to capitalise on the long-term growth opportunity, and good royalty revenue momentum based on the continuing proliferation of ARM technology into an ever-broader range of digital devices.

Results and dividend

The increasingly widespread adoption of ARM technology in consumer electronic devices was illustrated in 2007 by the 18% increase in the reported total shipments of ARM Powered® products to 2.90 billion units, up from the reported 2.45 billion units in 2006. ARM's strong financial performance continued in 2007 with dollar revenue growth of 6% to \$514.3 million and a 24% increase in the year-end order backlog compared to 2006.

Strong cash generation over several years has enabled us to invest in research and development, to make acquisitions of businesses with complementary technology and to return cash to shareholders through dividends and the share buyback programme. The board is recommending a final dividend of 1.2 pence per share, bringing the total for the year to 2.0 pence per share, an increase of 100% over the dividend paid in respect of 2006.

"We see a return of cash to shareholders through dividends as part of a package of measures to make the best use of the business's cash resources and we plan to continue the rolling share buyback programme initiated in July 2005."

We see a return of cash to shareholders through dividends as part of a package of measures to make the best use of the business's cash resources and we plan to continue the rolling share buyback programme initiated in July 2005. During 2007 we purchased a total of 94.5 million shares at a total cost of £128.6 million.

The market

We were pleased with ARM's performance in 2007 against a backdrop of slower growth in the semiconductor industry. Full-year dollar revenue growth at approximately twice the rate of the industry, and strong licensing momentum in our Processor Division throughout the year, confirm our continuing market share gains. Although 2007 was a challenging period for revenue in our Physical IP Division, the reallocation of resources during the year towards the development of leading-edge physical IP technology, together with changes to management and organisational focus, positions the business well for growth in 2008.

ARM Partners have shipped more than 10 billion ARM microprocessors since ARM was founded.

"In January 2007, ARM was chosen as European Business of the Year, having been voted UK Business of the Year in 2006. In November 2007, ARM received two further prestigious awards when Warren East was voted UK Business Leader of the Year and ARM was recognised as techMARK Company of the Year. These represent considerable accolades for the Company and recognise the significant efforts of all ARM employees worldwide."

Geographic expansion

In 2007, ARM continued to strengthen its position as a global entity across all regions. In the year, 42% of revenue arose from customers in North America, 41% from the Asia Pacific region and 17% from Europe. Royalties from China-based chip designers increased by 27%, with seven new licenses signed with design teams in China during the year.

People

2007 has been a year of growth with consolidation and simplification, building on the investments in businesses and employees during 2006. I thank all employees worldwide for the contribution they have each made to the progress achieved by ARM in 2007 in the increasingly demanding market in which we operate. At 31 December 2007 we had 1,728 full time employees compared to 1,659 at the end of 2006. Of these 650 are based in the UK, 523 in the US, 190 in Continental Europe, 292 in India and 73 in the Asia Pacific region.

Board changes

As previously announced, we were very pleased to welcome Young Sohn as an independent non-executive director on 2 April 2007. He has extensive experience in the semiconductor industry both in Silicon Valley and in Asia. A more detailed biography is included on page 23. He was appointed to the Audit and Remuneration Committees with effect from 15 May 2007. Peter Cawdron, who had been an independent non-executive director since 1998, retired from the board as planned at the Annual General Meeting (AGM) on 15 May 2007. The board is indebted to Peter for the excellent contribution he has made over the past nine years, in particular as senior independent director and Chairman of the audit committee.



Doug Dunn
Chairman



"ARM has a unique position in the global semiconductor industry. We are the leading intellectual property (IP) provider, designing processor and physical IP and related technology that is used by most of the chip manufacturers in the world."

In last year's annual report, I wrote about the important role that ARM plays in the development of an increasingly digital world. As we celebrate our tenth year as a public company, our goal remains the same as it was a decade ago – to generate returns for our shareholders by providing the technology at the heart of the digital world to the leading semiconductor companies. Today, people's lives are being made easier, safer and more efficient through the increasing use of digital electronics in everyday products.

ARM has a unique position in the global semiconductor industry. We are the leading intellectual property (IP) provider, designing processor and physical IP and related technology that is used by most of the chip manufacturers in the world. As a whole, the industry has annual revenues of nearly \$300 billion and in 2007 grew at about 3%. Over the medium term, because of ARM's position and unique business model, we expect to maintain revenue growth at a multiple of the industry.

ARM is in your mobile phone

ARM technology is at the heart of 90% of the world's mobile phones. In some developing countries low-cost phones can be purchased for as little as \$25, thereby helping to drive the number of subscribers to more than three billion globally. ARM is enabling the technology that allows the wireless communications, the user interface and the audio to run on a single semiconductor chip thus significantly lowering the cost of producing the phone itself.

Mobile phones are becoming an essential everyday device for

increasing numbers of people everywhere, yet billions of people still do not have access to a mobile phone. This number is likely to diminish rapidly as mobile networks expand and cost of the technology reduces, bringing mobile technology to an ever wider audience.

The growing momentum behind more intelligent phones has accelerated in 2007, with the arrival of a new generation of highly sophisticated smartphones that contain even more features, such as graphics, video and connectivity to WiFi and GPS, turning the mobile phone into a mobile internet device (MID). These devices can contain five or more separate ARM products.

Technology in the high-end smartphone quickly spreads into the rest of the market. The average mobile phone is already becoming more feature-rich and personalised. You can now choose your phone based on the camera specifications, audio and video playback quality, gaming, or on design for elegance, coolness or fun – all being enabled by technology from ARM.

Of the 13 billion microprocessor-based chips shipped in 2007, nearly three billion contained ARM processors.

UGOBE PLEO DINOSAUR

The ARM Powered UgoBle Pleo Dinosaur is a robotic dinosaur based on the Camarasaurus. Each one begins life as a newly-hatched baby Camarasaurus and is able to feel hunger and fatigue, sleep, graze, walk about on his own and get urges to explore and be nurtured. Pleo uses two ARM processors: one as a brain, acting as his mind and setting his mood; the other handling video and audio input, i.e. what Pleo sees and hears.



ARM's success in mobile devices has been accelerated through the ecosystem we have developed to remove cost and complexity from the development process. One of the major areas for new product development is the MID. To enable the MID ecosystem, we work with leading semiconductor companies such as Broadcom, Marvell, Qualcomm, Samsung and Texas Instruments to ensure that they can maximise the performance of the ARM processors in their chips. We work with software companies such as Adobe and Microsoft to ensure that their software runs efficiently on ARM technology-based chips. We also work with content providers such as Disney, Google and Electronic Arts so that the end-product, the mobile phone, gives a superb user experience. ARM believes that only through working together with the industry leaders is it possible to create a truly mobile internet. No one company can do this alone.

ARM is in your other digital products

ARM technology is ideally suited to act as the brain of a broad range of electronic devices beyond mobile phones. Since ARM technology can

enable chips that are low cost to develop and consume less power, we are enabling many more products to become "intelligent".

The fastest growing market for ARM is in microcontrollers that go into a wide range of electronic devices from washing machines to air-conditioning units to toys. ARM processors have

In 2007, nearly two billion ARM technology-based chips were shipped inside mobile phones.

been used in microcontrollers for many years, but the recent drive to make household devices more energy efficient has required increased intelligence to be built into many more products in the home. For example, a modern intelligent washing machine can use less than 50% of the energy of an older model. Intelligent lighting systems can save 40% of the energy consumed. With many ARM technology-based chips making the home a more intelligent and efficient place, ARM is seeing its royalty revenue increase as a result.

The use of ARM technology-based chips in cars is increasing. In Europe and the US, most cars sold today already contain at least one ARM processor, probably more. ARM is used in 60% of anti-lock braking systems, 40% of airbags and 40% of intelligent batteries. ARM processors are also used in many other components throughout the car including dashboard display, chassis control and engine management systems. On average, every car sold in 2007 contained 1.6 ARM processors – that is nearly 100 million ARM technology-based chips.

Toys are also becoming increasingly interactive and therefore need the intelligence to be able to respond to their play mates. Ugobe's Pleo dinosaur is a recent example of an autonomous toy that learns, explores and even develops its own personality through interaction with its environment. Pleo has two ARM technology-based chips embedded within it enabling Pleo to think, sense and move.

Physical IP Division – expanding the ARM business model

ARM's physical IP is a key technology that allows the chip's design to be implemented in the manufacturing process. It enables our customers to build low cost, highly-efficient chips.

ARM obtained the Physical IP Division (PIPD) through the acquisition of Artisan at the end of 2004. Prior to acquisition, Artisan mainly provided physical IP to the many small companies that did not have the capability to develop physical IP in-house. ARM's vision for PIPD is

“ARM is one of the great dark horses of computing, hardly known outside the industry yet far outselling Intel in the number of cores sold each year because its designs are used in a wider variety of devices – not least mobile phones, including Apple's iPhone.”

Article: How dark-horse ARM could help Linux and wean Apple off toys

Source: Clive Akass, Personal Computer World Magazine

to extend the market breadth to include ARM's traditional customers – the largest semiconductor manufacturers in the world. These companies are always pushing the boundaries of modern manufacturing capability. This is very expensive and ARM saw the opportunity for them to out-source some of the development of their physical IP.

Over the last three years ARM has evolved the PIPD business and product portfolio to become a viable IP provider to the market leaders. We have developed new technology and products for the latest manufacturing processes for our customers to evaluate. In 2007, we have already seen orders from our target customers and we expect this to accelerate in 2008.

When ARM acquired Artisan we stated that it would take four to seven years before the market-leading semiconductor companies would be regularly licensing physical IP from ARM. We remain on track to achieve this.

The future

After a decade as a public company, ARM is looking forward to the next ten years with confidence. We have established a strong position as a supplier into the large and growing mobile phone industry. We are using that base to develop the business further in the growing number of markets for digital products where intelligence is becoming increasingly important. PIPD is now well positioned to achieve profitable growth as the largest semiconductor companies increasingly look to out-source the development of physical IP. The Company's market-leading position, broad technology portfolio and cash-generative business model make ARM a unique investment opportunity.



Warren East
Chief Executive Officer

There are on average of 1.7 ARM processors per mobile phone.



"We reached a significant milestone in 2007 with our Partners shipping the ten billionth ARM microprocessor since ARM's inception in 1990."

Financial performance in 2007 was pleasing against a backdrop of slower growth in the semiconductor industry, with full-year dollar revenue growth at approximately twice the rate of the industry and strong licensing momentum in our Processor Division. We have also maintained normalised operating margins⁽¹⁾ despite the weakened dollar, grown backlog to a record level and also seen volumes of ARM Powered products increase by 18% to just under three billion units a year.

Performance

The Group's key financial performance indicators include dollar revenue, operating margin and earnings per share. Non-financial key performance indicators include the number of ARM technology-based chips sold and licenses signed. These are discussed as part of this review.

Revenues

Total revenues for the year ended 31 December 2007 amounted to £259.2 million (2006: £263.3 million). In US dollar terms, revenues grew from \$483.6 million in 2006 to \$514.3 million in 2007, an increase of 6%. The actual average dollar exchange rate for ARM in 2007 was \$1.98 compared to \$1.84 in 2006, which had the effect of reducing total reported revenues by approximately £20.7 million based on 2006 rates.

Total licensing revenues in 2007 were £110.7 million, being 43% of total revenues, compared to £110.6 million or 42% of total revenues in 2006. In US dollars, total licensing revenues in 2007 were \$217.9 million compared to \$202.5 million in 2006, an increase of 8%.

Royalty revenues in 2007 were £104.1 million, representing 40% of total revenues in the year, compared to £107.8 million or 41% of total revenues in 2006. Total royalty revenues in US dollars in 2007 were \$208.8 million, up 5% from \$199.0 million in 2006.

Sales of development systems in 2007 were £27.9 million, being 11% of total revenues, compared to £28.8 million, or 11% of total revenues in 2006. Development systems revenues in US dollars were up 5% in 2007 to \$55.6 million from \$53.0 million in 2006. Service revenues, which include consulting services and revenues from support, maintenance and training, were £16.5 million in 2007, representing 6% of total revenues, compared to £16.1 million, or 6% of total revenues in 2006. Service revenues in US dollars were up 10% to \$32.0 million from \$29.1 million in 2006.

Licensing revenues

Total licensing revenues for 2007 were £110.7 million, comprising £83.4 million from the Processor Division (PD) and £27.3 million

Nearly one billion ARM technology-based chips were shipped in non-mobile applications in 2007.

⁽¹⁾ See operating margin section on page 19.

“Integrated multimedia systems have become must-have features in new cars and buyers are shelling out big bucks for being able to talk on a cellphone hands-free or connect their MP3 player in their car. Ford’s Sync has surprised the industry with its simple and effective approach and its price tag may surprise even more... The CPU is based on a 400MHz ARM11 core and hosts Microsoft’s operating system, handles voice recognition and conducts all audio signal processing...”

Article: The Cost Of Ford’s Sync? \$30. Its Value? Priceless. Source: Wolfgang Gruener, TG Daily

from the Physical IP Division (PIPD). In US dollars, PD licensing revenues were \$163.5 million (up 18% on \$138.3 million in 2006) and PIPD was \$54.4 million (down 15% on \$64.2 million in 2006).

PD licensing comprised a rich mix from the ARM7, ARM9 and ARM11 families as well as from the newer technologies in the Cortex family and Mali™ graphics processors. 62 new licenses were signed in 2007, with 23 new companies becoming ARM Partners in the year, bringing the total to 210 at the end of the year. These included 14 licenses to the Cortex family (and three lead Partners for the next-generation Cortex-A9 processor) and three licenses to the Mali graphics processors. In addition, 2007 saw four large semiconductor companies underline their long-term commitment to ARM by signing subscription licenses, allowing them access to a broad range of ARM processor technology over a period of between three and five years.

In 2007, ARM maintained progress in achieving the long-term goal of providing ARM’s physical IP

to leading IDMs and fabless semiconductor companies. Momentum for PIPD’s 65nm products continued to grow with ten new licenses being signed in 2007, bringing the total to 32 65nm licenses signed with 15 companies cumulatively. In total, 68 licenses to PIPD products were signed in 2007, bringing the total number of licenses signed to 350.

Royalty revenues and unit shipments

Total royalty revenues for 2007 were £104.1 million, comprising £88.0 million from PD and £16.1 million from PIPD. Royalties in PD came from record unit shipments of 2.9 billion compared with £88.7 million and 2.45 billion units in 2006. Dollar royalty revenues earned in PD were \$176.5 million, up 8% on 2006 compared with the increase in year-on-year unit shipments of 18%. Average royalty rates (ARR) over the past three years were 6.1 cents in 2007, 6.7 cents in 2006 and 7.9 cents in 2005. The average royalty rate in a given period is based on a number of variables, including the average selling prices of the chips being shipped, the applicable royalty

rate payable to ARM and the mix of unit shipments by ARM product family. Unit volume growth more than compensated for the reductions in ARR and, as all royalty revenue is earned effectively at 100% margin, it represents incremental returns on the development cost of the ARM technology on which the royalty is earned.

ARM unit shipments showed significant resilience in a year that was affected by the industry-wide inventory correction which started in the second half of 2006. The proportion of shipments into the mobile and non-mobile segments during 2007 remained broadly consistent with the proportion of mobile shipments edging up slightly to 67%. The ARM content per phone continued to increase, reaching approximately 1.7 processors per phone by year-end. We continue to see strength in the embedded segment, in part due to the continued significant growth in MCU shipments with growth of 2.4x over 2006. MCUs are now the highest volume individual application after wireless handsets. We also reached

a significant milestone in 2007 with our Partners shipping the ten billionth ARM microprocessor since ARM's inception in 1990.

The total number of Partners shipping ARM technology-based product at the end of 2007 was 89 after taking into account corporate activity within the ARM partnership. 15 companies are paying meaningful royalties for physical IP products at the end of the year.

Gross margin

Gross margins in 2007 were 89.2% compared to 88.3% in 2006. Cost of sales in 2007 includes compensation charges in respect of share-based payments and related payroll taxes of £1.1 million (2006: £1.0 million). Excluding compensation charges in respect of share-based payments and related payroll taxes, gross margins in 2007 were 89.6% (2006: 88.7%).

Operating expenses

Over recent years, ARM has acquired a number of companies giving rise to the recognition of intangible assets other than goodwill. These are amortised over their expected useful lives, with the cost recorded against research and development, sales and marketing or general and administrative expenses as appropriate. In order to aid comparability, these costs have been separately identified as "acquisition-related charges" in the narrative below. In addition, the issuance of ARM share-based remuneration to employees of the Group gives rise to non-cash share-based compensation charges. These are also separately identified in the narrative below.

Total net operating expenses in the 12 months to 31 December 2007 were £191.4 million compared to £183.1 million in 2006. Operating expenses

AGEIA PHYSX PHYSICS PROCESSOR

ARM physical IP is used in high-performance graphics engines. Realtime physics simulation is the new big thing in PC gaming.

- Explosions that cause dust and collateral debris.
- Characters with more life-like motion and interaction.

To achieve the required performance in a shorter design cycle and with lower costs than assembling hard IP from different vendors, Ageia's chip development team used ARM physical IP for its PhysX gaming processor.



ARM Powered stability control systems
reduce single car accident rates by 40%.

Selected financial data/IFRS

	2007 £000	2006 £000	2005 £000	2004** £000	2003* £000
Revenues	259,160	263,254	232,439	152,897	128,070
Cost of revenues	(28,105)	(30,877)	(26,610)	(12,240)	(11,022)
Gross profit	231,055	232,377	205,829	140,657	117,048
Total operating expenses, net	(191,361)	(183,129)	(170,672)	(112,328)	(98,609)
Profit from operations	39,694	49,248	35,157	28,329	18,439
Investment income, net	5,402	6,758	5,317	6,944	4,801
Profit before tax	45,096	56,006	40,474	35,273	23,240
Tax	(9,846)	(7,850)	(10,827)	(9,398)	(7,977)
Profit after tax	35,250	48,156	29,647	25,875	15,263
Equity minority interest	-	-	-	-	(105)
Profit for the year	35,250	48,156	29,647	25,875	15,158
Dividends paid	18,547	12,367	10,436	8,975	-
Capital expenditure	5,444	8,559	6,064	5,036	3,605
Research and development expenditure	83,977	84,884	80,273	54,674	48,131
Cash, short- and long-term investments	51,323	128,494	160,902	142,817	159,786
Shareholders' funds	579,162	660,926	746,847	642,538	180,435
Employees at end of year (number)	1,728	1,659	1,324	1,171	740

* Figures for 2003 are shown under UK GAAP and are not comparable to 2004 to 2007 prepared under IFRS.

** Figures for 2004 have been restated from UK GAAP to IFRS.

in 2007 include acquisition-related charges relating to amortisation of intangibles of £19.2 million (2006: £19.3 million), other acquisition-related charges of £1.7 million (2006: £1.1 million), impairment of an available-for-sale security of £2.1 million (2006: £nil), profit on disposal of an available-for-sale investment of £nil (2006: £5.3 million), restructuring charges of £1.0 million (2006: £nil) and compensation charges in respect of share-based payments and related payroll taxes of £17.3 million (2006: £16.4 million). Excluding these charges and credits, total operating expenses in 2007 were £150.1 million, compared to £151.6 million in 2006.

Research and development expenses in 2007 were £84.0 million, representing 32% of revenues. This compares to £84.9 million or 32% of revenues in 2006. Average headcount in this area increased from 961 in 2006 to 1,163 in 2007. Research and development expenses in 2007 include total acquisition-related charges and credits of £11.4 million (2006: £10.6 million) and compensation charges in respect of share-based payments and related payroll taxes of £10.7 million (2006: £10.1 million). Excluding these charges, research and development expenses in 2007 were £61.9 million and £64.2 million in 2006, representing 24% and 24% of revenues respectively.

Sales and marketing costs in 2007 were £55.3 million or 21% of

revenues, compared to £53.3 million or 20% of revenues in 2006. Average headcount in this area increased from 302 in 2006 to 312 in 2007. Sales and marketing costs in 2007 include total acquisition-related charges of £8.6 million (2006: £9.1 million) and compensation charges in respect of share-based payments and related payroll taxes of £3.6 million (2006: £3.5 million). Excluding these charges, sales and marketing costs in 2007 were £43.0 million and £40.7 million in 2006, representing 17% and 15% of revenues respectively.

General and administrative expenses in 2007 were £52.1 million or 20% of revenues, compared to £50.2 million or 19% of revenues in 2006. Average headcount in this area increased from 209 in 2006 to 226 in 2007. General and administrative expenses in 2007 include total acquisition-related charges of £0.9 million (2006: £0.7 million), restructuring charges of £1.0 million (2006: £nil), impairment of an available-for-sale security of £2.1 million (2006: £nil) and compensation charges in respect of share-based payments and related payroll taxes of £2.9 million (2006: £2.8 million). Excluding these charges, general and administrative expenses in 2007 were £45.2 million, compared to £46.7 million in 2006 representing 17% and 18% of revenues respectively.

Additionally in 2006, the Group sold its investment in CSR plc, resulting in a profit of £5.3 million.

APPLE IPHONE

Probably the most talked about consumer product in 2007, the Apple iPhone is a revolutionary mobile phone combining a widescreen iPod with touch controls and a breakthrough Internet communications device with desktop-class email, web and searching facility. iPhone also introduces an entirely new user interface based on a large multi-touch display and pioneering new software, letting you control everything with your fingers.

According to press articles and product tear-down reports by independent analysts, the iPhone contains multiple ARM technology-based chips each from several different silicon providers which would provide functions such as the applications processor, baseband processor, WiFi and touchscreen.



Today's smartphone has more computing power than the first Cray Super computer.

Operating margin

The operating margin in 2007 was 15.3% compared to 18.7% in 2006. The operating margin in 2007, excluding acquisition-related charges of £20.9 million, restructuring charges of £1.0 million, impairment of an available-for-sale security of £2.1 million and compensation charges in respect of share-based payments and related payroll taxes of £18.4 million was 31.7% (the normalised operating margin) compared to 31.1%, before acquisition-related charges of £20.4 million, compensation charges in respect of share-based payments of £17.4 million and profit on disposal of an available-for-sale investment of £5.3 million in 2006.

Earnings and taxation

Profit before tax in 2007 was £45.1 million compared to £56.0 million in 2006. Profit before tax in 2007, excluding acquisition-related charges of £20.9 million, restructuring charges of £1.0 million, impairment of an available-for-sale security of £2.1 million and compensation charges in respect of share-based payments and related payroll taxes of £18.4 million, was £87.5 million or 33.8% of revenues. This compares to £88.5 million, before acquisition-related charges of £20.4 million, compensation charges in respect of share-based payments of £17.4 million and profit on disposal of an available-for-sale investment of £5.3 million, or 33.6% of revenues in 2006.

The Group's effective taxation rate in 2007 was 21.8%, compared to 14.0% in 2006. This increase was primarily due to a non-recurring tax credit in 2006 arising from a tax-deductible foreign exchange loss.

Fully diluted earnings per share in 2007 were 2.6 pence compared to 3.4 pence in 2006. Earnings per fully diluted share in 2007, before acquisition-related charges of £20.9 million, restructuring charges of £1.0 million, impairment of an available-for-sale security of £2.1 million and compensation charges in respect of share-based payments and related payroll taxes of £18.4 million and related estimated tax adjustments thereon of £9.9 million, were 5.0 pence, compared to 5.2 pence before acquisition-related charges of £20.4 million, compensation charges in respect of share-based payments of £17.4 million, profit on disposal of an available-for-sale investment of

£5.3 million and related estimated tax adjustments thereon of £7.6 million, in 2006.

Balance sheet and cash flow

Goodwill at 31 December 2007 was £420.8 million, compared to £427.7 million at 31 December 2006. The decrease in goodwill in 2007 is due primarily to foreign exchange movements, given the weakening of the US dollar against sterling from \$1.96 at 31 December 2006 to \$1.99 at the end of 2007. Goodwill is not amortised under IFRS but is subject to impairment review on at least an annual basis. The review performed in 2007 concluded that no impairment was required.

Other intangible assets at 31 December 2007 were £44.3 million, compared to £62.9 million at 31 December 2006. The movement in other intangible assets in 2007 primarily reflects the amortisation in the year of the intangible assets arising on acquisitions of £19.2 million. Other intangible assets are amortised through the profit and loss account over their estimated useful lives to the Group.

Accounts receivable at 31 December 2007 were £68.2 million, compared to £69.6 million at 31 December 2006. The allowance against receivables was £1.5 million at 31 December 2007, compared to £2.6 million at 31 December 2006. Deferred revenues were £27.5 million at 31 December 2007, compared to £31.5 million at the end of 2006.

Resources available

The consolidated cash, cash equivalents, short-term investments and marketable securities balance was £51.3 million at 31 December 2007 compared to £128.5 million at 31 December 2006. This reduction is as a result of the continued share buyback programme and payment of dividends (see below) as well as residual payments on prior year acquisitions. Excluding these outflows, the Group generated £76.0 million of cash in the year (2006: £73.7 million).

Interest receivable

Net interest receivable was £5.4 million for 2007 compared to £6.8 million in 2006. The reduction is due to the reduced cash balances held by the Group as a result of the return of cash to shareholders through dividends and share buybacks as detailed below.

"The growing momentum behind more intelligent phones has accelerated in 2007, with the arrival of a new generation of highly sophisticated smartphones that contain even more features, such as graphics, video and connectivity to WiFi and GPS, turning the mobile phone into a mobile internet device (MID). These devices can contain five or more separate ARM products."

Returns to shareholders

Dividend

The directors recommend payment of a final dividend in respect of 2007 of 1.2 pence per share, which taken together with the interim dividend of 0.8 pence per share paid in October 2007, gives a total dividend in respect of 2007 of 2.0 pence per share, an increase of 100% over 1.0 pence per share in 2006. Subject to shareholder approval, the final dividend will be paid on 21 May 2008 to shareholders on the register on 2 May 2008. Total dividends actually paid in 2007 amounted to £18.5 million (2006: £12.4 million).

Share buyback programme

In 2007, the Group continued its rolling share buyback programme to supplement dividends in returning surplus funds to shareholders. During the year, the Company bought back 94.5 million shares (2006: 63.6 million) at a total cost of £128.6 million (2006: £76.5 million).

Since introducing dividend payments in 2004 and commencing the share buyback programme in July 2005, £272 million has been returned to shareholders and 172 million shares, being 12.3% of issued share capital, have been bought back. This has contributed to a net reduction in the fully diluted shares in issue from 1,424 million in 2005 to 1,402 million in 2006 to 1,361 million in 2007. This programme is on-going and is expected to continue during 2008 and beyond.

Capital structure

The authorised share capital of the Company is 2,200,000,000 ordinary shares of 0.05 pence each (2006: 2,200,000,000). The issued share capital at 31 December 2007 was 1,344,055,696 ordinary shares of 0.05 pence each (2006: 1,389,907,834). As a result of the buyback programme, the Company owns 65,201,176 of its own shares at 31 December 2007 (2006: 49,500,000).

Treasury policies and objectives and liquidity

The Group has established treasury policies aimed both at mitigating the impact of foreign exchange fluctuations on reported profits

and cash flows and at ensuring appropriate returns are earned on the Group's cash resources.

With more than 95% of Group revenues earned in US dollars and approximately 40% of Group costs being incurred in US dollars, the Group has a significant exposure to movements in the exchange rate between the US dollar and sterling. This exposure is partially mitigated by an ongoing hedging programme, involving forward contracts and low-risk option contracts where appropriate.

Principal risks and uncertainties

In line with the guidance for the preparation of an operating and financial review, certain risk factors faced by the Group are identified below. A more detailed description is included in the Group's annual report on Form 20-F. Details of the Group's internal control and risk management procedures are included in the corporate governance report on pages 25 to 29.

ARM's quarterly results may fluctuate significantly and be unpredictable which could adversely affect the market price of ARM ordinary shares ARM has experienced, and may in the future experience, significant quarterly fluctuations in its results of operations. Quarterly results may fluctuate because of a variety of factors. Such factors include:

- The timing of entering into agreements with new licensees;
- The mixture of licence fees, royalties, revenues from the sale of development systems and fees from services;
- The introduction of new technology by us, our licensees or our competition;
- The timing of orders from, and shipments to, systems companies of ARM technology-based microprocessors from our semiconductor Partners;
- Sudden technological or other changes in the microprocessor industry; and
- New litigation or developments in current litigation.

"Since introducing dividend payments in 2004 and commencing the share buyback programme in July 2005, £272 million has been returned to shareholders."

Mobile phones outsell laptops five to one.

“The demand for smart cards is also escalating due to demand from increasingly security-conscious governments and enterprises, said Anoop Ubhey, Global Program Director, Smart Cards, Frost and Sullivan. Secure 32bit platforms such as the ARM SecurCore SC300 processor are essential in enabling the growing level of sophistication in smart cards.”

Article: Processor boosts energy efficiency
Source: www.electronicstalk.com

In future periods, ARM's operating results may not meet the expectations of public market analysts or investors. In such an event the market price of our shares could be materially adversely affected.

General economic conditions may reduce ARM's revenues and harm its business

ARM is subject to risks arising from adverse changes in global economic conditions. Because of economic uncertainties in many of our key markets, many industries may delay or reduce technology purchases and investments. The impact of this on ARM is difficult to predict, but if businesses defer licensing our technology, require fewer services or development tools, or if consumers defer purchases of new products which incorporate ARM's technology, revenue could decline. A decline in revenue would have an adverse effect on the results of operations and could have an adverse effect on ARM's financial condition.

ARM competes in the intensely competitive semiconductor market

The semiconductor market is intensely competitive and characterised by rapid technological change. ARM cannot give assurance that it will have the financial resources, technical expertise, or marketing or support capabilities to compete successfully in the future.

Competition is based on a variety of factors including price, performance, product quality, software availability, marketing and distribution capability, customer support, name recognition and financial strength. Further, given ARM's reliance on our semiconductor Partners, its competitive position is dependent on their competitive position. In addition, ARM's semiconductor Partners do not license ARM's architecture exclusively, and several of them also design, develop, manufacture and market microprocessors based on their own architectures or on other non-ARM architectures.

ARM may not operate systems which comply fully with the requirements of the Sarbanes-Oxley Act

Attestation under section 404 of the Sarbanes-Oxley Act as at 31 December 2007 has been successfully completed. Full details appear in the Group's annual report on Form 20-F. There can be no guarantee, however, that in future the detailed testing of internal controls required as part of the attestation process will not identify significant control deficiencies or material weaknesses that impact on the auditors' opinion on internal controls over financial reporting and/or require disclosure on Form 20-F for future years.

Other risks include ARM's inability to manage the significant changes in

the number of its employees and the size of its operations in the United States; dependence on semiconductor Partners and systems companies; availability of development tools; systems software and operating systems compatible with ARM's architecture; dependence on a small number of customers and products; ARM's inability to develop new products on a timely basis; unanticipated costs due to products that could have technical difficulties or undetected design errors; the ARM architecture not being continued to be accepted by the market; risks associated with any strategic investments or acquisitions; dependence on senior management personnel and on hiring and retaining qualified engineers; exposure from international operations; litigation and threats of litigation and protection of ARM's intellectual property; unavailability of debt financing or additional equity funding to satisfy future capital needs, adverse effects resulting from changes in share option accounting rules adversely impacting ARM's reported operating results and its competitiveness in the marketplace.



Tim Score
Chief Financial Officer

Board of directors



Doug Dunn, OBE, age 63
Chairman

Doug Dunn joined the board as an independent non-executive director in December 1998 and became non-executive Chairman on 1 October 2006. He was previously President and Chief Executive Officer of ASM Lithography Holding N.V. until his retirement in December 2004. Before joining ASML, he was Chairman and Chief Executive Officer of the Consumer Electronics Division of Royal Philips Electronics N.V. and a member of the board. He was previously Managing Director of the Semiconductor divisions of Plessey and GEC and held several engineering and management positions at Motorola. He was awarded an OBE in 1992. He is a non-executive director of ST Microelectronics N.V., Soitec S.A., LG. Philips LCD Co. Ltd and TomTom N.V.



Warren East age 46
Chief Executive Officer

Warren East joined ARM in 1994 to set up ARM's consulting business. He was Vice President, Business Operations from February 1998. In October 2000 he was appointed to the board as Chief Operating Officer and in October 2001 was appointed Chief Executive Officer. Before joining ARM he was with Texas Instruments. He is a chartered engineer, Fellow of the Institution of Engineering and Technology, Fellow of the Royal Academy of Engineering and a Companion of the Chartered Management Institute. He is a non-executive director of Reciva Limited and of De La Rue plc.

Tim Score age 47
Chief Financial Officer

Tim Score joined ARM as Chief Financial Officer and director in March 2002. Before joining ARM, he was Finance Director of Rebus Group Limited. He was previously Group Finance Director of William Baird plc, Group Controller at LucasVarity plc and Group Financial Controller at BTR plc. He is a non-executive director and Chairman of the Audit Committee of National Express Group plc.



Tudor Brown age 49
Chief Operating Officer

Tudor Brown was one of the founders of ARM. Before joining the Company, he was Principal Engineer at Acorn Computers, where he worked on the ARM R&D programme. At ARM, he was Engineering Director and Chief Technical Officer from 1993; in October 2000, he was appointed Executive Vice President (EVP), Global Development and in October 2001 he was appointed to the board as Chief Operating Officer. He is a non-executive director of ANT plc.

Mike Inglis age 48
Executive Vice President, Sales and Marketing

Mike Inglis joined ARM as EVP, Marketing in June 2002 and was appointed to the board in August that year. He became EVP, Sales and Marketing in January 2007. Before joining ARM, he worked in management consultancy with A.T. Kearney and held a number of senior operational and marketing positions at Motorola. He previously worked in semiconductor sales, marketing, design and consultancy with Texas Instruments, Fairchild and BIS Macintosh and gained his initial industrial experience with GEC Telecommunications. He is a chartered engineer and a Member of the Chartered Institute of Marketing.



Mike Muller age 49
Chief Technology Officer

Mike Muller was one of the founders of ARM. Before joining the Company, he was responsible for hardware strategy and the development of portable products at Acorn Computers. He was previously at Orbis Computers. At ARM he was VP, Marketing from 1992 to 1996 and EVP, Business Development until October 2000 when he was appointed Chief Technology Officer. In October 2001, he was appointed to the board.

Simon Segars age 40
General Manager – Physical IP Division

Simon Segars joined the board in January 2005 and was appointed General Manager of the Physical IP Division in September 2007. He has previously been EVP, Engineering, EVP, Worldwide Sales and latterly EVP, Business Development. He joined ARM in early 1991 and has worked on most of the ARM CPU products since then. He led the development of the ARM7 and ARM9 Thumb® families. He holds a number of patents in the field of embedded CPU architectures. He is a non-executive director of Plastic Logic Limited.



Lucio Lanza age 63
Independent non-executive director

Lucio Lanza joined ARM as a non-executive director in December 2004 following ARM's acquisition of Artisan. He was previously a director of Artisan, from 1996, becoming Chairman in 1997. He is currently Managing Director of Lanza techVentures, an early stage venture capital and investment firm, which he founded in January 2001. In 1990, he joined US Venture Partners, a venture capital firm, as a venture partner and was a general partner. From 1990 to 1995, he was an independent consultant to companies in the semiconductor, communications and computer-aided design industries, including Cadence Design Systems, Inc. and, from 1986 to 1989, was Chief Executive Officer of EDA Systems, Inc. He is also on the board of directors of PDF Solutions, Inc., a provider of technologies to improve semiconductor manufacturing yields. He holds a doctorate in electronic engineering from Politecnico of Milano.



Kathleen O'Donovan age 50
Independent non-executive director

Kathleen O'Donovan joined the board in December 2006. She is a non-executive director and Chairman of the Audit Committees of Prudential plc, Great Portland Estates plc and Trinity Mirror plc and Chairman of the InvenSys Pension Scheme. Previously she was a non-executive director and Chairman of the Audit Committees of the Court of the Bank of England and EMI Group plc and a non-executive director of O2 plc. Prior to that, she was Chief Financial Officer of BTR and InvenSys and before that she was a partner at Ernst & Young.

Philip Rowley age 55
Independent non-executive director

Philip Rowley joined the board in January 2005. He was Chairman and CEO of AOL Europe, the interactive services, web brands, internet technologies and e-commerce provider until February 2007. He is a qualified chartered accountant and was Group Finance Director of Kingfisher plc from 1998 to 2001. Prior to that, his roles included Executive Vice President and Chief Financial Officer of EMI Music Worldwide. He is a non-executive director of HMV Group plc and Skinkers Limited.



John Scarisbrick age 55
Independent non-executive director

John Scarisbrick joined the board in August 2001. He was CEO of CSR plc from June 2004 until October 2007 and previously worked for 25 years at Texas Instruments (TI) in a variety of roles including as Senior Vice President responsible for TI's \$5 billion ASP chip business, President of TI Europe and leader of the team that created TI's DSP business in Houston, Texas. Before joining TI, he worked in electronics systems design roles at Rank Radio International and Marconi Space and Defence Systems in the UK. He is a non-executive director of Intrinsicity, Inc and Netronome Inc.

Jeremy Scudamore age 60
Senior independent director

Jeremy Scudamore joined the board in April 2004. He was Chief Executive Officer of Avecia Group (formerly the specialty chemicals business of Zeneca) until April 2006 and previously held senior management positions both in the UK and overseas with Zeneca and ICI. He has been a board member of the Chemical Industries Association and is Chairman of England's North West Science Council. He was also a member of the DTI's Innovation and Growth Team for the Chemical Industry and Chairman of the Innovation Team. He is non-executive Chairman of SkyePharma plc and Oxford Advanced Surfaces plc and a non executive director of Oxford Catalysts Group plc.



Young Sohn age 52
Independent non-executive director

Young Sohn joined the board in April 2007. He has extensive experience in the semiconductor industry both in Silicon Valley and in Asia. He is CEO of Inphi Corporation, a director of Cymer, Inc. and Audium Semiconductor Limited and an adviser to Panorama Capital, a Silicon Valley based venture capital firm. Previously he was President of the semiconductor products group at Agilent Technology, Inc. and Chairman of Oak Technology, Inc. Prior to that, he was President of the hard drive business of Quantum Corporation and, before that, Director of Marketing at Intel Corporation.

Shareholder information

ARM Holdings plc
Secretary and registered office
Patricia Alsop
110 Fulfourn Road
Cambridge CB1 9NJ
United Kingdom

Registered number
2548782

Auditors
PricewaterhouseCoopers LLP
1 Embankment Place
London WC2N 6RH
United Kingdom

Stockbrokers
Morgan Stanley & Co.
International Limited
25 Cabot Square
Canary Wharf
London E14 4QA
United Kingdom

UBS Limited
2 Finsbury Avenue
London EC2M 2PP
United Kingdom

Registrars
Equiniti
Aspect House
Spencer Road
Lancing
West Sussex
BN99 6GU
United Kingdom

Shareholder Helpline: 0871 384 2139

Depository
The Bank of New York
101 Barclays Street
New York
New York 10286
United States of America

Legal advisers
UK Law
Linklaters
One Silk Street
London EC2Y 8HQ
United Kingdom

US Law
Davis Polk & Wardwell
99 Gresham Street
London EC2V 7NG
United Kingdom

Role of the board

The board is committed to high standards of corporate governance and business integrity, which it believes are essential to maintaining the trust of investors and other stakeholders in the Group. The board is responsible for setting the Group's strategic aims and standards of conduct, monitoring performance against the business plan and budget prepared by the executive directors and ensuring that the necessary financial and human resources are in place for it to meet its objectives. The board and all employees are subject to a Code of Business Conduct and Ethics, a copy of which is published on the corporate website at www.arm.com. The board has a formal schedule of matters specifically reserved for its decision, which includes the approval of major business matters, policies, and operating and capital expenditure budgets. The board is also responsible for sanctioning unusual commercial arrangements such as atypical licence agreements and investments. The board delegates authority to various committees that are constituted within written terms of reference and chaired by independent non-executive directors where required by the Combined Code.

Compliance with the Combined Code

The Group complies, and complied throughout 2007, with the Combined Code 2006, with the exception only that the board did not comprise a majority of independent non-executive directors throughout the year. The board has considered the overall balance between executive and non-executive directors and believes that the number of executive directors is fully justified by the contribution made by each of them. To increase the size of the board further to meet this particular provision is not considered appropriate.

Composition and operation of the board

The board currently comprises six executive directors, six independent non-executive directors and the Chairman. The executive directors are the Chief Executive Officer, the Chief Operating Officer, the Chief Financial Officer, the Chief Technology Officer, the Executive Vice President, Sales and Marketing and the General Manager, Physical IP Division, all of whom play significant roles in the day-to-day management of the business. The board reviews the independence of the non-executive directors on appointment and at appropriate intervals and considers the six non-executive directors to be independent in character, judgment and behaviour, based on both participation and performance at board and committee meetings. There are no relationships or circumstances which are likely to affect the judgment of any of them. The beneficial interests of the directors in the share capital of the Company are set out on page 41. In the opinion of the board, these shareholdings do not detract from the non-executive directors' independent status.

Young Sohn joined the board as an independent non-executive director on 2 April 2007. He has extensive experience in the semiconductor industry both in Silicon Valley and in Asia. A more detailed biography is included on page 23. He was appointed to the audit and remuneration committees with effect from 15 May 2007.

As planned, Peter Cawdron retired from the board at the AGM on 15 May 2007 having served for nine years. He was replaced as senior independent director by Jeremy Scudamore, who has a strong background in industry and commerce. Lucio Lanza and John Scarisbrick both have a broad understanding of the Group's technology and the practices of major US-based technology companies. Philip Rowley and Kathleen O'Donovan are both financial experts with strong financial backgrounds.

The table below shows directors' attendance at meetings which they were eligible to attend during the 2007 financial year:

	Board	Audit committee	Remuneration committee	Nomination committee
Number of meetings held	9	5	4	1
Doug Dunn	9/9C	–	–	1/1C
Warren East	9/9	–	–	–
Tudor Brown	9/9	–	–	–
Mike Inglis	8/9	–	–	–
Lucio Lanza	9/9	5/5	–	1/1
Mike Muller	9/9	–	–	–
Kathleen O'Donovan	8/9	4/5	3/4	–
Philip Rowley	7/9	4/5C	–	–
John Scarisbrick	7/9	–	–	1/1
Jeremy Scudamore	9/9	5/5	4/4C	–
Tim Score	9/9	–	–	–
Simon Segars	8/9	–	–	–
Young Sohn*	6/6	3/3	2/2	–
Peter Cawdron**	3/4	1/2	2/3	1/1

* Young Sohn was appointed to the board on 2 April 2007 and to the audit and remuneration committees on 15 May 2007.

** Peter Cawdron retired from the board on 15 May 2007.

C Chairman.

There is a procedure in place for additional meetings or conference calls on any pertinent issues to be organised as necessary during the year. In addition, the Chairman held at least two meetings with the non-executive directors without the executives present and the non-executive directors met on at least one occasion without the Chairman being present.

The directors have the benefit of directors' and officers' liability insurance and there is an established procedure for individual directors, who consider it necessary in the furtherance of their duties, to obtain independent professional advice at the Group's expense. In addition, all members of the board have access to the advice of the Company Secretary.

Information and communication with shareholders

Before each meeting, the board is furnished with information concerning the state of the business and its performance in a form and of a quality appropriate for it to discharge its duties. The ultimate responsibility for reviewing and approving the annual report and accounts and the quarterly reports, and for ensuring that they present a balanced assessment of the Group's position, lies with the board. The board delegates day-to-day responsibility for managing the Group to the executive committee and has a number of other committees, details of which are set out below.

The board makes considerable efforts to establish and maintain good relationships with shareholders. The main channel of communication continues to be through the CEO, the CFO and the VP Investor Relations, although the Chairman, the senior independent director and the other non-executive directors remain willing to engage in dialogue with major shareholders as appropriate.

There is regular dialogue with institutional shareholders throughout the year other than during close periods. The board also encourages communication with private investors and part of the Group's website is dedicated to providing accurate and timely information for all investors including comprehensive information about the business, its Partners and products, all press releases, RNS and Securities and Exchange Commission (SEC) announcements. At present, around 20 analysts write research reports on the Group. The Group publishes telephone numbers on its website, enabling shareholders to listen to earnings presentations and audio conference calls with analysts; and webcasts of key presentations are also made available through the website. Members of the board, including some of the non-executive directors, attend the annual analysts' day and develop an understanding of the views of major shareholders through any direct contact that may be initiated by shareholders, or through analysts' and brokers' briefings. The board also receives feedback from the Group's brokers and financial PR advisers, who obtain feedback from analysts and brokers following investor roadshows. All shareholders may register to receive the Group's press releases via the internet.

The board actively encourages participation at the Annual General Meeting, scheduled for 13 May 2008, which is the principal forum for dialogue with private shareholders. A presentation will be made outlining recent developments in the business and an open question-and-answer session will follow to enable shareholders to ask questions about the business in general.

The resolutions put to shareholders at the meeting and the voting results will be published via RNS and the SEC and will be available on the Group's website.

Board evaluation, induction and training

The board undertakes an annual board evaluation. During 2007, this exercise was conducted internally with each director completing a questionnaire and was led by the Chairman and facilitated by the Company Secretary. The evaluation covered board performance, processes, committees, composition, skills and director induction. The overall conclusion was that individual board members are satisfied that the board works well. They are also satisfied with the contribution made by their colleagues and that board committees operate properly and efficiently. Various recommendations resulted from the evaluation which have been discussed by the board and will be reviewed further and acted upon by the board in 2008, as appropriate. In particular, the non-executive directors now make a greater contribution to forward agenda setting. It is intended that there will be a further board evaluation each year, involving external consultants as and when the board deems appropriate.

A full, formal induction programme is arranged for new directors, tailored to their specific requirements, the aim of which is to introduce them to key executives across the business and to enhance their knowledge and understanding of the Group and its activities. The Group has a commitment to training and all directors, executive or non-executive, are encouraged to attend suitable training courses at the Group's expense. During the year a presentation was given to the board on the key provisions of the Companies Act 2006, including directors' duties.

Executive committee

The executive committee is responsible for implementing the strategy approved by the board. Among other things, this committee is responsible for ensuring that the Group's budget and forecasts are properly prepared, and that targets are met, and generally managing and developing the business within the overall budget. Variations from the budget and changes in strategy require approval from the main board of the Group. The executive committee, which meets monthly, comprises the Chief Executive Officer, Chief Financial Officer, Chief Operating Officer, EVP Sales & Marketing, the General Managers of the Processor and Physical IP Divisions, the EVP Human Resources, the General Counsel and the Company Secretary and meetings are attended by other senior operational personnel, as appropriate.

Audit committee

The audit committee has written terms of reference which are published on the corporate website at www.arm.com. The committee has responsibility for, among other things, monitoring the integrity of the financial statements of the Group and any formal announcements relating to the Group's financial performance, and for reviewing any significant financial reporting judgments contained in them; reviewing the effectiveness of the Group's internal controls over financial reporting and providing oversight of the Group's risk management systems; making recommendations to the board in relation to the appointment, remuneration and resignation or dismissal of the Group's external auditors; reviewing and monitoring the external auditors' independence and objectivity and the effectiveness of the audit process; developing and implementing policy on the engagement of the external auditors to supply non-audit services; and considering compliance with legal requirements, accounting standards, the Listing Rules of the Financial Services Authority and the requirements of the SEC. There is a procedure in place for employees to report areas of concern to management in confidence and, if they prefer, anonymously through a third-party telephone line. The committee receives any such confidential reports from the compliance committee. No whistleblowing incidents were reported in 2007. There has been one confidential report to date in 2008, which has been fully investigated and the committee is satisfied that there is no evidence of impropriety.

The committee also keeps under review the value for money of the audit and the nature, extent and cost-effectiveness of the non-audit services provided by the auditors. The committee has discussed with the external auditors their independence, and has received and reviewed written disclosures from the external auditors as required by the Auditing Practices Board's International Standard on Auditing (ISA) (UK and Ireland) 260 "Communication of audit matters with those charged with governance", as well as those required by the US Independence Standards Board's Standard No. 1, "Independence discussions with audit committees". To avoid the possibility of the auditors' objectivity and independence being compromised, the Group's tax consulting work is carried out by the auditors only in cases where they are best suited to perform the work. In other cases, the Group has engaged another independent firm of accountants to perform tax consulting work. The Group does not normally award general consulting work to the auditors. From time to time, however, the Group will engage the auditors to perform work on matters relating to human resources and royalty audits. The Group may also seek professional advice from another firm of independent consultants or its legal advisers.

The current audit committee comprises Philip Rowley (Chairman), Kathleen O'Donovan, Lucio Lanza, Jeremy Scudamore and Young Sohn. Philip Rowley is the financial expert as defined in the Sarbanes Oxley Act 2002 (US) and Kathleen O'Donovan is also qualified to fulfil this role. Both have recent and relevant financial expertise. The external auditors, Chief Executive Officer, Chief Financial Officer and the Company Secretary attend all meetings in order to ensure that all the information required by the audit committee for it to operate effectively is available. Representatives of the Group's external auditors meet with the audit committee at least once a year without any executive directors being present.

Remuneration committee

A description of the composition, responsibility and operation of the remuneration committee is set out in the remuneration report on page 38. The terms of reference of the remuneration committee are published on the Group's website at www.arm.com.

Nomination committee

The nomination committee leads the process for board appointments and makes recommendations to the board in relation to new appointments of executive and non-executive directors and on board composition and balance. The terms of reference of the nomination committee are published on the Group's website at www.arm.com. It is chaired by Doug Dunn, and the other members are John Scarisbrick and Lucio Lanza. The committee considers the roles and capabilities required for each new appointment, based on an evaluation of the skills and experience of the existing directors. In relation to the appointment of new directors, the services of external search consultancies are generally used and this was the case in relation to the appointment of Young Sohn.

Internal control/risk management

The Group fully complies with the Combined Code's provisions on internal control, having established procedures to implement the guidance in the Turnbull Report (2005). The board has established a continuous process for identifying, evaluating and managing the significant risks faced by the Group. The board confirms that the necessary actions have been or are being taken to remedy any significant failings or weaknesses identified from this process.

The board of directors has overall responsibility for ensuring that the Group maintains an adequate system of internal control and risk management and for reviewing its effectiveness. Building on the successful project to achieve compliance with section 404 of the Sarbanes Oxley Act 2002 (US) for the 2006 financial year, a considerable amount of resource and effort continued to be committed during 2007 and compliance in relation to the 2007 financial year was also successfully completed. This is reported on in more detail in the annual report on Form 20-F that is filed with the SEC. The processes and procedures have been successfully integrated into day-to-day business operations and proven to provide a sustainable solution for ongoing compliance. The board has reviewed the system of internal control, including internal controls over financial reporting, which has been in place for the year under review and up to the date of approval of the annual report. Such systems are designed to manage rather than eliminate the risks inherent in a fast-moving, high-technology business and can, therefore, provide only reasonable and not absolute assurance against material misstatement or loss.

The Group has a number of other committees which contribute to the overall control environment. These include:

Risk review committee

The risk review committee consists of the Chief Technology Officer, the Chief Financial Officer, the Group Financial Controller and the Company Secretary and it receives and reviews quarterly reports from the divisions and corporate functions. The committee is responsible for identifying and evaluating risks which may impact the Group's strategic and business objectives and for monitoring the progress of actions designed to mitigate such risks. The risk review committee reports formally to the executive committee twice a year where its findings are considered and challenged and, in turn, the executive committee reports to the board once a year.

Compliance committee

The compliance committee consists of the General Counsel, the Chief Operating Officer, the Chief Financial Officer, the EVP Human Resources, the VP Corporate Operations, the VP of IT and the Company Secretary. It oversees compliance throughout the business with all appropriate international regulations, trading requirements and standards, including oversight of financial, employment, environmental and security processes and policies. The compliance committee has a reporting line to the audit committee.

Disclosure committee

The disclosure committee comprises the Chief Executive Officer, the Chief Financial Officer, the Group Financial Controller, the General Counsel, the VP Investor Relations and the Company Secretary. It is responsible for ensuring that disclosures made by the Group to its shareholders and the investment community are accurate, complete and fairly present the Group's financial condition in all material respects.

In addition, there is a series of interconnected meetings that span the Group from the weekly management meeting chaired by the Chief Executive Officer, and the weekly business review meeting chaired by the Chief Operating Officer, the purpose of which is to monitor and control all main business activities, sales forecasts and other matters requiring approval that have arisen within the week, to the board meetings of the Group. Each month there are customer satisfaction and process review meetings attended by managers representing different functions across the Group to review key performance indicators such as revenues, orders booked, costs, product and project delivery dates and levels of defects found in products in development. The outputs of the weekly business review meeting and the monthly operations meeting are reviewed by the executive committee which, in turn, raises relevant issues with the board of the Group. These processes for identifying, evaluating and managing the significant business, operational, financial, compliance and other risks facing the Group have been in place for the year under review and up to the date of approval of the annual report and financial statements.

As required by the Combined Code, the audit committee has considered whether it would be appropriate for the Group to have its own financial internal audit function and has concluded that, taking account of its relatively small number of employees and a high degree of centralisation in the way the business is run, this is not appropriate at present. The committee has confirmed this view to the board. The Group does, however, have an operational internal audit function that audits the Group's business and product/project management processes. These processes are documented, maintained and continuously improved, for effectiveness and efficiency. In addition, they are audited externally by Lloyd's Register Quality Assurance for compliance with ISO 9001:2000.

Any significant control failings identified through the operational internal audit function or the independent auditors are brought to the attention of the compliance committee and undergo a detailed process of evaluation of both the failing and the steps taken to remedy it. There is then a process for escalation of any significant control failures to the audit committee.

Environmental, social, corporate governance and ethical policies

While the Group is accountable to its shareholders, it also endeavours to take into account the interests of all its stakeholders, including its employees, customers and suppliers and the local communities and environments in which it operates. The Chief Financial Officer takes responsibility for these matters, which are considered at board level. A corporate social responsibility (CSR) report is on pages 30 to 32 of this report and also on the Group's website www.arm.com. The company's Code of Business Conduct and Ethics is available on the Group's website and the Group regularly monitors employees' awareness of Group policies and procedures, including ethical policies. The Group also operates a whistleblowing policy which provides for employees to have access to senior management to raise concerns in strict confidence about any unethical business practices. There is also a facility to make reports by telephone to an independent third party through a whistleblowing hotline.

As a company whose primary business is the licensing of IP, employees are highly valued and their rights and dignity are respected. The Group strives for equal opportunities for all its employees and does not tolerate any harassment of, or discrimination against, its staff. In January 2007, ARM was chosen as European Business of the Year, having been voted UK Business of the Year in 2006. In November 2007, ARM received two further prestigious awards when Warren East was voted UK Business Leader of the year and ARM was recognised as techMARK Company of the year. These represent considerable accolades for the Group and recognise the efforts of all ARM employees worldwide.

The Group endeavours to be honest and fair in its relationships with its customers and suppliers and to be a good corporate citizen respecting the laws of the countries in which it operates.

Environmental, social, corporate governance and ethical policies continued

The Group's premises are composed entirely of offices since it has no manufacturing activities. Staff make use of computer-aided design tools to generate IP. This involves neither hazardous substances nor complex waste emissions. With the exception of development systems products, the majority of "products" sold by the Group comprise microprocessor core and physical IP designs that are delivered electronically to customers.

The Group recognises the increasing importance of environmental issues and these are discussed at board level where the Chief Financial Officer takes responsibility for them. A number of initiatives in this area have continued in 2007. The Group's environmental policy is published on its website within the CSR report. An environmental action plan is implemented through various initiatives. These include monitoring resource consumption and waste creation so that targets set for improvement are realistic and meaningful, ensuring existing controls continue to operate satisfactorily and working with suppliers to improve environmental management along supply chains.

Energy usage and resource consumption data is published in the Group's CSR report on its website.

At the 2007 AGM, resolutions were passed to amend the articles of association in line with the Companies Act 2006 to enable the Company to send information to shareholders electronically and make documents available through the website rather than in hard copy, which provide both environmental and cost benefits. Shareholders can opt to continue receiving a printed copy of the annual report if they prefer.

Health and safety

Although ARM operates in an industry and in environments which are considered low risk from a health and safety perspective, the safety of employees, contractors and visitors is a priority in all ARM workplaces worldwide. Continual improvement in safety management systems is achieved through detailed risk assessments to identify and eliminate potential hazards, and occupational health assessments for employees. More detail about the Group's approach to environmental matters and health and safety is included in the CSR report on pages 30 to 32.

By order of the board



Patricia Alsop
Company Secretary

ARM considers itself to be a good corporate citizen and continually strives to improve its performance in this area. The Group aims to reduce the impact it makes on the environment and to make positive connections with the communities in which it operates. Considerable efforts are made to communicate effectively with the Group's shareholders, Partners, suppliers and employees.

Achievements

ARM was techMARK Company of the Year in 2007 where the judges recognised that ARM has "harnessed its technological achievements and produced sound commercial and financial success. The award also acknowledges analyst and investor recognition of ARM as well as its outstanding long-term growth potential and strategy to ensure successful delivery of its commercial advantages and to build shareholder value".

Chief Executive Officer, Warren East was voted UK Business Leader of the Year at the 2007 National Business Awards, in recognition of being "an outstanding individual who has demonstrated exceptional leadership and vision under whose stewardship the organisation has significantly improved performance for its stakeholders – employees, customers, suppliers and shareholders".

ARM was named as Business of the Year in 2007 at the European Business Awards. The judges commented that "ARM demonstrated an innovative growth strategy, strong financial performance and sustained market leadership in the industry sector". They were particularly impressed with ARM's strong market share in the mobile industry and the partnerships with some of the world's leading technology companies. The European Business Awards is a completely independent programme designed to recognise and celebrate business excellence across the 25 territories of the EU.

The environment

ARM designs the technology at the heart of low-power products across a whole range of application areas from mobile phones to cars, consumer electronics and toys. Intelligence within its low-power IP cores can be used to measure, manage and control the environmental performance of consumer electronics and IT equipment, while improving their functional performance and reducing their carbon footprint. Additionally, ARM can leverage its Connected Community™ of Partners to provide complete low-power solutions for products based on the ARM architecture.

The Group's activities do not produce harmful waste or emissions and the Ethical Investment Research Service (EIRIS) grades ARM as an environmentally "low impact" business. Nevertheless, environmental performance is monitored to enable targets to be set, for example reducing resource usage, increasing the amount recycled and controlling carbon emissions through energy use.

A global environmental impact study of the Group's operations has been undertaken, covering inputs, processes and outputs. This has provided data upon which to base plans and targeted improvements. For example, electricity supplies for our Cambridge offices are now 100% renewable and the application of a greener policy on energy procurement will be extended to other ARM locations where practicable. In 2007 the Group again demonstrated an increase in paper and packaging recycling and improved facilities to promote recycling of these and other materials, including aluminium cans. Air conditioning systems run on non-ozone-depleting refrigerants.

The environmental impact of travel is carefully considered. The supply of company cars is discouraged and in a Group of more than 1,700 people, there are fewer than 30 company cars. Employees are encouraged to cycle to work through the provision of improved facilities at the Group's offices, to share car journeys, or to use public transport. Consistent with local custom and practice, we provide bus transport for employees in Bangalore so that we do not add to local traffic problems and the environmental impact of individual travel to work. Business travel is important in maintaining ARM's very effective partnership network but ways in which it can be reduced are regularly reviewed and, where possible, travel is reduced through the use of video conferencing equipment. Data regarding flights is being benchmarked with a view to reducing business travel, to the extent compatible with ensuring that good business relationships are maintained.

Building upon the work carried out with the British Safety Council and Lloyd's Register Quality Assurance (LRQA), the Group has developed an internal audit process for all of its offices worldwide with regard to health and safety issues, environmental objectives and performance. ARM continues to work with suppliers and service providers to minimise environmental impact, wherever practicable, in the provision of facilities and infrastructure for ARM's business operations. ARM has adopted LRQA's Business Assurance approach involving twice-yearly themed audits which provide an independent assessment of the ARM Management System and the various review procedures in place within the Group. The themed audit approach enables LRQA to verify compliance with ISO9001:2000 and components of other relevant ISO standards.

Connecting with communities

The Group aims to be a good corporate citizen of the communities in which it operates and participates in networking and support initiatives. ARM has established relationships with the local business community in Cambridge and is a founding member of The Learning Collaboration (TLC) within the business community in the UK. The TLC enables member companies to pool resources to collaborate to learn, improving the quality, availability and value of training and related services.

ARM is also a founder member of the Cambridge Network whose aim is "to link like minded people from business and academia to each other and to the global high technology community for the benefit of the Cambridge region".

ARM is a founding sponsor of the Electronics Knowledge Transfer Network – an organisation which seeks to promote collaboration and the sharing of knowledge throughout the UK electronics industry in order to harness and promote the sector's global potential.

Supporting education

ARM's support for education stretches to financial sponsorship of science/IT-related education initiatives, donations of redundant computer equipment to schools and education charities, working on extra-curricular engineering projects with school and college students and working on specific projects with students at management schools.

The Group supports the Engineering Education Scheme, Young Engineers and Young Enterprise. ARM's University Programme directly engages with universities worldwide, designing course material, providing technical seminars, donating equipment and software and offering assistance to students. ARM has now engaged with universities in nearly every region of the world, including the EU, North and South America, Australia, China and Japan. With a growing demand in India for engineers, ARM has recently hired a university programme manager for the region. This reflects ARM's commitment to help universities produce graduates with the necessary skills that its Partners need.

Supporting good causes

ARM encourages employees to support their local communities. Some are school governors, some mentor young people, some organise events to raise money, others support charities directly. In India, ARM employees have organised blood donor sessions. In the US, ARM employees have supported a variety of charitable organisations including those supporting sufferers of leukaemia and lymphoma, cancer, multiple sclerosis, diabetes and AIDS. The Group "doubles the efforts" of employees who raise money for approved charities by matching the funds they raise (with the exception of political donations or other non-approved causes). Charities supporting sufferers of heart disease, Alzheimers, colitis and Crohn's disease, the Air Ambulance and the Samaritans have been some of the beneficiaries of this scheme.

Connecting with employees

ARM's aim is to attract and retain the best people available by being a good and ethical employer. The skills, knowledge and motivation of employees are crucial to ARM's success. The Group promotes and supports individuals and teams through on-the-job and formal training, coaching and mentoring. A comprehensive portfolio of learning and development opportunities is available to all employees, depending upon their needs and career aspirations. Every effort is made to keep employees well informed about the Group and matters that affect them. This is achieved through both formal and informal communication methods across all offices worldwide and includes employee consultation groups in regions where they are culturally appropriate. The Group also carries out a regular, comprehensive global opinion survey to monitor employee views and to provide valuable input on how the Group operates. The Employee Assistance Programme helps staff and their families with issues such as care for children or elderly relatives, legal and health advice and stress or other counselling.

Equal opportunities

The Group needs highly-qualified staff and does not see age, colour, disability, ethnic origin, gender, political or other opinion, religion or sexual orientation as a barrier to employment. If any member of staff becomes disabled, their needs and abilities are assessed with a view to them continuing in their current role. If this is impossible, every effort is made to offer them alternative employment.

Benefits

Employees receive benefits including private medical/healthcare; health, travel and life insurance; pensions/401k plan; sabbaticals; flexible working; restricted shares under the employee equity plan and the opportunity to buy shares through savings schemes. The Group supports family-friendly initiatives and offers a child care voucher scheme for UK tax payers. Flexible working arrangements are available for all employees, regardless of whether they have children. Understanding and acceptance of national and cultural diversity is encouraged by giving employees the opportunity to work in offices other than in their home country, where appropriate.

Accessibility

The Group endeavours to provide access to all whether through building design to allow easy disabled access or through improving access to our website for those with visual impairments.

Health and safety

The safety and welfare of employees, contractors and visitors is a priority. ARM measures and analyses all accidents and "near misses" as part of its continuous improvement in this area. This data, along with sickness data, is monitored to ensure trends are understood and action taken to reduce these occurrences. To date ARM has had no serious issues and retains a very low accident rate. Despite the low-risk nature of its operations, ARM aims to provide a safe, secure and sustainable working environment for all employees and stakeholders.

The Group's UK offices are audited by the British Safety Council and, as the UK legislative framework is seen as one of the most developed in the world, ARM has adopted this as a corporate standard in health and safety provision to all sites worldwide. To this end, the British Safety Council was engaged to audit its two largest sites outside the UK in 2006; Sunnyvale, California and Bangalore, India. Building on the results of this, ARM has now developed a global internal audit system, which enables the implementation of a consistent programme of health and safety provision worldwide. In the UK, there is a health and safety committee and all other ARM offices have fire wardens and first aiders. Health and safety is high on the agenda and there has been an increase in the amount of communication with employees particularly on occupational health matters. Health and safety issues are communicated through different media including the intranet and an extensive health and safety workshop is run as part of the Group's induction process.

Business continuity planning

The Group has developed disaster recovery plans for all of its operations worldwide, regardless of their size, to enable business to continue should a serious event or incident occur. These plans are designed to protect the interests of ARM's stakeholders – people, property and other assets – and to provide facilities and infrastructure to reinstate business operations as quickly as possible after the event.

Directors' report/ UK reporting

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

Principal activities and review of business

The principal activities of the Group and its subsidiaries are the licensing, marketing, research and development of RISC-based microprocessors, physical IP and systems. The nature of the global semiconductor industry is such that most of its business is conducted overseas and, to serve its customers better, the Group has sales offices around the world. These include six offices in the US and offices in Shanghai and Beijing, PR China; Shin-Yokohama, Japan; Seoul, South Korea; Taipei, Taiwan; Kfar Saba, Israel; Paris, France; Munich, Germany and Bangalore, India. Design offices are based in Cambridge, Maidenhead, Sheffield and Blackburn, UK; Sophia Antipolis and Grenoble, France; Leuven-Heverlee, Belgium; Aachen and Grasbrunn, Germany; Trondheim, Norway; Sentjerne, Slovenia; Austin, Texas, Olympia, Washington and Sunnyvale, California in the US and Bangalore, India. More information about the business and key performance indicators are set out in the business review comprising the Chairman's statement on pages 9 and 10, the Chief Executive Officer's review of operations on pages 11 to 13, and the financial review on pages 14 to 21.

Future developments

The Group's stated objective is to establish a global standard for RISC architecture and physical IP for the embedded microprocessor market. The directors believe that, in order to achieve this goal, it is important to expand the number and range of potential customers for its technology. The Group intends to enter into licence agreements with new customers and to increase the range of new technology supplied to existing customers. Relationships will continue to be established with third-party tools and software vendors to ensure that their products will operate with the ARM architecture. As a result of its position as an emerging standard in its industry, the Group is presented with many opportunities to acquire complementary technology or resources and it intends to continue to make appropriate acquisitions from time to time.

Going concern

After reviewing the 2008 budget and longer-term plans, the directors are satisfied that, at the time of approving the financial statements, it is appropriate to adopt the going concern basis in preparing the financial statements of both the Group and the parent company.

Dividends

The directors recommend a final dividend in respect of the year to 31 December 2007 of 1.2 pence per share which, subject to approval at the Annual General Meeting on 13 May 2008, will be paid on 21 May 2008 to shareholders on the register on 2 May 2008. This final dividend, combined with the interim dividend of 0.8 pence per share paid during the year, makes a total of 2.0 pence per share for the year, an increase of 100% on the total dividend of 1.0 pence per share for 2006.

Share buyback programme

In accordance with the rolling authority given by shareholders at the 2007 AGM, 94.5 million shares (representing 7% of the issued share capital) of 0.05 pence each were bought back by the Company in 2007 (2006: 63.6 million shares) at a total cost of £128.6 million (2006: £76.5 million). In 2008 to date, 14.7 million shares (representing 1.1% of the issued share capital) were bought back at a cost of £13.0 million.

Research and development (R&D)

R&D is of major importance and, as part of its research activities, the Group collaborates closely with universities worldwide and plans to continue its successful engagement with Michigan University. Key areas of product development for 2008 include the development of further high-power, high-performance engines for both data and control applications such as ARM cores based on symmetric multiprocessor and superscalar technology. The Group is investing in future physical IP development including low-power, low-leakage technologies for both bulk CMOS and silicon on insulator (SOI) processes to ensure leadership in this market. In addition, the Group will deliver development tools, graphics processors and fabric IP to enable its customers to design and programme systems-on-chip (SoCs).

The Group incurred R&D expenses of £84.0 million in 2007, representing 32.4% of revenues, compared with £84.9 million in 2006. R&D expenses have been charged to the income statement since the requirements for capitalisation were not met. The requirements for capitalisation are considered in more detail in note 1 on page 57.

Donations

During the year the Group made donations for charitable purposes of £41,214 (2006: £44,831). The total amounts given for each such purpose were:

Local Cambridge charities	£10,331
Promotion of education	£4,957
Wider understanding of science, maths and information technology	£15,628
Medical research	£6,015
Relief of poverty	£2,603
Environmental protection and animal welfare	£550
Other	£1,130

ARM employees are encouraged to offer their time and expertise to help charities and other groups in need. The Group operates a gift matching system for employee fundraising. The Group does not make any political donations.

Directors in the year

The following served as directors of the Company during the year ended 31 December 2007:

Doug Dunn OBE (Chairman)
Warren East (Chief Executive Officer)
Tim Score (Chief Financial Officer)
Tudor Brown (Chief Operating Officer)
Mike Muller (Chief Technology Officer)
Mike Inglis (Executive Vice President, Sales and Marketing)
Simon Segars (General Manager, Physical IP Division from September 2007 and previously Executive Vice President, Business Development)
Lucio Lanza (independent non-executive director)
Kathleen O'Donovan (independent non-executive director)
Philip Rowley (independent non-executive director and financial expert)
John Scarisbrick (independent non-executive director)
Jeremy Scudamore (senior independent non-executive director)
Young Sohn (independent non-executive director – appointed 2 April 2007)
Peter Cawdron (independent non-executive director – resigned 15 May 2007)

(See pages 22 to 23 for the directors' biographies.)

Election and re-election of directors

In accordance with Article 79 of the Group's articles of association, Doug Dunn, Tudor Brown, Mike Muller, Philip Rowley, John Scarisbrick, Jeremy Scudamore, Simon Segars and Tim Score will retire by rotation at the Company's Annual General Meeting and will seek re-election at that meeting.

Directors' shareholdings in the Company

The interests of the directors in the Company's ordinary shares of 0.05 pence, all of which were beneficially held, are disclosed in the remuneration report on page 41.

The additional information required for shareholders as a result of the implementation of the EU Takeovers Directive is set out below:

Share capital

As at 31 December 2007, ARM's share capital comprised a single class of ordinary shares of 0.05 pence each and there were 1,344,055,696 ordinary shares in issue (2006: 1,389,907,834) of which 65,201,176 ordinary shares were held in treasury (2006: 49,500,000). The rights attached to treasury shares are restricted in accordance with the Companies Acts. The rights attached to ordinary shares are as follows:

- 1 On a show of hands at a general meeting, every shareholder present in person (or, in the case of a corporation, present at the meeting by way of a representative) and entitled to vote shall have one vote and every proxy present who has been duly appointed by a shareholder entitled to vote on the resolution has one vote;
- 2 On a poll, every shareholder present in person (or in the case of a corporation, present at the meeting by way of a representative) or by proxy and entitled to vote shall have one vote for every ordinary share held;
- 3 Shareholders are entitled to a dividend where declared or paid out of profits available for such purposes; and
- 4 Shareholders are entitled to participate in a return of capital on a winding-up.

The notice of the AGM specifies deadlines for exercising voting rights and appointing a proxy or proxies to vote in relation to resolutions to be passed at the AGM. All proxy votes are counted and the numbers for, against or withheld in relation to each resolution are announced at the AGM and published on ARM's website after the meeting.

There are no restrictions on the transfer of ordinary shares in ARM other than:

- Restrictions that may from time to time be imposed by laws and regulations (for example, those relating to market abuse and insider dealing);
- Restrictions that may be imposed pursuant to the Listing Rules of the Financial Services Authority under which certain employees of ARM require the approval of the Company to deal in shares;
- Restrictions on the transfer of shares that may be imposed under article 61.2 of ARM's articles of association or under Part 22 of the Companies Act 2006, in either case following a failure to supply information required to be disclosed following service of a request under section 793 of the Companies Act 2006; and
- Restrictions on transfer of shares held under certain of the Company's employee share plans while they remain subject to the plan.

Substantial shareholdings

The directors are aware of the following substantial interests in the issued share capital of the Company as at 21 March 2008:

	Percentage of issued ordinary share capital
Janus Capital Corporation	13.37%
Fidelity Investments	8.63%
Thornburg Investment Management	7.57%
Capital Group Companies	5.96%
Invesco	5.23%
Wellington Management Company	5.02%
Legal and General Investment Management	4.01%

Save for the above, the Company has not been notified, as at 21 March 2008, of any material interest of 3% or more or any non-material interest exceeding 10% of the issued share capital of the Company.

Appointment of directors

ARM shareholders may by ordinary resolution appoint any person to be a director. ARM must have not less than two and no more than 16 directors holding office at all times. ARM may by ordinary resolution from time to time vary the minimum and/or maximum number of directors.

At each AGM, any director who was elected or last re-elected at or before the AGM held in the third calendar year before the then current calendar year must retire by rotation. A retiring director is eligible for re-election unless the directors have agreed otherwise.

The directors may appoint a director to fill a casual vacancy or as an additional director to hold office until the next AGM, who shall then be eligible for election.

Articles of association

ARM's articles of association may be amended only by a special resolution at a general meeting of shareholders. At the 2008 AGM, a special resolution will be put to shareholders proposing amendments to ARM's existing articles of association in order to accommodate the provisions of the new Companies Act 2006 relating to directors' conflicts of interests. For a more detailed explanation of the proposed amendments, see the Circular and Notice of AGM 2008.

Directors' authority

The directors are responsible for the management of the business of ARM and may exercise all powers of ARM subject to applicable legislation and regulation and the memorandum and articles of association.

At the 2007 AGM, the directors were given authority to buy back a maximum number of 133,361,000 ordinary shares at a minimum price of 0.05 pence each. The maximum price was an amount equal to 105% of the average of the closing mid market prices of ARM's ordinary shares as derived from the London Stock Exchange Daily Official List for the five business days immediately preceding the day on which such ordinary shares are contracted to be purchased. This authority will expire at the earlier of the conclusion of the 2008 AGM or 15 August 2008.

Accordingly, resolution 14 will be proposed as a special resolution at the 2008 AGM to give ARM authority to acquire up to 127,208,000 ordinary shares following expiry of the current authority. The directors will use this authority only after careful consideration, taking into account market conditions prevailing at the time, other investment opportunities, appropriate gearing levels and the overall position of ARM. In particular, this authority will be exercised only if the directors believe that it is in the best interests of shareholders generally and will increase earnings per share.

The articles of association authorise the directors to allot up to £170,500 in nominal amount of ordinary shares. Further, the directors have authority to allot ordinary shares for cash in connection with a Rights Issue (as defined in the articles of association) up to the aggregate nominal amount of £170,500 or, otherwise than in connection with a Rights Issue, up to an aggregate nominal amount of £25,500, in each case as if section 89(1) of the Companies Act 1985 did not apply to such allotment. The period of authorisation will expire at the earlier of the conclusion of the 2009 AGM or 25 April 2009.

Change of control

All of ARM's equity-based plans contain provisions relating to a change of control. Outstanding awards and options would normally vest and become exercisable on a change of control, subject to the satisfaction of any performance conditions at that time.

There are no significant agreements to which ARM is a party that take effect, alter or terminate upon a change of control.

Disabled persons

The Group has a strong demand for highly qualified staff and, as such, disability is not seen to be an inhibitor to employment or career development. In the event of any staff becoming disabled while with the Group, their needs and abilities would be assessed and the Group would, where possible, seek to offer alternative employment to them if they were no longer able to continue in their current role.

Employee involvement

As the Group is an IP enterprise, it is vital that all levels of staff are consulted and involved in its decision-making processes. To this end, internal conferences and communications meetings are held regularly which involve employees from all parts of the Group in discussions on future strategy and developments. Furthermore, employee share ownership is encouraged and all employees are able to participate in one of the Group's schemes to encourage share ownership. The Group has an informal and delegated organisational structure. It does not presently operate any collective agreements with any trade unions.

Policy on payment of creditors

The Group's policy is to pay suppliers before the end of the month following the month of receipt of the invoice, unless terms have been specifically agreed in advance. This policy and any specific terms agreed with suppliers are made known to the appropriate staff and to suppliers on request. Trade creditors of the Group at 31 December 2007 were equivalent to ten days' purchases for the Group (2006: nine days) and nil days for the Company in both years.

Financial instruments

The Group's financial risk management and policies and exposure to risks in relation to financial instruments are detailed in note 1c.

Annual General Meeting (AGM)

The AGM will be held at 110 Fulbourn Road, Cambridge, CB1 9NJ, UK, on 13 May 2008 at 2pm. A presentation will be made at this meeting outlining recent developments in the business. The Group will convey the results of proxy votes cast at the AGM. Shareholders are invited to submit written questions in advance of the meeting. Questions should be sent to The Company Secretary, ARM Holdings plc, 110 Fulbourn Road, Cambridge CB1 9NJ.

A resolution to reappoint PricewaterhouseCoopers LLP as auditors to the Group will be proposed at the AGM. Details of other resolutions to be proposed at the meeting are set out in the Circular and Notice of AGM 2008 which will be made available to all shareholders together with a proxy card.

Statement of directors' responsibilities

The directors are responsible for preparing the annual report, the directors' remuneration report and the Group and the parent company 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 prepared the Group financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union, and the parent company financial statements and the directors' remuneration report in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice). The Group and parent company financial statements are required by law to give a true and fair view of the state of affairs of the Company and the Group and of the profit or loss of the Group for that period.

In preparing those financial statements, the directors are required to:

- Select suitable accounting policies and then apply them consistently;
- Make judgments and estimates that are reasonable and prudent;
- State that the Group financial statements comply with IFRSs as adopted by the European Union, and with regard to the parent company financial statements, that applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- Prepare the Group and parent company financial statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business, in which case there should be supporting assumptions or qualifications as necessary.

The directors confirm that they have complied with the above requirements in preparing the financial statements.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Company and the Group and to enable them to ensure that the Group financial statements comply with the Companies Act 1985 and Article 4 of the IAS Regulation and the parent company financial statements and the directors' remuneration report comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the Group's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

[Disclosure of information to auditors](#)

So far as each director is aware, there is no relevant audit information of which the Group's auditors are unaware. Each director has taken all steps that he or she ought to have taken in his or her duty as a director in order to make himself or herself aware of any relevant audit information and to establish that the Group's auditors are aware of that information.

By order of the board



Patricia Alsop
Company Secretary

Remuneration committee

The remuneration committee has responsibility for determining and agreeing with the board, within agreed terms of reference, the Group's policy for the remuneration of the executive directors and the individual remuneration packages for each executive director. This includes basic salary, annual bonus, the level and terms of conditional awards under the Long Term Incentive Plan and the terms of performance conditions that apply to such benefits, pension rights and any compensation payments. Where the remuneration committee considers it appropriate, the committee will make recommendations in relation to the remuneration of senior management. The committee also liaises with the board in relation to the preparation of the board's annual report to shareholders on the Group's policy on the remuneration of executive directors and in particular the directors' remuneration report, as required by the Companies Act 1985, the Combined Code and the Listing Rules of the Financial Services Authority. The committee's terms of reference are published on the company's website at www.arm.com.

The committee is chaired by Jeremy Scudamore and the other members are Kathleen O'Donovan and Young Sohn, who was appointed in place of Peter Cawdron on 15 May 2007. The committee met four times during 2007. Given their diverse experience, these three independent non-executive directors are able to offer a balanced view and international expertise in relation to remuneration issues for the Group. The committee has access to professional advice from external advisers (generally appointed by the Executive Vice President, Human Resources) in the furtherance of its duties and makes use of such advice. During 2007, KPMG provided general advice on remuneration and benefits, Linklaters provided legal services, Deloitte and Monks both provided salary survey data, Kepler Associates provided independent verification of TSR calculations for the Long Term Incentive Plan and the Executive Vice President, Human Resources, also provided advice to the committee and to the Group. Monks is an associate of the Group's external auditor and these services were approved by the audit committee as in accordance with the procedure described in the corporate governance report. The Chief Executive Officer and the Executive Vice President, Human Resources, normally attend for part of remuneration committee meetings. No director is involved in deciding his or her own remuneration.

The Deferred Annual Bonus Plan for executive directors and senior managers and the Employee Equity Plan for all other employees were approved by shareholders at the 2006 AGM. These plans brought the Group's remuneration structure more closely in line with UK market norms, increased alignment between remuneration and financial performance and strengthened the retention aspect of the deferred bonus. Cessation of option grants to executive directors (other than in exceptional circumstances) and the reduction from three plans to two for executive directors and senior managers, together with the move away from options to shares for all employees, reduces potential dilution and simplifies remuneration arrangements.

Remuneration policy

The remuneration committee, in its deliberations on the remuneration policy for the Group's executive directors, seeks to give full consideration to the principles set out in the Combined Code. The committee is able to consider corporate performance on environmental, social and corporate governance issues when setting the remuneration of executive directors. The committee also monitors developments in accounting for equity-based remuneration on an ongoing basis.

The Group operates a remuneration policy and framework for executive directors designed to ensure that it attracts and retains the high quality management skills necessary to achieve a high level of corporate performance, in line with the best interests of shareholders. This policy seeks to provide rewards and incentives for the remuneration of executive directors that reflect their performance and align with the objectives of the Group. These comprise a mix of performance-related and non-performance-related remuneration. The committee believes that a director's total remuneration should seek to recognise his worth in the external market and, to this end, operates a policy of paying base salaries which are in line with the market median, as part of a total remuneration package which is upper quartile. The committee believes that this is justified, recognising that more than 50% of total potential remuneration is performance-related. The committee obtains information about the external market from various independently published remuneration surveys and is committed to benchmarking the total remuneration package.

The nature of the Group's development has meant that there has been a good deal of focus on the attainment of short-term objectives with a high level of variable remuneration. From 2007 onwards, variable remuneration consists of two performance-related elements: annual bonus and a conditional award under the Long Term Incentive Plan. A shareholding guideline is in place for executive directors and certain senior managers who are required to build up a holding of shares in the Company over a period of five years. The shareholdings may be built up of shares received through earlier grants under the Company's share option schemes and/or the Long Term Incentive Plan and/or the Deferred Annual Bonus Plan and, in the case of executive directors, the required holding is 100% of basic salary.

Incentive arrangements

The remuneration committee aims to ensure that individuals are fairly rewarded for their contribution to the success of the Group. The various incentive schemes that comprise the remuneration packages of executive directors and senior managers are described later in this report:

Deferred Annual Bonus Plan

There is a strong variable element to executive directors' remuneration and a bonus of up to 125% of base salary (after application of a personal performance multiplier which flexes the payment by 0.75 to 1.25) can be earned through the Deferred Annual Bonus Plan (DAB) if all targets are met. The personal performance multiplier depends on the achievement of pre-determined objectives which are reviewed and approved by the committee each year. These include key strategic objectives related to each director's role and responsibilities including compliance with the Management Charter which is designed to foster employee development, understanding of the overall vision and strategy of the Group and good governance.

There is compulsory deferral of shares of 50% of the bonus earned and an opportunity to earn an equity match of up to 2:1, subject to achievement of an EPS performance condition. Deferred shares and any matching shares earned will normally be transferred three years from the date of award. Payment of bonus for 2007 was subject to the achievement of US dollar revenue and EPS targets set by the remuneration committee, which were directly related to the Group's financial results. The bonuses payable to executive directors in respect of performance during 2007 are shown in the table on page 46 and are in the range 37.0% to 38.6% of base salary, 50% of which was compulsorily deferred into shares. At EPS growth equal to the increase in the Consumer Prices Index (CPI) plus 4% per annum, the deferred shares will be matched on a 0.3:1 basis, rising to 2:1 when EPS growth is in excess of CPI plus 12% per annum. The deferred shares can be forfeited in the event of gross misconduct and the matching shares are subject to forfeiture for "bad leavers".

For 2008, 50% of bonus is dependent on achieving a US dollar revenue target and 50% on achieving a normalised operating profit target, which the committee believes have been set at challenging but motivational levels. These targets are directly related to the Group's financial results and encourage achievement of the Group's short-term financial goals, while the deferral and matching elements encourage a longer term view of the success of the Group. Maximum bonus is 125% of base salary depending on the personal performance multiplier described above.

Existing option schemes

The grant of options under the existing share option schemes ceased in 2006 when the DAB and the Employee Equity Plan were approved by shareholders. The Employee Equity Plan has the facility for option grants to be made, but this will be done only in exceptional circumstances. The existing option grants to executive directors remain available for exercise and vesting in accordance with the rules of the relevant schemes. In line with practice among the Group's peers in the technology sector, there are generally no performance conditions attached to the issue or exercise of discretionary options under the existing schemes, except for those issued to executive directors where performance conditions based on real EPS growth apply. Share options issued to executive directors prior to their appointment to the board of the Group do not have performance conditions attached to them. However, discretionary options issued to executive directors after their appointment to the board of the Group do have performance conditions attached to them. These discretionary options will vest after seven years, but may vest after three years from grant to the extent that the performance conditions are satisfied.

The performance conditions applicable to the Long Term Incentive Plan are described in more detail below and are based on TSR rather than EPS, providing the link to performance against an appropriate peer group.

These performance conditions were selected having regard to the position of the Group within its sector and the nature of the companies against which it competes to attract and retain high calibre employees. The committee believes that the performance conditions represent the correct balance between being motivational and challenging.

Pensions

The Group does not operate its own pension scheme but makes payments into a Group personal pension plan, which is a money purchase scheme. For executive directors, the rate of Group contribution is 10% of the executive's basic salary.

Service agreements

Executive directors have "rolling" service contracts that may be terminated by either party on one year's notice. These agreements provide for each of the directors to provide services to the Group on a full-time basis and contain restrictive covenants for periods of three to six months following termination of employment relating to non-competition, non-solicitation of the Group's customers, non-dealing with customers and non-solicitation of the Group's suppliers and employees. In addition, each service contract contains an express obligation of confidentiality in respect of the Group's trade secrets and confidential information and provides for the Group to own any intellectual property rights created by the directors in the course of their employment.

The dates of the service contracts of each person who served as an executive director during the financial year are as follows:

Director	Date
Warren East	29 January 2001
Tim Score	1 March 2002
Tudor Brown	3 April 1996
Mike Inglis	17 July 2002
Mike Muller	31 January 1996
Simon Segars	4 January 2005

Where notice is served to terminate the appointment, whether by the Group or the executive director, the Group in its absolute discretion is entitled to terminate the appointment by paying to the executive director his salary in lieu of any required period of notice.

Non-executive directors

During 2007, the Chairmen of the audit and remuneration committees and the senior independent director each received a total fee of £41,000 per annum and the other non-executive directors each received a total fee of £36,000 per annum. These fees were arrived at by reference to fees paid by other companies of similar size and complexity, and reflected the amount of time non-executive directors were expected to devote to the Group's activities during the year, which is between 10 and 15 working days a year. The remuneration of the non-executive directors is set by the executive directors and the term of appointment is three years. Fees paid to non-executive directors are reviewed annually.

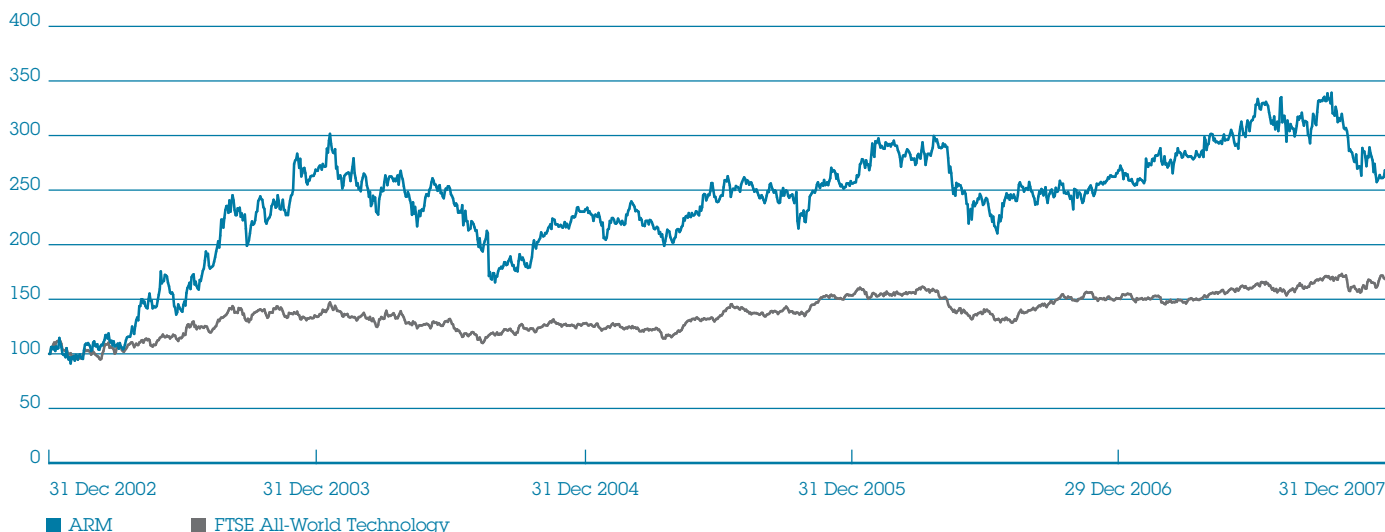
Non-executive directors do not have service contracts, are not eligible to participate in bonus or share incentive arrangements and their service does not qualify for pension purposes or other benefits. No element of their fees is performance-related. Share options held by Lucio Lanza were granted prior to the Group's acquisition of Artisan.

Performance graphs

A performance graph showing the Company's total shareholder return (TSR) together with the TSR for the FTSE All-World Technology Index from 31 December 2002 is shown below. The TSR has been calculated in accordance with the Directors' Remuneration Report Regulations 2002.

The TSR for the Company's shares was 167% over this period compared with 68% for the FTSE All-World Technology Index for the same period.

ARM total shareholder return performance from 31 December 2002 to 31 December 2007



The directors consider the FTSE All-World Technology Index to be an appropriate choice as the Index contains companies from the US, Asia and Europe and therefore reflects the global environment in which the Group operates. In addition, the Index includes many companies that are currently the Group's customers, as well as companies which use ARM technology in their end products.

Directors' shareholdings in the Company

The directors' beneficial interests in the Company's ordinary shares of 0.05 pence, which excludes interests under its share option schemes, Long Term Incentive Plan and Deferred Annual Bonus Plan, are set out below.

Director	At date of report Number	31 December 2007 Number	31 December 2006 Number
Warren East	741,603	627,480	332,480
Tim Score	343,549	247,250	147,250
Tudor Brown	1,766,814	1,655,636	1,755,636
Mike Inglis	226,609	149,771	129,771
Mike Muller	1,971,750	1,911,860	1,911,860
Simon Segars	224,070	172,735	172,735
Doug Dunn	48,000	48,000	48,000
Lucio Lanza	1,277,291	1,277,291	1,277,291
Kathleen O'Donovan	—	—	—
Philip Rowley	50,000	50,000	50,000
John Scarisbrick	10,800	10,800	10,800
Jeremy Scudamore	125,000	125,000	125,000
Young Sohn (appointed 2 April 2007)*	159,000	—	—
Peter Cawdron (resigned 15 May 2007)*	n/a	98,000	98,000

* At date of appointment, retirement or resignation.

In addition to the interests disclosed above, all the executive directors (together with all the employees of the Group) are potential beneficiaries of the ARM Holdings plc Employee Share Ownership Plan. They are, therefore, treated as interested in all the shares held by this trust, being 1,201,434 ordinary shares at 31 December 2007 (and 1,201,434 ordinary shares at 31 December 2006). The executive directors also have interests in dividend shares that could be awarded under the Long Term Incentive Plan, the amount of which will depend on the extent to which the performance criteria are satisfied and the dividends declared during the performance period. Changes in directors' interests in the Company's shares that have taken place in the period from 31 December 2007 to the date of approval of the remuneration report are shown above.

Auditable information

The following information has been audited by the Group's auditors, PricewaterhouseCoopers LLP, as required by Schedule 7A to the Companies Act 1985.

Interests in share options

Details of discretionary options beneficially held by directors are set out below:

Director	As at 1 January 2007 Number	Granted Number	Exercised Number	Lapsed Number	As at 31 December 2007 Number	Exercise price £	Earliest date of exercise	Expiry date
Warren East	8,480	—	—	—	8,480	1.224	11/03/02	10/03/09*
	3,187	—	—	—	3,187	6.155	22/05/03	21/05/10*
	20,962	—	—	(20,962)	—	6.155	22/05/01	21/05/07†
	62,909	—	—	—	62,909	3.815	22/05/04	22/05/08***
	100,000	—	—	—	100,000	2.465	19/04/05	19/04/09***
	914,285	—	(914,285)	—	—	0.4375	30/01/06	30/01/10***
	400,000	—	—	—	400,000	1.25	30/01/07	30/01/11***
	592,417	—	—	—	592,417	1.055	04/02/08	04/02/12***
	573,585	—	—	—	573,585	1.325	01/02/09	01/02/13***
	2,675,825	—	(914,285)	(20,962)	1,740,578			
Tim Score	206,896	—	—	—	206,896	2.465	19/04/05	19/04/09***
	777,142	—	(777,142)	—	—	0.4375	30/01/06	30/01/10***
	320,000	—	—	—	320,000	1.25	30/01/07	30/01/11***
	473,934	—	—	—	473,934	1.055	04/02/08	04/02/12***
	483,019	—	—	—	483,019	1.325	01/02/09	01/02/13***
	2,260,991	—	(777,142)	—	1,483,849			

Director	As at 1 January 2007 Number	Granted Number	Exercised Number	Lapsed Number	As at 31 December 2007 Number	Exercise price £	Earliest date of exercise	Expiry date
Tudor Brown	3,736	–	–	–	3,736	6.155	22/05/03	21/05/10*
	21,264	–	–	(21,264)	–	6.155	22/05/01	21/05/07†
	2,091	–	–	–	2,091	3.35	14/05/04	13/05/11*
	22,909	–	–	–	22,909	3.35	14/05/02	13/05/08†
	50,000	–	–	–	50,000	2.465	19/04/05	19/04/09***
	731,428	–	–	–	731,428	0.4375	30/01/06	30/01/10***
	320,000	–	–	–	320,000	1.25	30/01/07	30/01/11***
	436,019	–	–	–	436,019	1.055	04/02/08	04/02/12***
	392,453	–	–	–	392,453	1.325	01/02/09	01/02/13***
	1,979,900	–	–	(21,264)	1,958,636			
Mike Inglis	223,515	–	–	–	223,515	2.1475	27/05/03	26/05/09†
	292,572	–	(292,572)	–	–	0.4375	30/01/06	30/01/10***
	288,000	–	–	–	288,000	1.25	30/01/07	30/01/11***
	379,147	–	–	–	379,147	1.055	04/02/08	04/02/12***
	339,623	–	–	–	339,623	1.325	01/02/09	01/02/13***
	1,522,857	–	(292,572)	–	1,230,285			
Mike Muller	3,736	–	–	–	3,736	6.155	22/05/03	21/05/10*
	17,615	–	–	(17,615)	–	6.155	22/05/01	21/05/07†
	2,091	–	–	–	2,091	3.35	14/05/04	13/05/11*
	22,909	–	–	–	22,909	3.35	14/05/02	13/05/08†
	50,000	–	–	–	50,000	2.465	19/04/05	19/04/09***
	288,000	–	–	–	288,000	1.25	30/01/07	30/01/11***
	398,104	–	–	–	398,104	1.055	04/02/08	04/02/12***
	339,623	–	–	–	339,623	1.325	01/02/09	01/02/13***
	1,122,078	–	–	(17,615)	1,104,463			
Simon Segars	6,155	–	–	(6,155)	–	6.155	22/05/03	21/05/07**
	6,792	–	–	–	6,792	3.35	14/05/04	13/05/11*
	33,208	–	–	–	33,208	3.35	14/05/02	13/05/08†
	40,000	–	–	–	40,000	2.465	19/04/03	18/04/09†
	325,142	–	(220,000)	–	105,142	0.4375	30/01/04	29/01/10†
	224,000	–	–	–	224,000	1.25	30/01/05	29/01/11†
	341,232	–	–	–	341,232	1.055	04/02/08	04/02/12***
	316,981	–	–	–	316,981	1.325	01/02/09	01/02/13***
	1,293,510	–	(220,000)	(6,155)	1,067,355			
Lucio Lanza	89,912	–	–	–	89,912	0.57	17/03/00	16/02/10
	7,498	–	–	–	7,498	0.22	16/05/01	15/04/11
	26,236	–	–	–	26,236	0.44	07/03/02	06/02/12
	177,615	–	–	–	177,615	0.66	11/04/04	10/03/14
	301,261	–	–	–	301,261			

* Denotes share options issued under the Group's Approved Share Option Scheme.

** Denotes share options issued under the Group's Unapproved Share Option Scheme.

*** Denotes share options issued under the Group's Unapproved Share Option Scheme with performance conditions attached.

† Denotes share options issued under the Group's Unapproved Share Option Scheme which are exercisable as follows:

25% maximum from first anniversary, 50% maximum from second anniversary, 75% maximum from third anniversary,

100% maximum on fourth anniversary.

For options granted before January 2003, the performance condition is that the Group must achieve average real EPS growth of at least 33.1% (i.e. 33.1% greater than the percentage over a performance period of three years from the start of the financial year in which the options were granted (the "performance period")).

For options granted in 2003 and 2004 the performance conditions requiring average real EPS growth of at least 33.1% were satisfied and 100% of the options vested on 1 February 2006 and 8 February 2007 respectively. For options granted in 2005 the performance conditions were satisfied to the extent that 89.44% of the options vested on 8 February 2008 and the balance will vest seven years from the date of grant.

For options granted in 2006 under the performance condition, 50% of the shares under option will vest after three years if the Group achieves average real EPS growth of 12.5% over the performance period. If average real EPS growth of at least 33.1% is achieved over the performance period, 100% of the shares under option will vest after three years. Where the average real EPS growth over the performance period is between 12.5% and 33.1%, the number of shares which vest after three years increases on a straight-line basis.

Details of options held by directors under the Group's Save As You Earn option schemes are set out below:

Director	As at 1 January 2007 Number	Granted Number	Exercised Number	As at 31 December 2007 Number	Exercise price £	Earliest date of exercise	Expiry date
Warren East	–	8,559	–	8,559	1.104	01/09/10	28/02/11
Tim Score	27,152	–	–	27,152	0.5865	01/08/08	31/01/09
Tudor Brown	–	8,559	–	8,559	1.104	01/09/10	28/02/11
Mike Inglis	9,109	–	–	9,109	1.0264	01/08/09	31/01/10

Options issued under this scheme were issued at a 15% discount to market value for grants made in 2006 and before and at a 20% discount for those granted in 2007.

Details of options exercised by directors during the year are as follows:

Director	Number of shares	Exercise price £	Market price on date of exercise £	Gains on exercise £
Warren East	914,285	0.4375	1.5254	994,623
Tim Score	777,142	0.4375	1.5250	845,124
Mike Inglis	292,572	0.4375	1.3107	255,467
Simon Segars	120,000	0.4375	1.3078	104,432
Simon Segars	100,000	0.4375	1.5300	109,250
				2,308,896

Long Term Incentive Plan

A Long Term Incentive Plan was approved by shareholders at the 2003 Annual General Meeting. Conditional share awards held by directors are as follows:

Director	Performance period ending 31 December	Award date	Market price at date of award £	As at 1 January 2007 Number	Conditional award Number	Lapsed Number	As at 31 December 2007 Number	Vesting date
Warren East	2006	3 November 2004	1.005	248,756	–	(248,756)*	–	February 2007
	2007	20 July 2005	1.165	268,240	–	–	268,240**	February 2008
	2008	8 May 2006	1.365	278,388	–	–	278,388	February 2009
	2009	8 February 2007	1.28	–	308,594	–	308,594	February 2010
				795,384	308,594	(248,756)	855,222	
Tim Score	2006	3 November 2004	1.005	199,005	–	(199,005)*	–	February 2007
	2007	20 July 2005	1.165	214,592	–	–	214,592**	February 2008
	2008	8 May 2006	1.365	234,432	–	–	234,432	February 2009
	2009	8 February 2007	1.28	–	261,719	–	261,719	February 2010
				648,029	261,719	(199,005)	710,743	
Tudor Brown	2006	3 November 2004	1.005	199,005	–	(199,005)*	–	February 2007
	2007	20 July 2005	1.165	197,425	–	–	197,425**	February 2008
	2008	8 May 2006	1.365	190,476	–	–	190,476	February 2009
	2009	8 February 2007	1.28	–	214,844	–	214,844	February 2010
				586,906	214,844	(199,005)	602,745	
Mike Inglis	2006	3 November 2004	1.005	179,104	–	(179,104)*	–	February 2007
	2007	20 July 2005	1.165	171,674	–	–	171,674**	February 2008
	2008	8 May 2006	1.365	164,835	–	–	164,835	February 2009
	2009	8 February 2007	1.28	–	187,500	–	187,500	February 2010
				515,613	187,500	(179,104)	524,009	
Mike Muller	2006	3 November 2004	1.005	179,104	–	(179,104)*	–	February 2007
	2007	20 July 2005	1.165	180,258	–	–	180,258**	February 2008
	2008	8 May 2006	1.365	164,835	–	–	164,835	February 2009
	2009	8 February 2007	1.28	–	183,594	–	183,594	February 2010
				524,197	183,594	(179,104)	528,687	
Simon Segars	2006	3 November 2004	1.005	149,254	–	(149,254)*	–	February 2007
	2007	20 July 2005	1.165	154,506	–	–	154,506**	February 2008
	2008	8 May 2006	1.365	153,846	–	–	153,846	February 2009
	2009	8 February 2007	1.28	–	179,688	–	179,688	February 2010
				457,606	179,688	(149,254)	488,040	

* The performance conditions applicable to the 2004 conditional awards were not satisfied and these awards lapsed in January 2007.

** The performance conditions applicable to the 2005 conditional awards were satisfied to the extent of 55% plus dividend shares as detailed below.

Annual grants to executive directors are normally made at a level equivalent to base salary. Conditional awards vest to the extent that the performance criteria are satisfied over a three-year performance period from 1 January of the year of award and no re-testing thereafter is possible. The performance conditions are based on the Company's TSR when measured against that of two comparator groups (each testing half of the shares comprised in the award). The first index comprises UK companies across all sectors (FTSE 350) and the second comprises predominantly US companies within the Hi Tech sector (FTSE Global Technology Index). For each comparator group, the number of shares that may vest may be up to a maximum of 200% of relevant half of the shares comprised in the conditional award if the Company's TSR ranks in the upper decile, 50% will vest in the event of median performance and between median and upper decile performance vesting will increase on a straight-line basis. Additional shares may vest to cover dividends paid by the Company during the performance period. No shares will be received for below-median performance. In addition, no shares will vest unless the committee is satisfied that there has been a sustained improvement in the underlying financial performance of the Company.

The performance conditions applicable to the conditional awards granted on 20 July 2005 were satisfied to the extent of 55% plus dividend shares which vested on 8 February 2008, as follows:

Director	Conditional award Number	Vested award Number	Dividend shares Number	Total award Number	Market value at vesting £
Warren East	268,240	147,532	3,525	151,057	143,504
Tim Score	214,592	118,026	2,820	120,846	114,804
Tudor Brown	197,425	108,584	2,594	111,178	105,619
Mike Inglis	171,674	94,420	2,256	96,676	91,842
Mike Muller	180,258	99,141	2,369	101,510	96,434
Simon Segars	154,506	84,979	2,030	87,009	82,659
Total	1,186,695	652,682	15,594	668,276	634,862

The following conditional awards over ordinary shares were made under the LTIP on 8 February 2008: Warren East 446,237; Tim Score 387,097; Tudor Brown 306,452; Mike Inglis 268,817; Mike Muller 263,441 and Simon Segars 268,817. The mid-market closing price of an ordinary share on the date of these conditional awards was 95 pence.

Deferred annual bonus plan

As described above, there is a compulsory deferral of 50% of the annual bonus earned by executive directors in the year. The emoluments detailed below include the full bonus earned, although only half has been settled in cash and the deferred elements will be settled in shares after three years. The following share awards were made on 8 February 2008 in respect of the deferred proportion of the 2007 bonus: Warren East 82,043; Tim Score 69,581; Tudor Brown 54,739; Mike Inglis 48,810; Mike Muller 48,810 and Simon Segars 47,772.

Except as described above, there have been no changes in directors' interests under the Group's share option schemes since the end of the 2007 financial year up to the date of approval of the remuneration report.

The Company's register of directors' interests contains full details of directors' shareholdings and options to subscribe and conditional awards under the LTIP.

Share prices

The market value of the shares of the Company as at 31 December 2007 was 124 pence. The closing mid-price ranged from 119.25 pence to 157.5 pence during the year.

Directors' emoluments

The emoluments of the executive directors of the Group in respect of services to the Group were paid through its wholly-owned subsidiary, ARM Limited, as were the non-executive directors with the exception of Lucio Lanza and Young Sohn who were paid through ARM Inc., and were as follows:

Director	Fees £	Basic salary £	Benefits*** £	Bonus payments† £	Subtotal £	Pension contributions £	Total 2007 £	Subtotal 2006 £	Pension contributions 2006 £	Total 2006 £
Executive										
Warren East	–	395,000	14,418	152,602	562,020	39,500	601,520	670,530	31,140	701,670
Tim Score	–	335,000	19,641	129,422	484,063	33,500	517,563	574,764	26,640	601,404
Tudor Brown	–	275,000	14,418	101,815	391,233	27,500	418,733	462,552	22,140	484,692
Mike Inglis	–	240,000	14,418	90,788	345,206	24,000	369,206	401,891	19,515	421,406
Mike Muller	–	235,000	14,418	90,788	340,206	23,500	363,706	395,793	19,515	415,308
Simon Segars	–	230,000	41,607	88,857	360,464	23,000	383,464	369,735	18,390	388,125
Sir Robin Saxby*	–	–	–	–	–	–	–	121,448	25,350	146,798
Total	–	1,710,000	118,920	654,272	2,483,192	171,000	2,654,192	2,996,713	162,690	3,159,403
Non-executive										
Doug Dunn	150,000	–	–	–	150,000	–	150,000	65,250	–	65,250
Peter Cawdron**	15,552	–	–	–	15,552	–	15,552	37,000	–	37,000
Lucio Lanza	36,000	–	–	–	36,000	–	36,000	33,000	–	33,000
Kathleen O'Donovan**	38,354	–	–	–	38,354	–	38,354	2,354	–	2,354
Philip Rowley	41,000	–	–	–	41,000	–	41,000	35,728	–	35,728
John Scarisbrick	36,000	–	–	–	36,000	–	36,000	33,000	–	33,000
Jeremy Scudamore	41,000	–	–	–	41,000	–	41,000	34,000	–	34,000
Young Sohn**	27,000	–	–	–	27,000	–	27,000	–	–	–
Mark Templeton**	–	–	–	–	–	–	–	16,500	–	16,500
Total	384,906	–	–	–	384,906	–	384,906	256,832	–	256,832
Total	384,906	1,710,000	118,920	654,272	2,868,098	171,000	3,039,098	3,253,545	162,690	3,416,235

* Sir Robin Saxby ceased to be a Chairman and a director on 1 October 2006. He was appointed as Chairman Emeritus for the year from 1 October 2006 to 1 October 2007 and in this capacity received a fee of £37,000.

** Mark Templeton's fees are for the period up to his date of resignation on 25 July 2006. Peter Cawdron's fees are for the period up to his date of resignation on 15 May 2007. Kathleen O'Donovan's fees are for the period from her appointment on 7 December 2006. Young Sohn's fees are for the period from his appointment on 2 April 2007.

*** All the executive directors receive family healthcare and annual travel insurance as part of their benefits in kind. In addition, Tim Score has the use of a company car and Warren East, Tudor Brown, Mike Inglis, Mike Muller and Simon Segars receive a car and petrol allowance. Simon Segars also has £31,587 of disturbance payments resulting from his relocation to the US.

† The bonus payments above represent the full bonus earned during 2007. According to the terms of the deferred annual bonus, 50% of this bonus is not paid in cash, but is deferred and becomes payable in shares after three years. Details of the awards made in February 2008 in respect of these deferrals are detailed above.

It is the Company's policy to allow executive directors to hold non-executive positions at other companies and to receive remuneration for their services. The board believes that experience of the operations of other companies and their boards and committees is valuable to the development of the executive directors. Details of executive directors' roles within other companies and their remuneration are as follows:

Warren East is a non-executive director of Reciva Limited and of De La Rue plc. The Group holds 1.4% of the issued share capital of Reciva Limited and more details about this investment are included in note 14 on page 76. In relation to Reciva Limited he was awarded options on 17 February 2006 which vested monthly in equal instalments as to 1,620 shares at an option price of £25.00 between January and October 2007 and as to 450 shares at an option price of £20.00 between November and December 2007 and received no other remuneration. In relation to De La Rue plc he received remuneration totalling £36,247 up to 31 December 2007, following his appointment in January 2007.

Tudor Brown is a non-executive director of ANT plc. In this capacity he received remuneration totalling £26,250 up to 31 December 2007 (2006: £30,000). Mike Inglis was a non-executive director of Superscape Group plc until March 2008. During 2007 the Group held 8.1% of the issued share capital of Superscape Group plc and more details about this investment are included in note 14 on page 75. In this capacity, Mike Inglis received remuneration totalling £22,000 up to 31 December 2007 (2006: £17,019). He also holds vested options over 13,333 shares in Superscape Group plc at an option price of 33 pence per share which will be cancelled following its acquisition by Glu Mobile, Inc. Tim Score is a non-executive director of National Express Group plc. In this capacity he received remuneration totalling £48,000 up to 31 December 2007 (2006: £45,000). Simon Segars is a non-executive director of Plastic Logic Limited and in this capacity he received remuneration totalling £15,000 up to 31 December 2007 (2006: £15,000).

All the executive directors are accruing benefits under a money purchase pension scheme as a result of their services to the Group, contributions for which were all paid during the year.

Jeremy Scudamore
Chairman of the Remuneration Committee

Independent auditors' report to the members of ARM Holdings plc/IFRS

We have audited the Group financial statements of ARM Holdings plc for the year ended 31 December 2007 which comprise the consolidated income statement, the consolidated balance sheet, the consolidated cash flow statement, the consolidated statement of changes in shareholders' equity and the related notes. These Group financial statements have been prepared under the accounting policies set out therein.

We have reported separately on the parent company financial statements of ARM Holdings plc for the year ended 31 December 2007 and on the information in the directors' remuneration report that is described as having been audited.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report and the Group financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the statement of directors' responsibilities.

Our responsibility is to audit the Group 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 Group financial statements give a true and fair view and whether the Group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation. We also report to you whether in our opinion the information given in the directors' report is consistent with the Group financial statements. The information given in the directors' report includes that specific information presented in the Chairman's statement, the Chief Executive Officer's review of operations and the financial review that is cross referred from the review of business section of the directors' report.

In addition we report to you if, in our opinion, we have not received all the information and explanations we require for our audit, or if information specified by law regarding director's remuneration and other transactions is not disclosed.

We review whether the corporate governance statement reflects the Company's compliance with the nine provisions of the Combined Code 2006 specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read other information contained in the annual report and consider whether it is consistent with the audited Group financial statements. The other information comprises only growth strategies, business highlights, the Chairman's statement, the Chief Executive Officer's review of operations, the financial review, board of directors, shareholder information, the corporate governance statement, the corporate social responsibility statement, the directors' report and that part of the remuneration report that is unaudited. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Group financial statements. Our responsibilities do not extend to any other information.

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 Group financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the Group financial statements, and of whether the accounting policies are appropriate to the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Group 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 Group financial statements.

Opinion

In our opinion:

- The Group financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Group's affairs as at 31 December 2007 and of its profit and cash flows for the year then ended;
- The Group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation; and
- The information given in the directors' report is consistent with the Group financial statements.



PricewaterhouseCoopers LLP

Chartered Accountants and Registered Auditors

London

3 April 2008

Consolidated income statement/IFRS

For the year ended 31 December

	Note	2007 £000	2006 Restated £000
Revenues			
Product revenues		242,726	247,194
Service revenues		16,434	16,060
Total revenues	2	259,160	263,254
Cost of revenues			
Product costs		(21,475)	(24,156)
Service costs		(6,630)	(6,721)
Total cost of revenues		(28,105)	(30,877)
Gross profit		231,055	232,377
Operating expenses			
Research and development		(83,977)	(84,884)
Sales and marketing		(55,298)	(53,291)
General and administrative		(52,086)	(50,224)
Profit on disposal of available-for-sale investment		–	5,270
Total operating expenses, net		(191,361)	(183,129)
Profit from operations		39,694	49,248
Investment income		5,459	6,758
Interest payable		(57)	–
Profit before tax	2, 6	45,096	56,006
Tax	7	(9,846)	(7,850)
Profit for the year	2	35,250	48,156
Earnings per share			
Basic and diluted earnings		35,250	48,156
Number of shares ('000)			
Basic weighted average number of shares		1,321,860	1,366,816
Effect of dilutive securities: Employee incentive schemes		39,301	35,145
Diluted weighted average number of shares		1,361,161	1,401,961
Basic EPS	9	2.7p	3.5p
Diluted EPS	9	2.6p	3.4p

All activities relate to continuing operations. All the profit for the year is attributable to the equity holders of the parent. The Company has opted to present its own accounts under UK GAAP. The accompanying notes are an integral part of the financial statements.

Details of dividends paid and proposed are in notes 8 and 28 of the financial statements respectively.

Consolidated balance sheet/IFRS

As at 31 December

	Note	2007 £000	2006 Restated £000
Assets			
Current assets:			
Financial assets: Cash and cash equivalents	10, 19	49,509	90,743
Short-term investments	14, 19	232	18,600
Short-term marketable securities	14, 19	1,582	19,151
Available-for-sale investments	14, 19	1,180	–
Fair value of currency exchange contracts	19	–	439
Accounts receivable	11	68,232	69,552
Prepaid expenses and other assets	12	13,089	12,229
Current tax assets		6,552	5,761
Inventories: finished goods	13	2,339	1,933
Total current assets		142,715	218,408
Non-current assets:			
Financial assets: Available-for-sale investments	14, 19	3,701	3,855
Prepaid expenses and other assets	12	2,860	1,328
Property, plant and equipment	15	9,336	10,296
Goodwill	16	420,835	427,679
Other intangible assets	17	44,264	62,913
Deferred tax assets	7	19,233	19,708
Total non-current assets		500,229	525,779
Total assets		642,944	744,187
Liabilities and shareholders' equity			
Current liabilities:			
Financial liabilities: Accounts payable	19	2,230	1,826
Fair value of currency exchange contracts	19	496	–
Current tax liabilities		3,704	5,572
Accrued and other liabilities	18	28,174	39,586
Deferred revenue		27,543	31,485
Total current liabilities		62,147	78,469
Net current assets		80,568	139,939
Non-current liabilities:			
Deferred tax liabilities	7	1,635	4,792
Total liabilities		63,782	83,261
Net assets		579,162	660,926
Capital and reserves attributable to equity holders of the Company			
Share capital	20	672	695
Share premium account		351,578	449,195
Share option reserve		61,474	61,474
Retained earnings		185,125	161,453
Revaluation reserve		(214)	(544)
Cumulative translation adjustment		(19,473)	(11,347)
Total equity		579,162	660,926

The accompanying notes are an integral part of the financial statements. The financial statements on pages 48 to 95 were approved by the board of directors on 3 April 2008 and were signed on its behalf by:



Doug Dunn
Chairman

Consolidated cash flow statement/IFRS

For the year ended 31 December

	Note	2007 £000	2006 Restated £000
Operating activities			
Profit from operations		39,694	49,248
Adjustments for:			
Depreciation and amortisation of tangible and intangible assets		26,907	26,726
Profit on disposal of available-for-sale investment		–	(5,270)
Loss on disposal of property, plant and equipment		317	63
Compensation charge in respect of share-based payments		16,786	17,437
Impairment of available-for-sale investments		2,100	–
Provision for doubtful debts		215	932
Provision for obsolescence of inventories		247	65
Movement in fair value of currency exchange contracts		935	(2,147)
Changes in working capital			
Accounts receivable		260	(18,986)
Inventories		(653)	(508)
Prepaid expenses and other assets		(3,291)	1,015
Accounts payable		404	(672)
Deferred revenue		(3,877)	11,071
Accrued and other liabilities		(7,954)	5,373
Cash generated by operations before tax		72,090	84,347
Income taxes paid		(12,265)	(21,147)
Net cash from operating activities		59,825	63,200
Investing activities			
Interest received		5,607	6,636
Purchases of property, plant and equipment	15	(4,661)	(7,189)
Proceeds on disposal of property, plant and equipment		–	31
Purchases of other intangible assets	17	(3,332)	(1,370)
Purchases of available-for-sale investments	14	(2,657)	(165)
Proceeds on disposal of available-for-sale investments		–	5,567
Maturity/(purchase) of short-term investments		35,937	(4,926)
Purchase of subsidiaries, net of cash acquired*	22	(3,357)	(17,270)
Net cash from/(used in) investing activities		27,537	(18,686)
Financing activities			
Cash received on issue of new share capital on exercise of share options	20	5,509	2,106
Proceeds received on issuance of shares from treasury		13,383	15,754
Purchase of own shares	21	(128,561)	(76,519)
Dividends paid to shareholders		(18,547)	(12,367)
Net cash used in financing activities		(128,216)	(71,026)
Net decrease in cash and cash equivalents		(40,854)	(26,512)
Cash and cash equivalents at beginning of the year		90,743	128,077
Effect of foreign exchange rate changes		(380)	(10,822)
Cash and cash equivalents at end of the year	10	49,509	90,743

* The aggregate cash outflow for purchase of subsidiaries in 2007 was £3,357,000 (2006: £17,241,000) and net cash acquired was £nil (2006: net cash of £29,000).

The accompanying notes are an integral part of the financial statements.

Consolidated statement of changes in shareholders' equity/IFRS

For the year ended 31 December

	Attributable to equity holders of the Company						
	Share capital £000	Share premium account £000	Share option reserve £000	Retained earnings* £000	Revaluation reserve** £000	Cumulative translation adjustment £000	Total £000
Balance at 31 December 2005 (restated)	693	447,091	61,474	164,810	2,921	68,012	745,001
Dividends	–	–	–	(12,367)	–	–	(12,367)
Movement on tax arising on share options	–	–	–	4,182	–	–	4,182
Purchase of own shares	–	–	–	(18,622)	–	–	(18,622)
Appropriation for future share cancellations	–	–	–	(57,897)	–	–	(57,897)
Proceeds from sale of own shares	–	–	–	15,754	–	–	15,754
Realised gain on available-for-sale investments transferred to profit for the year (net of tax of £850,000)	–	–	–	–	(2,375)	–	(2,375)
Unrealised holding losses on available-for-sale investments (net of tax of £477,000)	–	–	–	–	(1,090)	–	(1,090)
Currency translation adjustment	–	–	–	–	–	(79,359)	(79,359)
Total expense recognised directly in equity in 2006	–	–	–	(68,950)	(3,465)	(79,359)	(151,774)
Shares issued on exercise of options	2	2,104	–	–	–	–	2,106
Profit for the year (restated)	–	–	–	48,156	–	–	48,156
Credit in respect of employee share schemes	–	–	–	17,437	–	–	17,437
Balance at 31 December 2006 (restated)	695	449,195	61,474	161,453	(544)	(11,347)	660,926
Dividends	–	–	–	(18,547)	–	–	(18,547)
Movement on tax arising on share options	–	–	–	2,212	–	–	2,212
Purchase of own shares	–	–	–	(120,419)	–	–	(120,419)
Appropriation for future share cancellations	–	–	–	(8,142)	–	–	(8,142)
Cancellation of shares*	(28)	–	–	28	–	–	–
Cancellation of share premium account	–	(103,121)	–	103,121	–	–	–
Proceeds from sale of own shares	–	–	–	13,383	–	–	13,383
Unrealised holding gain on available-for-sale investments (net of tax of £146,000)	–	–	–	–	330	–	330
Currency translation adjustment	–	–	–	–	–	(8,126)	(8,126)
Total income/(expense) recognised directly in equity in 2007	(28)	(103,121)	–	(28,364)	330	(8,126)	(139,309)
Shares issued on exercise of options	5	5,504	–	–	–	–	5,509
Profit for the year	–	–	–	35,250	–	–	35,250
Credit in respect of employee share schemes	–	–	–	16,786	–	–	16,786
Balance at 31 December 2007	672	351,578	61,474	185,125	(214)	(19,473)	579,162

* **Own shares held** Offset within retained earnings is an amount of £90,000,000 (2006: £58,245,000) representing the cost of own shares held. These shares are expected to be used in part for the benefit of the Group's employees and directors to satisfy share option, restricted stock units (RSUs) and conditional share awards in future periods. Own shares held include £348,000 (2006: £348,000), being the cost of 1,201,434 (2006: 1,201,434) shares in the Company held by the Group's ESOP. Own shares also include £89,652,000 (2006: £57,897,000), being the cost of 65,201,176 (2006: 49,500,000) shares in the Company. On 11 July 2007, the 49,500,000 shares held at 31 December 2006 were cancelled. Refer to note 21 for further details on the movement on these balances in 2007.

** **Revaluation reserve** The Group includes on its balance sheet publicly traded investments, which are classified as available-for-sale. These are carried at market value. Unrealised holding gains or losses on such securities are included, net of related taxes, within the revaluation reserve. Any unrealised gains within this reserve are undistributable.

1 The Group and a summary of its significant accounting policies

1a General information about the Group

The business of the Group

ARM Holdings plc and its subsidiary companies (ARM or “the Group”) design reduced instruction set computing (RISC) microprocessors, physical IP and related technology and software and sell development systems, to enhance the performance, cost-effectiveness and power-efficiency of high-volume embedded applications.

The Group licenses and sells its technology and products to leading international electronics companies, which in turn manufacture, market and sell microprocessors, application-specific integrated circuits (ASICs) and application-specific standard processors (ASSPs) based on the Group’s architecture to systems companies for incorporation into a wide variety of end products.

By creating a network of Partners, and working with them to best utilise the Group’s technology, the Group is establishing its architecture as a RISC processor for use in many high-volume embedded microprocessor applications, including digital cellular phones, storage devices and automotive functions and for potential use in many growing markets, including smart cards, household goods and digital video.

The Group also licenses and sells development systems direct to systems companies and provides consulting and support services to its licensees, systems companies and other systems designers.

The Group’s principal geographic markets are Europe, the US and Asia Pacific.

Incorporation and history

ARM is a public limited company incorporated and domiciled under the laws of England and Wales. The registered office of the Company is 110 Fulbourn Road, Cambridge, CB1 9NJ.

The Company was formed on 16 October 1990, as a joint venture between Apple Computer (UK) Limited and Acorn Computers Limited, and operated under the name Advanced RISC Machines Holdings Limited until 10 March 1998, when its name was changed to ARM Holdings plc. Its initial public offering was on 17 April 1998.

Group undertakings include ARM Limited (incorporated in the UK), ARM Inc. (incorporated in the US), ARM KK (incorporated in Japan), ARM Korea Limited (incorporated in South Korea), ARM France SAS (incorporated in France, merged with Soisic SA during 2007 – another Group company incorporated in France), ARM Belgium NV (incorporated in Belgium), ARM Germany GmbH (incorporated in Germany), Keil™ Elektronik GmbH (incorporated in Germany), ARM Norway AS (incorporated in Norway), ARM Embedded Technologies Pvt. Limited (incorporated in India), ARM Physical IP Asia Pacific Pte. Limited (incorporated in Singapore), ARM Taiwan Limited (incorporated in Taiwan) and ARM Consulting (Shanghai) Co. Limited (incorporated in PR China).

1b Summary of significant accounting policies

The principal accounting policies applied in the presentation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

Basis of preparation

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS), as adopted by the EU, IFRIC interpretations and with those parts of the Companies Act 1985 applicable to companies reporting under IFRS. This is in accordance with the Listing Rules of the Financial Services Authority.

The consolidated financial statements have been prepared under the historical cost convention as modified by the revaluation to fair value of available-for-sale investments; share-based payments; financial assets and liabilities (including derivative instruments) at fair value through the income statement; and embedded derivatives.

Restatement

The 2006 results and balance sheet have been restated to harmonise the Group’s treatment of accounting for provisions for sabbatical leave under IFRS and US GAAP. Following the adoption of EITF 06-2 under US GAAP, the Group has re-assessed its accounting for sabbatical leave under IFRS, and has determined that provision for the cost of sabbatical leave should be made under IFRS. Previously no such provision had been made under IFRS. The change in policy has been accounted for as a prior year adjustment. This has resulted in shareholders’ equity at 31 December 2006 being reduced by £2.3 million and the profit for the year ended 31 December 2006 being reduced by £0.4 million, when compared with the amounts previously reported.

Critical accounting estimates and judgments

The preparation of these financial statements requires the directors to make critical accounting estimates and judgments that affect the amounts reported in the financial statements and accompanying notes. These estimates and judgments are summarised in note 1d.

1b Summary of significant accounting policies continued
New standards, amendments and interpretations

(a) Standards, amendments and interpretations effective in 2007

IFRS 7, "Financial instruments: Disclosures" This is a new standard on disclosures in respect of financial instruments. It replaces IAS 30 and the disclosure requirements in IAS 32 such that all disclosures relating to financial instruments are located in one place. The new requirements incorporate many of IAS 32's disclosures as well as additional qualitative and quantitative disclosures on the risks arising from financial instruments.

Amendment to IAS 1, "Capital disclosures" This requires new disclosures about entities' management of their capital resources.

Both these standards were published by the IASB in August 2005 and are effective for annual periods beginning on or after 1 January 2007. Their adoption by the Group has resulted in revised disclosure of the Group's financial risk management policies and its financial instruments but has had no impact on the classification and valuation of the Group's financial instruments.

IFRIC 8, "Scope of IFRS 2" This requires consideration of transactions involving the issuance of equity instruments, where the identifiable consideration received is less than the fair value of the equity instrument issued in order to establish whether or not they fall in the scope of IFRS 2. This standard does not have any impact on the Group's financial statements.

IFRIC 9, "Re-assessment of embedded derivatives" This clarifies that an entity should assess whether an embedded derivative is required to be separated from the host contract and accounted for as a derivative when the entity first becomes a party to the contract. Subsequent reassessment is prohibited, unless there is a change in the contract's terms, in which case it is required. This interpretation does not have any impact on the Group's financial statements.

IFRIC 10, "Interim financial reporting and goodwill" This prohibits the impairment losses recognised in an interim period on goodwill and investments in equity instruments and in financial assets carried at cost to be reversed at a subsequent balance sheet date. This interpretation does not have any impact on the Group's financial statements.

(b) Standards and interpretations early adopted by the Group

IFRS 8, "Operating segments" This supersedes IAS 14, "Segmental reporting", under which segments were identified and reported on risk and return analysis. Under IFRS 8, segments are reported based on internal reporting, bringing segment reporting in line with the requirements of US standard FAS 131. Published by the IASB in November 2006, this standard is effective for annual periods beginning on or after 1 January 2009 but has been early adopted by the Group.

IFRIC 11, "IFRS 2, Group and treasury share transactions" This interpretation provides guidance on how share-based transactions involving treasury shares or options should be accounted for. Published by the IASB in November 2006 and effective for annual periods beginning on or after 1 March 2007, this interpretation has been early adopted by the Group in 2007 but has no impact on the Group's financial statements.

(c) Standards, amendments and interpretations effective in 2007 but not relevant

Revised guidance on implementing IFRS 4, "Insurance contracts" This reflects the changes made to IFRS 4 by IFRS 7, 'Financial instruments: Disclosures'. Published by the IASB in December 2005, it applies when an entity adopts IFRS 7. As the Group does not provide insurance, this guidance is not relevant.

IFRIC 7, "Applying the restatement approach under IAS29, Financial reporting in hyper-inflationary economies" Since the Group does not operate in hyper-inflationary economies, this guidance is not relevant.

(d) Standards, amendments and interpretations that are not yet effective and have not been early adopted

Amendment to IFRS 2, "Share-based payments" This clarifies what events constitute vesting conditions and also specifies that all cancellations, whether by the Group or by another party, should receive the same accounting treatment. This may have an impact on the Group's financial statements and is currently being assessed. Published by the IASB on 17 January 2008, this amendment is effective for annual periods beginning on or after 1 January 2009.

IFRS 3, (Revised), "Business combinations" This is equivalent to FAS 141R issued by the FASB in December 2007. The revision to this standard changes accounting for business combinations. While the acquisition method is still applied, there are significant changes to the treatment of contingent payments, transaction costs and the calculation of goodwill. Published by the IASB in January 2008, the standard is applicable to business combinations occurring in accounting periods beginning on or after 1 July 2009, with earlier application permitted. This could impact the Group's financial statements in future if it makes further acquisitions.

1b Summary of significant accounting policies continued

New standards, amendments and interpretations continued

IAS 1 (Revised), "Presentation of financial statements" This new standard will require "non-owner changes in equity" to be presented separately from "owner changes in equity". As the Group currently does not have any minority interests, it will not be relevant. Published by the IASB in September 2007, this standard is effective for annual periods beginning on or after 1 January 2009.

IAS 23 (Revised), "Borrowing costs" A result of the joint short-term convergence project with the FASB, this new standard requires an entity to capitalise borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset. The option of immediately expensing those borrowing costs has been removed. This will be relevant if the Group funds acquisitions with debt in the future. Published by the IASB March 2007, this is effective for annual periods beginning on or after 1 January 2009 (prospective application).

IAS 27 (Revised), "Consolidated and separate financial statements" This is similar to FAS 160 issued by the FASB in December 2007. Both revise the accounting for transactions with non-controlling interests. Published by the IASB in January 2008. This is not relevant to the Group as it does not have any non-controlling interests.

IFRIC 12, "Service concession arrangements" This applies to contractual arrangements whereby a private sector operator participates in the development, financing, operation and maintenance of infrastructure for public sector services, for example, under private finance initiative contracts (PFI) contracts. It is not relevant for the Group. Published by the IASB November 2006, it is effective for annual periods beginning on or after 1 January 2008.

IFRIC 13, "Customer loyalty programmes relating to IAS 18, Revenue" This provides guidance on accounting for customer loyalty programmes. As the Group does not offer such incentives, it will not be relevant. Published by the IASB in June 2007, it is effective for annual periods beginning on or after 1 July 2008.

IFRIC 14, "IAS 19, The limit on a defined benefit asset, minimum funding requirements and their interaction" This provides guidance on accounting for defined benefit pension schemes. The Group does not have any such schemes and therefore it will not be relevant. Published by the IASB in July 2007, it is effective for annual periods beginning on or after 1 January 2008.

The directors expect that the adoption of these standards and interpretations in future periods will have no material impact on the financial statements when they come into effect for periods after 1 January 2008.

Consolidation

Principles of consolidation The consolidated financial statements incorporate the financial statements of the Company and all its subsidiaries. Intra-group transactions, including sales, profits, receivables and payables, have been eliminated on consolidation. All subsidiaries use uniform accounting policies for like transactions and other events and similar circumstances.

Business combinations The results of subsidiaries acquired in the year are included in the income statement from the date they are acquired. On acquisition, all of the subsidiaries' assets and liabilities that exist at the date of acquisition are recorded at their fair values reflecting their condition at that date. Revisions were made retrospectively in 2007 to goodwill recognised on acquisitions from earlier years – see note 16.

Segment reporting

The Group now accounts for segmental results under IFRS 8, which brings the disclosure in line with that presented under US GAAP per FAS 131. This has no impact on the definition of the Group's primary and secondary reporting segments nor on how items are allocated between those segments. However, it has led to revised disclosures – see note 2.

At 31 December 2007, the Group is organised on a worldwide basis into three business segments, namely the Processor Division (PD), the Physical IP Division (PIPD) and the Systems Design Division (SDD – previously known as DevSys). This is based upon the Group's internal organisation and management structure and is the primary way in which the Chief Operating Decision Maker (CODM) and the rest of the board are provided with financial information.

Segment expenses are expenses that are directly attributable to a segment together with the relevant portion of other expenses that can reasonably be allocated to the segment. Foreign exchange gains or losses, gains or losses on the disposal of available-for-sale investments, investment income, interest payable and tax are not allocated by segment.

Segment assets and liabilities include items that are directly attributable to a segment plus an allocation on a reasonable basis of shared items. Corporate assets and liabilities are not included in business segments and are thus unallocated. At 31 December 2007 and 2006, these comprise cash and cash equivalents, short-term investments, short-term marketable securities, tax-related and other assets and the fair value of currency exchange contracts. Any current and deferred tax assets and liabilities are also not included in business segments and are thus unallocated.

Foreign currency translation

(a) Functional and presentation currency The functional currency of each Group entity is the currency of the primary economic environment in which each entity operates. The consolidated financial statements are presented in sterling, which is the presentation currency of the Group.

1b Summary of significant accounting policies continued

Foreign currency translation continued

(b) Transactions and balances Transactions denominated in foreign currencies have been translated into the functional currency of each Group entity at actual rates of exchange ruling at the date of transaction. Monetary assets and liabilities denominated in foreign currencies have been translated at rates ruling at the balance sheet date. Such exchange differences have been included in general and administrative expenses.

(c) Group companies The results and financial position of all the Group entities (none of which has the currency of a hyper-inflationary economy) not based in the UK are translated into sterling as follows:

- (i) Assets and liabilities for each balance sheet presented are translated at the closing rate of exchange at the balance sheet date;
- (ii) Income and expenses for each income statement presented are translated at the average monthly exchange rates during the period; and
- (iii) All resulting exchange differences are recognised as a separate component of equity, being taken directly to equity via the cumulative translation adjustment.

When a foreign operation is partially disposed of or sold, exchange differences that were recognised in equity are recognised in the income statement as part of the gain or loss on sale.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

Fair value estimation

The fair value of financial instruments traded in active markets (such as trading and available-for-sale securities) is based on quoted market prices at the balance sheet date. The quoted market price used for financial assets held by the Group is the current bid price.

The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined using valuation techniques. The Group uses a variety of methods and makes assumptions that are based on market conditions existing at each balance sheet date. The fair value of forward exchange contracts is determined using quoted forward exchange rates at the balance sheet date. The fair value of foreign currency options is based upon valuations performed by an independent bank as well as management's view of market conditions.

The carrying value less impairment provision of trade receivables and payables are assumed to approximate their fair values as this is the amount which would be receivable/payable if the assets/liabilities had crystallised at the balance sheet date. Any current tax liabilities are not included in this category.

Revenue recognition

The Group follows the principles of IAS 18, "Revenue recognition", in determining appropriate revenue recognition policies. In principle, therefore, revenue is recognised to the extent that it is probable that the economic benefits associated with the transaction will flow into the Group.

Revenue is shown net of value-added tax, returns, rebates and discounts, and after eliminating sales within the Group.

Revenue comprises the value of sales of licences, royalties arising from the resulting sale of licencees' ARM technology-based products, revenues from support, maintenance and training, consulting contracts and the sale of boards and software toolkits.

Revenue from standard licence products which are not modified to meet the specific requirements of each customer is recognised when the risks and rewards of ownership of the product are transferred to the customer.

Many licence agreements are for products which are designed to meet the specific requirements of each customer. Revenue from the sale of such licences is recognised on a percentage-of-completion basis over the period from signing of the licence to customer acceptance. Under the percentage-of-completion method, provisions for estimated losses on uncompleted contracts are recognised in the period in which the likelihood of such losses is determined. The percentage-of-completion is measured by monitoring progress using records of actual time incurred to date in the project compared with the total estimated project requirement, which approximates to the extent of performance.

Where invoicing milestones on licence arrangements are such that the receipts fall due significantly outside the period over which the customisation is expected to be performed or significantly outside its normal payment terms for standard licence arrangements, the Group evaluates whether it is probable that economic benefits associated with these milestones will flow to the Group and therefore whether these receipts should initially be included in the arrangement consideration.

1b Summary of significant accounting policies continued

Revenue recognition continued

In particular, it considers:

- Whether there is sufficient certainty that the invoice will be raised in the expected timeframe, particularly where the invoicing milestone is in some way dependent on customer activity;
- Whether it has sufficient evidence that the customer considers that the Group's contractual obligations have been, or will be, fulfilled;
- Whether there is sufficient certainty that only those costs budgeted to be incurred will indeed be incurred before the customer will accept that a future invoice may be raised; and
- The extent to which previous experience with similar product groups and similar customers support the conclusions reached.

Where the Group considers that there is insufficient evidence that it is probable that the economic benefits associated with such future milestones will flow to the Group, taking into account these criteria, such milestones are excluded from the arrangement consideration until there is sufficient evidence that it is probable that the economic benefits associated with the transaction will flow into the Group. The Group does not discount future invoicing milestones, as the effect of so doing would be immaterial.

Where agreements involve several components, the entire fee from such arrangements is allocated to each of the individual components based on each component's fair value, where fair value is the price that is regularly charged for an item when sold separately. The Group uses vendor-specific objective evidence (VSOE) of fair value to determine fair value of the individual components in multiple-component agreements. VSOE is determined by reference to licence agreements with other customers where the components are sold, where fair value is the price that is regularly charged for an item when sold separately. Where, in substance, two elements of a contract are linked and cannot be allocated to the individual components, the revenue recognition criteria are applied to the elements as if they were a single element.

Agreements including rights to unspecified products (as opposed to unspecified upgrades and enhancements) are accounted for using subscription accounting, with revenue from the arrangement being recognised on a straight-line basis over the term of the arrangement, or an estimate of the economic life of the products offered if no term is specified, beginning with the delivery of the first product.

Certain products have been co-developed by the Group and a collaborative partner, with both parties retaining the right to sell licences to the product. In those cases where the Group makes sales of these products and is exposed to the significant risks and benefits associated with the transaction, the total value of the licence is recorded as revenue and the amount payable to the collaborative partner is recorded as cost of sales. Where the collaborative partner makes sales of these products, the Group records as revenue the commission it is due when informed by the collaborative partner that a sale has been made.

In addition to the licence fees, contracts generally contain an agreement to provide post-delivery service support, in the form of support, maintenance and training which consists of the right to receive services and/or unspecified product upgrades or enhancements that are offered on a when-and-if-available basis. Fees for post-delivery service support, which takes place after customer acceptance of delivery, are generally specified in the contract. Revenue related to post-delivery service support is recognised based on VSOE of fair value, which is determined with reference to contractual renewal rates. If no renewal rates are specified, the entire fee under the transaction is amortised and recognised on a straight-line basis over the contractual post-delivery service support period. Where renewal rates are specified, revenue for post-delivery service support is recognised on a straight-line basis over the period for which support and maintenance is contractually agreed by the Group with the licensee.

If the amount of revenue recognised exceeds the amounts invoiced to customers, the excess amount is recorded as amounts recoverable on contracts within accounts receivable.

The excess of licence fees and post-delivery service support invoiced over revenue recognised is recorded as deferred revenue.

Sales of software, including development systems, which are not specifically designed for a given licence (such as off-the-shelf software) are recognised upon delivery, when the significant risks and rewards of ownership have been transferred to the customer. At that time, the Group has no further obligations except that, where necessary, the costs associated with providing post contract support (PCS) have been accrued. Services (such as training) that the Group provides which are not essential to the functionality of the IP are separately stated and priced in the contract and, therefore, accounted for separately. Revenue is recognised as services are performed and it is probable that the economic benefits associated with the transaction will flow into the Group.

Royalty revenues are earned on sales by the Group's customers of products containing ARM technology. Royalty revenues are recognised when it is probable that the economic benefits associated with the transaction will flow to the Group and the amount of revenue can be reliably measured.

1b Summary of significant accounting policies continued

Revenue recognition continued

Revenue from consulting is recognised when the service has been provided and all obligations to the customer under the consulting agreement have been fulfilled. For larger consulting projects containing several project milestones, revenue is recognised on a percentage-of-completion basis as milestones are achieved. Consulting costs are recognised when incurred.

As disclosed above, in accordance with IAS 8, "Accounting policies, changes in accounting estimates and errors", the Group makes significant estimates in applying its revenue recognition policies. In particular, as discussed in detail above, estimates are made in relation to the use of the percentage-of-completion accounting method, which requires that the extent of progress toward completion of contracts may be anticipated with reasonable certainty. The use of the percentage-of-completion method is itself based on the assumption that, at the outset of licence agreements, there is an insignificant risk that customer acceptance is not obtained. The Group also makes assessments, based on prior experience, of the extent to which future milestone receipts represent a probable future economic benefit to the Group. In addition, when allocating revenue to various components of arrangements involving several components, it is assumed that the fair value of each element is reflected by its price when sold separately. The complexity of the estimation process and issues related to the assumptions, risks and uncertainties inherent with the application of the revenue recognition policies affect the amounts reported in the financial statements. If different assumptions were used, it is possible that different amounts would be reported in the financial statements.

Research and development expenditure

All ongoing research expenditure is expensed in the period in which it is incurred. Where a product is technically feasible, production and sale are intended, a market exists, expenditure can be measured reliably, and sufficient resources are available to complete the project, development costs are capitalised and amortised on a straight-line basis over the estimated useful life of the respective product. The Group believes its current process for developing products is essentially completed concurrently with the establishment of technological feasibility which is evidenced by a working model. Accordingly, development costs incurred after the establishment of technological feasibility have not been significant and, therefore, no costs have been capitalised to date.

Where no internally-generated intangible asset can be recognised, development expenditure is recognised as an expense in the period in which it is incurred. Any collaborative agreement whereby a third party agrees to partially fund the Group's research and development is recognised over the period of the agreement as a credit within research and development costs.

Government grants

Grants in respect of specific research and development projects are credited to research and development costs within the income statement to match the projects' related expenditure.

Retirement benefit costs

The Group contributes to defined contribution plans substantially covering all employees in Europe and the US and to government pension schemes for employees in Japan, South Korea, Taiwan, PR China, Israel and India. The Group contributes to these plans based upon various fixed percentages of employee compensation, and such contributions are expensed as incurred.

Operating leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Costs in respect of operating leases are charged on a straight-line basis over the lease term even if payments are not made on such a basis.

Investment income

Investment income relates to interest income, which is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable.

Dividends

Distributions to equity holders are not recognised in the income statement under IFRS, but are disclosed as a component of the movement in shareholders' equity. A liability is recorded for a dividend when the dividend is approved by the Company's shareholders. Interim dividends are recognised as a distribution when paid.

Earnings per share

Basic earnings per share is calculated by dividing the earnings attributable to ordinary shareholders by the weighted average number of ordinary shares in issue during the period, excluding treasury stock and those shares held in the Employee Share Ownership Plan (ESOP) which are treated as cancelled. For diluted earnings per share, the weighted number of ordinary shares in issue is adjusted to assume conversion of all dilutive potential ordinary shares. The diluted share base for the year ended 31 December 2007 excludes incremental shares of approximately 8,786,000 (2006: 33,390,000) related to employee share options. These shares are excluded due to their anti-dilutive effect as a result of the exercise price of these shares being higher than the market price.

1b Summary of significant accounting policies continued

Property, plant and equipment

The cost of property, plant and equipment is their purchase cost, together with any incidental costs of acquisition. External costs and internal costs are capitalised to the extent they enhance the future economic benefit of the asset.

Depreciation is calculated so as to write off the cost of property, plant and equipment, less their estimated residual values, which are adjusted, if appropriate, at each balance sheet date, on a straight-line basis over the expected useful economic lives of the assets concerned. The principal economic lives used for this purpose are:

Freehold buildings	25 years
Leasehold improvements	Five years or term of lease, whichever is shorter
Computers	Three to five years
Fixtures and fittings	Five to ten years
Motor vehicles	Four years

Provision is made against the carrying value of property, plant and equipment where an impairment in value is deemed to have occurred. Asset lives and residual values are reviewed on an annual basis.

Intangible assets

(a) Goodwill Goodwill represents the excess of the fair value of the consideration paid on acquisition of a business over the fair value of the assets, including any intangible assets identified and liabilities acquired. Goodwill is not amortised but is measured at cost less impairment losses. In determining the fair value of consideration, the fair value of equity issued is the market value of equity at the date of completion, the fair value of share options assumed is calculated using the Black-Scholes valuation model, and the fair value of contingent consideration is based upon whether the directors believe any performance conditions will be met and thus whether any further consideration will be payable.

As permitted by IFRS 1, "First-time adoption of international financial reporting standards", goodwill arising on acquisitions before 1 January 2004 (date of transition to IFRS) has been frozen at the UK GAAP amounts subject to being tested for impairment at that date.

(b) Other intangible assets Computer software, purchased patents and licences to use technology are capitalised at cost and amortised on a straight-line basis over a prudent estimate of the time that the Group is expected to benefit from them, which is typically three to ten years. Costs that are directly attributable to the development of new business application software and which are incurred during the period prior to the date that the software is placed into operational use, are capitalised. External costs and internal costs are capitalised to the extent they enhance the future economic benefit of the asset.

Although an independent valuation is made of any intangible assets purchased as part of a business combination, the directors are primarily responsible for determining the fair value of intangible assets. Developed technology, existing agreements and customer relationships, core technology, trademarks and tradenames, and order backlog are capitalised and amortised over a period of one to six years, being a prudent estimate of the time that the Group is expected to benefit from them.

In-process research and development projects purchased as part of a business combination may meet the criteria set out in IFRS 3, "Business combinations", for recognition as intangible assets other than goodwill. The directors track the status of in-process research and development intangible assets such that their amortisation commences when the assets are brought into use. This typically means a write off period of one to five years.

Amortisation is calculated so as to write off the cost of intangible assets, less their estimated residual values, which are adjusted, if appropriate, at each balance sheet date, on a straight-line basis over the expected useful economic lives of the assets concerned. The principal economic lives used for this purpose are:

Computer software	Three to five years
Patents and licences	Three to ten years
In-process research and development	One to five years
Developed technology	One to five years
Existing agreements and customer relationships	Two to ten years
Core technology	Five years
Trademarks and tradenames	Four to five years
Order backlog	One year

Impairment of non-financial assets

Assets that have an indefinite useful life, for example goodwill, are not subject to amortisation but are tested annually for impairment.

Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For purposes of assessing impairment assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

1b Summary of significant accounting policies continued

Impairment of non-financial assets continued

At the date of transition to IFRS, and at the annual tests in 2006 and 2007, impairment tests showed there was no impairment with respect to goodwill. Furthermore, no trigger events have been identified that would suggest the impairment of any of the Group's other intangibles.

Financial assets

The Group does not trade in financial instruments.

The Group classifies its financial assets in the following categories: at fair value through profit or loss, loans and receivables, and available for sale. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

(a) Financial assets at fair value through profit or loss Financial assets at fair value through profit or loss are financial assets held for trading – that is, assets that have been acquired principally for the purpose of selling in the short-term. Assets in this category are classified as current assets. They are initially recognised at fair value with transaction costs being expensed in the income statement. Specifically, the Group's currency exchange contracts fall within this category. Gains or losses arising from changes in the fair value of "financial assets at fair value through profit or loss" are presented in the income statement within general and administrative expenses in the period in which they arise.

(b) Loans and receivables Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the balance sheet date. These are classified as non-current assets. "Accounts receivable" and "cash and cash equivalents" are classified as "Loans and receivables" in the balance sheet.

(c) Available-for-sale investments Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the investment within 12 months of the balance sheet date.

Publicly-traded investments are classified as available-for-sale. Initially recognised at fair value plus transaction costs on the trade date, they are revalued at market value at each period end. Unrealised holding gains or losses on such securities are included, net of related taxes, directly in equity via a revaluation reserve except where there is evidence of permanent impairment (see below).

Equity securities that are not publicly traded are also classified as available-for-sale and are recorded at fair value plus transaction costs at the trade date. Given the markets for these assets are not active, the Group establishes fair value by using valuation techniques. At 31 December 2007 and 2006, the estimated fair value of these investments approximated to cost less any permanent diminution in value, based on estimates determined by the directors.

Impairment of financial assets The Group considers at each reporting date whether there is any indication that any financial asset is impaired. If there is such an indication, the Group carries out an impairment test by measuring the assets' recoverable amount, which is the higher of the assets' fair value less costs to sell and their value in use. If the recoverable amount is less than the carrying amount an impairment loss is recognised, and the assets are written down to their recoverable amount.

In the case of equity securities classified as available for sale, a significant or prolonged decline in the fair value of the security below its cost is considered as an indicator that the securities are permanently impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any permanent impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement.

When securities classified as available-for-sale are sold or permanently impaired, the accumulated fair value adjustments recognised in equity are recycled through the income statement.

Impairment testing of trade receivables is described under "Accounts receivable" below.

Derivative financial instruments

The Group utilises currency exchange contracts to manage the exchange risk on actual transactions related to accounts receivable, denominated in a currency other than the functional currency of the business. The Group's currency exchange contracts do not subject the Group to risk from exchange rate movements because the gains and losses on such contracts offset losses and gains, respectively, on the transactions being hedged. The currency exchange contracts and related accounts receivable are recorded at fair value at each period end. Fair value is estimated using the settlement rates prevailing at the period end. All recognised gains and losses resulting from the settlement of the contracts are recorded within general and administrative expenses in the income statement. The Group does not enter into currency exchange contracts for the purpose of hedging anticipated transactions.

Cash and cash equivalents

Cash and cash equivalents includes cash in hand, deposits held at call with banks and other short-term highly liquid investments with original maturities of three months or less.

1b Summary of significant accounting policies continued

Short-term investments and short-term marketable securities

The Group considers all highly-liquid investments with original maturity dates of greater than three months but less than one year to be either short-term investments or short-term marketable securities. Any investments with a maturity date of greater than one year from the balance sheet date are classified as long-term.

Accounts receivable

Accounts receivable are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables.

Accounts receivable are first assessed individually for impairment. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments (more than 90 days overdue) are considered indicators that the trade receivable may be impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate.

Where there is no objective evidence of impairment for an individual receivable, it is included in a group of receivables with similar credit risk characteristics and these are collectively assessed for impairment.

In the case of impairment, the carrying amount of the asset(s) is reduced through the use of an allowance account, and the amount of the loss is recognised in the income statement within general and administrative costs. When a trade receivable is uncollectible, it is written off against the allowance account for trade receivables. Subsequent recoveries of amounts previously written off are credited against general and administrative costs in the income statement.

Inventories

Inventories are stated at the lower of cost and net realisable value. In general, cost is determined on a first-in, first-out basis and includes transport and handling costs. Where necessary, provision is made for obsolete, slow-moving and defective inventory.

Accounts payable

Accounts payable are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

Income taxes

The current income tax charge is calculated on the basis of tax laws enacted or substantively enacted at the balance sheet date in the countries where the Group's subsidiaries operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation and establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income taxes are computed using the liability method. Under this method, deferred tax assets and liabilities are determined based on temporary differences between the financial reporting and tax bases of assets and liabilities and are measured using enacted rates and laws that will be in effect when the differences are expected to reverse. The deferred tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction, other than a business combination, that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred tax assets are recognised to the extent that it is probable that future taxable profits will arise against which the temporary differences will be utilised.

Deferred tax is provided on temporary differences arising on investments in subsidiaries except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets and liabilities arising in the same tax jurisdiction are offset.

In the UK and the US, the Group is entitled to a tax deduction for amounts treated as compensation on exercise of certain employee share options under each jurisdiction's tax rules. As explained under "Share-based payments" below, a compensation expense is recorded in the Group's income statement over the period from the grant date to the vesting date of the relevant options. As there is a temporary difference between the accounting and tax bases, a deferred tax asset is recorded. The deferred tax asset arising is calculated by comparing the estimated amount of tax deduction to be obtained in the future (based on the Company's share price at the balance sheet date) with the cumulative amount of the compensation expense recorded in the income statement. If the amount of estimated future tax deduction exceeds the cumulative amount of the remuneration expense at the statutory rate, the excess is recorded directly in equity, against retained earnings.

As explained under "Share-based payments" below, no compensation charge is recorded in respect of options granted before 7 November 2002 or in respect of those options which have been exercised or have lapsed before 1 January 2005. Nevertheless, tax deductions have arisen and will continue to arise on these options. The tax effects arising in relation to these options are recorded directly in equity, against retained earnings.

1b Summary of significant accounting policies continued

Provisions

Provisions for restructuring costs and legal claims are recognised when: the Group has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount of the outflow can be reliably estimated.

Embedded derivatives

In accordance with IAS 39, "Financial instruments: recognition and measurement", the Group has reviewed all its contracts for embedded derivatives that are required to be separately accounted for if they do not meet certain requirements set out in the standard. From time to time, the Group may enter into contracts denominated in a currency (typically US dollars) that is neither the functional currency of the Group entity nor the functional currency of the customer or the collaborative partner. Where there are uninvoiced amounts on such contracts, the Group carries such derivatives at fair value. The resulting gain or loss is recognised in the income statement under general and administrative expenses, as shown below:

	2007 £000	2006 £000
Gain/(loss) in income statement	1,400	(898)

Share-based payments

The Group issues equity-settled share-based payments to certain employees. In accordance with IFRS 2, "Share-based payments", equity-settled share-based payments are measured at fair value at the date of grant. Fair value is measured by use of the Black-Scholes pricing model. The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight-line basis over the vesting period, based on the Group's estimate of the number of shares that will eventually vest.

The Group operates Save As You Earn (SAYE) schemes in the UK and an Employee Share Purchase Plan (ESPP) in the US. Options under the SAYE schemes are granted at a 20% (2006: 15%) discount to market price of the underlying shares on the date of grant and at a 15% discount to the lower of the market prices at the beginning and end of the scheme for the ESPP. The UK SAYE schemes are approved by the UK tax authorities, which stipulates that the saving period must be at least 36 months. The Group has recognised a compensation charge in respect of the SAYE plans and US ESPPs. The charges for these are calculated as detailed above.

The Group also has a Long Term Incentive Plan (LTIP) on which it is also required to recognise a compensation charge under IFRS 2, calculated as detailed above.

The Group has applied the exemption available, and has applied the provisions of IFRS 2 only to those options granted after 7 November 2002 and which were outstanding at 31 December 2004.

The share-based payments charge is allocated to cost of sales, research and development expenses, sales and marketing expenses and general and administrative expenses on the basis of headcount.

Employer's taxes on share options

Employer's National Insurance in the UK and equivalent taxes in other jurisdictions are payable on the exercise of certain share options. In accordance with IFRS 2, this is treated as a cash-settled transaction. A provision is made, calculated using the intrinsic value of the relevant options at the balance sheet date, pro-rated over the vesting period of the options.

Employee share ownership plans

The Group's Employee Benefit Trust (the "Trust") was set up on 16 April 1998 to administer the Group's Employee Share Ownership Plan (ESOP). The Trust is funded by loans from the Group, with its assets comprising shares in the Company. The Group recognises the assets and liabilities of the Trust in its own accounts and the carrying value of the Company's shares held by the Trust are recorded as a deduction in arriving at shareholders' funds until such time as the shares vest unconditionally to employees.

Treasury shares

Where the Group purchases its own equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs is deducted from equity attributable to the Company's equity holders until the shares are cancelled or reissued. Where such shares are subsequently sold or reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to equity holders of the Company.

Equity instruments

Equity instruments issued by the Group are recorded at the proceeds received, net of direct issue costs.

1b Summary of significant accounting policies continued

1c Financial risk management

The Group operates in the intensely competitive semiconductor industry which has been characterised by price erosion, rapid technological change, short product life cycles, cyclical market patterns and heightened foreign and domestic competition. Significant technological changes in the industry could affect operating results.

The Group's operations expose it to a variety of financial risks that include currency risk, interest rate risk, price risk, credit risk and liquidity risk.

Given the size of the Group, the directors have not delegated the responsibility for monitoring financial risk management to a sub-committee of the board. The policies set by the board of directors are implemented by the Group's finance department. The department has a policy and procedures manual that sets out specific guidelines to manage currency risk, interest rate risk, securities price risk, credit risk and liquidity risk and also sets out circumstances where it would be appropriate to use financial instruments to manage these.

Currency risk

The Group's earnings and liquidity are affected by fluctuations in foreign currency exchange rates, principally in respect of the US dollar, reflecting the fact that most of its revenues and cash receipts are denominated in US dollars, while a significant proportion of its costs are settled in sterling. The Group seeks to use currency exchange contracts and currency options to manage the US dollar/sterling risk as appropriate, by monitoring the timing and value of anticipated US dollar receipts (which tend to arise from low-volume, high-value licence deals and royalty receipts) in comparison with its requirement to settle certain expenses in US dollars. The Group reviews the resulting exposure on a regular basis and hedges this exposure using currency exchange contracts and currency options for the sale of US dollars as appropriate. Such contracts are entered into with the objective of matching their maturity with projected US dollar cash receipts.

The Group is also exposed to currency risk in respect of the foreign currency denominated assets and liabilities of its overseas subsidiaries. At present, the Group does not mitigate this risk, for example by using foreign currency intra-group loans, as it has currently no requirement for external borrowings.

At 31 December 2007, the Group had outstanding currency exchange contracts to sell \$34 million (2006: \$29 million) for sterling. In addition, the Group utilises option instruments which have various provisions that, depending on the spot rate at maturity, give either the Group or the counterparty the option to exercise. At 31 December 2007, the Group had outstanding currency options under which the Group may, under certain circumstances, be required to sell up to \$145 million (2006: \$118 million) for sterling. A common scenario with options of this type is that the spot price at expiry is such that neither the Group nor the counterparty chooses to exercise the option. The Group had \$88 million (2006: \$91 million) of accounts receivable denominated in US dollars at that date, and US dollar cash, cash equivalents, short-term investments and short-term marketable securities balances of \$78 million (2006: \$111 million). Thus the Group's currency exchange contracts and currency options at the year end potentially exceeded its US dollar current assets. This compares to 2006, when they only represented 73% of the total balance of the Group's US dollar current assets. This is because the Group has taken longer term positions through its option contracts in 2007 given the expected nature of the Group's cash flow during 2008.

The Group does not qualify for hedge accounting, and all movements in the fair value of derivative foreign exchange instruments are recorded in the income statement, offsetting the foreign exchange movements on the accounts receivable, cash, cash equivalents, short-term investments and short-term marketable securities balances being hedged.

In addition, certain customers remit royalties and licence fees in other currencies, primarily the euro. The Group is also required to settle certain expenses in euros, primarily in its French, Belgian and German subsidiaries, and as the net amounts involved are not considered significant, the Group does not take out euro currency exchange contracts.

As at 31 December 2007, if sterling had strengthened by 10% against foreign currencies with all other variables held constant, post-tax profit for the year would have been £5.6 million (2006: £3.3 million) lower, mainly as a result of the mix of financial instruments at respective year-ends. Equity would have been £9.1 million (2006: £8.8 million) lower, for the same reason.

Interest rate risk

At 31 December 2007, the Group had £54 million (2006: £128 million) of interest-bearing assets. At 31 December 2007, 79% (2006: 68%) of interest-bearing assets, comprising cash equivalents; short-term investments; short-term marketable securities; and the Group's long-term investment in W&W Communications Inc. (see note 14), are at fixed rates and are therefore exposed to fair value interest rate risk. Floating rate cash earns interest based on relevant national LIBID equivalents and is therefore exposed to cash flow interest rate risk. The proportion of funds held in fixed rather than floating rate deposits is determined in accordance with the policy outlined under "Liquidity risk" below. Other financial assets, such as available-for-sale investments, are not directly exposed to interest rate risk.

Whilst the Group had no borrowings at 31 December 2007, it did have limited level of borrowings during the year. Had interest rates been 1% higher throughout the year, interest payable would have increased by less than £0.01 million. However, a 1% decrease in the average interest rate during the year would have reduced interest income by approximately £1.0 million and profit after tax by £0.7 million.

1c Financial risk management continued

Interest rate risk continued

The Group has no derivative financial instruments to manage interest rate fluctuations in place at the year-end since it has no loan financing, and as such no hedge accounting is applied. The Group's cash flow is carefully monitored on a daily basis. Excess cash, considering expected future cash flows, is placed on either short-term or medium-term deposit to maximise the interest income thereon. Daily surpluses are swept into higher-interest earning accounts overnight.

Securities price risk

The Group is exposed to equity securities price risk on available-for-sale investments. As there can be no guarantee that there will be a future market for securities (which are generally unlisted at the time of investment) or that the value of such investments will rise, the directors evaluate each investment opportunity on its merits before committing ARM's funds. The board of directors reviews holdings in such companies on a regular basis to determine whether continued investment is in the best interests of the Group. Funds for such ventures are strictly limited in order that the financial effect of any potential decline of the value of investments will not be substantial in the context of the Group's financial results.

(i) Listed investments At present the Group's only listed investment is a minority stake in Superscape Group plc (Superscape), the carrying value of which as at 31 December 2007 was £1.2 million (2006: £1.9 million). A 10% decrease in Superscape's share price as at 31 December 2007 from 7.98 pence to 7.18 pence would have reduced the Group's post-tax profit by £nil (2006: £nil) and resulted in a £0.1 million (2006: £0.2 million) charge to other components of equity on the basis that such a reduction in value would have been deemed temporary. Superscape was acquired by Glu Mobile Inc. post year-end for 10 pence per share, this being the value that the Group had permanently impaired its investment to as at 31 December 2007.

(ii) Unlisted investments The Group has unlisted investments with a carrying value as at 31 December 2007 of £3.7 million (2006: £2.0 million). A permanent 10% fall in the underlying value of these companies as at 31 December 2007 would therefore have reduced the Group's post-tax profit by £0.4 million (2006: £0.2 million) and resulted in a £nil (2006: £nil) reduction in other components of equity.

Credit risk

Credit risk is managed on a Group basis. Credit risk arises from cash and cash equivalents, derivative financial instruments and deposits with banks and financial institutions, as well as credit exposures to customers, including outstanding receivables and committed transactions.

As at 31 December 2007, the Group has no significant concentrations of credit risk. The amount of exposure to any individual counterparty is subject to a limit, which is reassessed annually by the board of directors.

Financial instrument counterparties are subject to pre-approval by the board of directors and such approval is limited to financial institutions with at least an AA rating, or (in the case of UK building societies) had over £1 billion in assets, except in certain jurisdictions where the cash holding concerned is immaterial. At 31 December 2006 and 2007, the Group's cash, cash equivalents, short-term investments and marketable securities were deposited with major clearing banks and building societies in the UK and US in the form of money market deposits and corporate bonds for varying periods up to two years.

Over 90% of the Group's cash and cash equivalents; short-term investments and short-term marketable securities were held with global financial institutions with at least an AA rating, or (in the case of UK building societies) had over £1 billion in assets, as at 31 December 2007 and 2006.

The Group has implemented policies that require appropriate credit checks on potential customers before sales commence. The Group generally does not require collateral on accounts receivable, as many of its customers are large, well-established companies. The Group has not experienced any significant losses related to individual customers or groups of customers in any particular industry or geographic area.

The Group markets and sells to a relatively small number of customers with individually large value transactions. At 31 December 2007 and 2006 no customers accounted for more than 10% of accounts receivable. Over 80% of the year-end accounts receivable balance was owed by large, established semiconductor companies where the risk of default on monies owed is deemed negligible. The Group performs credit checks on all customers (other than those paying in advance) in order to assess their credit worthiness and ability to pay its invoices as they become due. As such, the balance of accounts receivable not owed by the large semiconductor companies is still deemed by management to be of low risk of default due to the nature of the checks performed on them, and accordingly a relatively small allowance against these receivables is in place to cover this low risk of default.

No credit limits were exceeded during the reporting period and management does not expect any losses from non-performance by these counterparties.

1c Financial risk management continued

Liquidity risk

The Group's policy is to maintain balances of cash, cash equivalents, short-term investments and short-term marketable securities, such that highly liquid resources exceed the Group's projected cash outflows at all times. Surplus funds are placed on fixed- or floating-rate deposits depending on the prevailing economic climate at the time (with reference to forward interest rates) and also on the required maturity of the deposit (as driven by the expected timing of the Group's cash receipts and payments over the short to medium term).

Management monitors rolling forecasts of the Group's liquidity reserve (comprising an undrawn borrowing facility, and cash and cash equivalents) on the basis of expected cash flow. This is carried out at both a local and a Group level – although only the parent company has access to the borrowing facility.

The table below analyses the Group's financial liabilities which will be settled on a net basis into relevant maturity groupings based on the remaining period at the balance sheet to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying balances as the impact of discounting is not significant.

	Less than six months £000	Between six months and one year £000
At 31 December 2007: Trade and other payables	2,230	–
At 31 December 2006: Trade and other payables	1,826	–

The table below analyses the Group's derivative financial instruments which will be settled on a gross basis into relevant maturity groupings based on the remaining period at the balance sheet to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying balances as the impact of discounting is not significant.

	Less than three months 000s	Over three months but less than six months 000s	Between six months and one year 000s
Forward foreign exchange contracts – held-for-trading at 31 December 2007			
Outflow	\$34,000	–	–
Inflow	£16,772	–	–
Foreign exchange options – held-for-trading at 31 December 2007			
Outflow (maximum)	\$34,000	\$36,000	\$75,000
Inflow (maximum)	£17,210	£18,152	£38,077
Forward foreign exchange contracts – held-for-trading at 31 December 2006			
Outflow	\$29,000	–	–
Inflow	£15,153	–	–
Foreign exchange options – held-for-trading at 31 December 2006			
Outflow (maximum)	\$27,000	\$37,000	\$54,000
Inflow (maximum)	£14,599	£20,095	£29,198

Capital risk management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares, sell assets to raise cash or take on debt.

During 2007, the Group's strategy, which was unchanged from 2006, was to increase its balance sheet efficiency by reducing its cash balance and looking to take on new debt facilities. In 2008, while the Group plans to continue to return cash to shareholders through share buybacks and dividends, the current uncertain economic climate has meant that the Group's focus will be on decreasing liquid resources (that is cash and cash equivalents, short-term investments and short-term marketable securities) towards its £50m target rather than on achieving a specific debt-to-equity ratio in the short term.

1c Financial risk management continued

Capital risk management continued

During the year, the Group entered into a £100 million revolving credit facility providing the Group access to funds for any corporate purpose. Whilst the Group did drawdown on this facility at various times during the year, these funds had been fully repaid, and the facility was undrawn at the balance sheet date. Any drawn amounts accrue interest at a LIBOR-plus rate whilst there is a nominal charge for the undrawn portion. Furthermore, the facility requires the Group to adhere to various financial covenants relating to EBITDA multiples and interest cover; the Group adhered to all covenants during the year.

Fair value of currency exchange contracts

The fair value of currency exchange contracts is estimated using the settlement rates. The estimation of the fair value of the liability in respect of currency exchange contracts is £496,000 at 31 December 2007 (2006: asset of £439,000). The decrease in 2007 is due to the mix of contracts, settlement rates, year-end spot rates and currency volatility. The resulting gain or loss on the movement of the fair value of currency exchange contracts is recognised in the income statement under general and administrative expenses, as shown below:

	2007 £000	2006 £000
Gain/(loss) in income statement	(935)	2,147

1d Critical accounting estimates and judgments

The preparation of financial statements in accordance with generally accepted accounting principles requires the directors to make critical accounting estimates and judgments that affect the amounts reported in the financial statements and accompanying notes. These estimates and judgments are continually evaluated and are based on historical experiences and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

Impairment of goodwill

The Group tests goodwill for impairment at least annually. This requires an estimation of the value in use of the cash generating units (CGUs) to which goodwill is allocated. As discussed in detail in note 16, estimating the value in use requires the Group to make an estimate of the expected future cash flows from the CGUs and also to choose a suitable discount rate in order to calculate the present values of those cash flows.

Revenue recognition

Revenue from the sale of licence agreements which are designed to meet the specific requirements of each customer is recognised on a percentage-of-completion method basis. Use of this method requires the directors to estimate the total project resource requirement and also any losses on uncompleted contracts.

Provisions for income taxes

The Group is subject to income taxes in numerous jurisdictions. Significant judgment is required in determining the worldwide provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Group recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

Provision for impairment of trade receivables

The Group assesses trade receivables for impairment which requires the directors to estimate the likelihood of payment forfeiture by customers.

Legal settlements and other contingencies

Determining the amount to be accrued for legal settlement requires the directors to estimate the committed future legal and settlement fees the Group is expecting to incur. Where suits are filed against the Group for infringement of patents, the directors assess the extent of any potential infringement based on legal advice and written opinions received from external counsel and then estimate the level of accrual required.

Contingent consideration for an acquisition is recognised as part of the purchase consideration if the contingent conditions are expected to be satisfied. This requires the directors to estimate the acquiree's future financial performance, typically more than one year post-acquisition.

2 Segmental reporting

At 31 December 2007 the Group is organised on a worldwide basis into three main business segments:

Processor Division (PD), encompassing those resources that are centred around microprocessor cores, including specific functions such as graphics IP, fabric IP, embedded software and configurable digital signal processing IP.

Physical IP Division (PIPD), concerned with the building blocks necessary for translation of a circuit design into actual silicon.

Systems Design Division (SDD), focused on the tools and models used to create and debug software and system-on-chip (SoC) designs.

This is based upon the Group's internal organisation and management structure and is the primary way in which the board of directors is provided with financial information. Whilst revenues are reported into four main revenue streams (namely licensing, royalties, development systems and services), the costs, operating results and balance sheets are only analysed into these three divisions.

In 2007, the Group early-adopted IFRS 8, "Operating segments". This supersedes IAS 14, "Segmental reporting", under which segments were identified and reported on risk and return analysis. Under IFRS 8, segments are reported based on internal reporting, bringing segment reporting in line with the requirements of US standard FAS 131. For the Group, the impact of this is purely presentational – as under IAS 14, the Group's business segments were still defined as PD, PIPD and SDD.

Acquisitions in 2006 were allocated to the divisions as follows: Falanx to PD and Soisic to PIPD. Goodwill on each acquisition has also been allocated into these divisions.

The following analysis is of revenues; operating costs; investment income; interest payable; profit/(loss) before tax, tax; profit/(loss) after tax; depreciation; amortisation of other intangible assets; share-based payment costs; capital expenditure; total assets and liabilities; net assets and goodwill for each segment and the Group in total.

Business segment information

	Processor Division £000	Physical IP Division £000	Systems Design Division £000	Unallocated £000	Group £000
Year ended 31 December 2007					
Segmental income statement					
Revenue	187,829	43,418	27,913	–	259,160
Operating costs	(113,901)	(62,799)	(43,006)	240	(219,466)
Investment income	–	–	–	5,459	5,459
Interest payable	–	–	–	(57)	(57)
Profit/(loss) before tax	73,928	(19,381)	(15,093)	5,642	45,096
Tax	–	–	–	(9,846)	(9,846)
Profit/(loss) for the year	73,928	(19,381)	(15,093)	(4,204)	35,250
Segmental balance sheet					
Total assets	171,653	358,292	32,160	80,839	642,944
Total liabilities	(33,562)	(14,443)	(10,307)	(5,470)	(63,782)
Net assets	138,091	343,849	21,853	75,369	579,162
Other segmental items					
Depreciation	2,756	1,800	936	–	5,492
Amortisation of other intangible assets	2,623	15,117	3,675	–	21,415
Capital expenditure	3,161	1,336	947	–	5,444
Share-based payments cost	10,575	3,356	2,855	–	16,786
Goodwill	107,265	302,050	11,520	–	420,835

2 Segmental reporting continued

Year ended 31 December 2006 (Restated)	Processor Division £000	Physical IP Division £000	Systems Design Division £000	Unallocated £000	Group £000
Segmental income statement					
Revenue	180,426	53,996	28,832	–	263,254
Operating costs	(116,076)	(67,219)	(40,503)	4,522	(219,276)
Investment income	–	–	–	6,758	6,758
Profit on disposal of available-for-sale investment	–	–	–	5,270	5,270
Profit/(loss) before tax	64,350	(13,223)	(11,671)	16,550	56,006
Tax	–	–	–	(7,850)	(7,850)
Profit/(loss) for the year	64,350	(13,223)	(11,671)	8,700	48,156
Segmental balance sheet					
Total assets	171,160	383,039	33,617	156,371	744,187
Total liabilities	(38,647)	(21,265)	(11,727)	(11,622)	(83,261)
Net assets	132,513	361,774	21,890	144,749	660,926
Other segmental items					
Depreciation	2,775	1,300	1,210	–	5,285
Amortisation of other intangible assets	1,870	15,735	3,836	–	21,441
Share-based payments cost	10,114	4,882	2,441	–	17,437
Capital expenditure	9,396	6,768	3,107	–	19,271
Goodwill	108,866	307,054	11,759	–	427,679

There are no inter-segment revenues. Unallocated operating costs are foreign exchange revaluation on monetary items, including cash and cash equivalents. Unallocated assets and liabilities include: cash and cash equivalents; short-term investments and marketable securities; some deferred tax balances; current tax and VAT. Capital expenditure comprises additions to property, plant and equipment and other intangible assets, including additions resulting from acquisitions through business combinations.

The results of each segment have been prepared using accounting policies consistent with those of the Group as a whole.

Geographical information

The Group manages its business segments on a global basis. The operations are based in three main geographical areas. The UK is the home country of the parent. The main operations in the principal territories are as follows:

- Europe
- United States
- Asia Pacific

Analysis of revenue by destination*:

	2007 £000	2006 £000
United States	96,140	92,058
Japan	41,868	40,303
Taiwan	28,358	29,531
South Korea	22,664	20,658
Netherlands	14,743	16,608
Rest of Europe	27,911	26,138
Rest of North America	13,755	19,136
Rest of Asia Pacific	13,721	18,822
	259,160	263,254

* Destination is defined as the location of ARM's customers.

The Group's exports from the UK were £217.0 million and £195.9 million for the years ended 31 December 2007 and 2006 respectively.

2 Segmental reporting continued

Analysis of revenue by origin:

	2007 £000	2006 £000
Europe*	215,371	198,386
United States	42,115	63,028
Asia Pacific	1,674	1,840
	259,160	263,254

* Includes the UK which had total revenues of £213.9 million in 2007 (2006: £195.5 million).

Analysis of revenue by revenue stream:

	2007 £000	2006 £000
Licensing	110,663	110,548
Royalties	104,150	107,814
Services	16,434	16,060
Development systems	27,913	28,832
	259,160	263,254

Analysis of non-current assets (excluding deferred tax assets):

	2007 £000	2006 £000
Europe*	11,025	13,045
United States	2,827	3,614
Asia Pacific	1,891	1,166
	15,743	17,825

* Includes the UK which had non-current assets (excluding deferred tax assets) of £10.7 million in 2007 (2006: £12.8 million).

3 Recognised income and expense

	2007 £000	2006 Restated £000
Movement on tax arising on share options	2,212	4,182
Gain/(loss) on revaluation of publicly-traded available-for-sale investments, net of tax of £146,000 (2006: £477,000)	330	(1,090)
Foreign exchange difference on consolidation	(8,126)	(79,359)
Total loss recognised directly in equity for the year	(5,584)	(76,267)
Profit for the year (2006 restated to include provision for sabbatical)	35,250	48,156
Total recognised income/(loss) for the year	29,666	(28,111)

All activities relate to continuing operations. All of the total recognised profit for the year is attributable to the equity holders of the parent.

4 Key management compensation and directors' emoluments

Key management compensation

The directors are of the opinion that the key management of the Group comprises the executive and non-executive directors of ARM Holdings plc together with the board of directors of ARM Limited. These persons have authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly. At 31 December 2007, key management comprised 17 people (2006: 17).

The aggregate amounts of key management compensation are set out below:

	2007 £000	2006 £000
Salaries and short-term employee benefits	3,858	4,170
Share-based payments	3,768	4,213
Group pension contributions to money purchase schemes	237	206
	7,863	8,589

Directors' emoluments

The aggregate emoluments of the directors of the Company are set out below:

	2007 £000	2006 £000
Aggregate emoluments in respect of qualifying services	2,868	3,254
Aggregate Group pension contributions to money purchase schemes	171	163
Aggregate gains on exercise of share options	2,309	3,804
Aggregate amounts receivable under the Long Term Incentive Plan	–	2,876
	5,348	10,097

Detailed disclosures of directors' emoluments are shown on pages 45 and 46. Details of directors' interests in share options and awards are shown on pages 41 to 45 which form part of the financial statements.

5 Employee information

The average monthly number of persons, including executive directors, employed by the Group during the year was:

	2007 Number	2006 Number
By segment		
Processor Division	962	850
Physical IP Division	449	417
Systems Design Division	290	205
	1,701	1,472
	2007 Number	2006 Number
By activity		
Research and development	1,163	961
Sales and marketing	312	302
General and administrative	226	209
	1,701	1,472
	2007 £000	2006 £000
Staff costs (for the above persons)		
Wages and salaries	84,524	83,007
Share-based payments (note 23)	16,786	17,437
Social security costs	9,603	8,480
Other pension costs	4,327	3,840
	115,240	112,764

6 Profit before tax: analysis of expenses by nature

The following items have been charged/(credited) to the income statement in arriving at profit before tax:

	2007 £000	2006 £000
Staff costs, including share-based payments (note 5)	115,240	112,764
Cost of inventories recognised as an expense (included in cost of sales)	2,781	4,951
Depreciation of property, plant and equipment – owned assets (note 15)	5,492	5,285
Amortisation of other intangible assets (note 17):		
– Cost of sales	400	310
– Research and development	10,201	9,791
– Sales and marketing	8,653	9,351
– General and administrative	2,161	1,989
Impairment of available-for-sale investments	2,100	–
Profit on disposal of available-for-sale investment	–	(5,270)
Loss on disposal of property, plant and equipment	317	63
Other operating lease rentals payable		
– Plant and machinery	11,973	13,398
– Property	5,585	5,402
Repairs and maintenance expenditure on property, plant and equipment	1,792	1,696
Trade receivables impairment	215	932
Amortisation of government grants	–	(467)
Foreign exchange gains	(240)	(4,522)

Services provided by the Group's auditor and its associates

During the year the Group (including its overseas subsidiaries) obtained the following services from the Group's auditor and its associates:

	2007 £000	2006 £000
Fees payable to the Group's auditor for the audit of the Company and consolidated financial statements	399	320
Fees payable to the Group's auditor and its associates for other services:		
– The audit of the Group's subsidiaries pursuant to legislation	296	222
– Services pursuant to section 404 of the Sarbanes-Oxley Act	649	533
– Other services pursuant to legislation	47	79
– Tax services	302	861
– All other services	129	90
	1,822	2,105

* Included within the 2007 costs are fees of £255,000 incurred in relation to the Group's initial compliance with section 404 of the Sarbanes-Oxley Act.

Fees payable to other major firms of accountants for non-audit services for 2007 amount to £1,449,000 (2006: £1,466,000).

7 Tax

Analysis of charge in the year:

	2007 £000	2006 Restated £000
Current tax	14,489	15,192
Deferred tax	(4,643)	(7,342)
Taxation	9,846	7,850

Analysis of tax on items charged to equity:

	2007 £000	2006 £000
Deferred tax credit on available-for-sale investments	146	1,327
Deferred tax credit/(charge) on outstanding share options	(657)	399
Current tax benefit on share options	(4,297)	3,783

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

	2007 £000	2006 Restated £000
Profit before tax	45,096	56,006
Profit before tax multiplied by rate of corporation tax in the UK of 30% (2006: 30%)	13,529	16,802
Effects of:		
Adjustments to tax in respect of prior years	(838)	1,220
Adjustments in respect of foreign tax rates	(895)	613
Research and development tax credits	(5,170)	(2,879)
Permanent differences – foreign exchange	(84)	(7,558)
Permanent differences – other*	(2,726)	(5,951)
Losses for which deferred tax assets were not recognised	4,824	3,394
Foreign withholding tax	912	2,450
Amortisation of other intangible assets	(1,359)	(1,546)
Change in accounting policy relating to provisions for sabbaticals	–	(23)
Timing differences in respect of share-based payments	599	1,415
Other differences	1,054	(87)
Total taxation	9,846	7,850

* Includes benefits resulting from restructuring following the acquisition of Artisan.

Deferred tax

Deferred tax is calculated in full on temporary differences under the liability method using a tax rate relevant to each tax jurisdiction.

The movement on the deferred tax account is shown below:

	2007 £000	2006 £000
At 1 January	14,916	4,440
Profit and loss credit	4,643	7,342
Adjustment in respect of share-based payments	(1,837)	399
Exchange differences	22	340
Available-for-sale investments	(146)	1,327
Change in accounting policy relating to provisions for sabbaticals	–	971
Transfer to current tax liabilities	–	757
Recognition of pre-acquisition losses	–	687
Amount acquired with subsidiary undertakings	–	(1,347)
At 31 December	17,598	14,916

During the year, as a result of the change in German and UK corporation tax rates which will be effective from 1 January 2008 and 1 April 2008 respectively, deferred tax balances have been remeasured. Deferred tax relating to temporary differences which are expected to reverse prior to the effective date is measured at 38% and 30% respectively. Deferred tax relating to temporary differences which are expected to reverse after the effective date is measured at the tax rate of 29% and 28% respectively as these are the tax rates that will apply on reversal.

7 Tax continued

Deferred tax assets have been partially recognised in respect of tax losses and other temporary differences giving rise to deferred tax assets because it is not probable that the unrecognised portion of these assets will be recovered. The amount of deferred tax assets unrecognised at 31 December 2007 is £9,574,000 (2006: £5,362,000).

No deferred tax is recognised on the unremitted earnings of overseas subsidiaries. As the earnings are continually reinvested by the Group, no tax is expected to be payable on them in the foreseeable future. If the earnings were remitted, tax of £7,981,000 would be payable.

The movements in deferred tax assets and liabilities (prior to offsetting of balances within the same tax jurisdiction as permitted by IAS 12, "Income Taxes") during the year are shown below. Deferred tax assets and liabilities are only offset where there is a legally enforceable right of offset and there is an intention to settle the balances net.

Deferred tax assets

	Amounts relating to share-based payments £000	Temporary difference on available- for-sale investments £000	Temporary differences relating to fixed assets £000	Tax losses and R&D tax credits carried forward £000	Non- deductible reserves £000	Amounts relating to share option benefits £000	Total £000
At 1 January 2007	13,315	231	5,244	13,626	3,878	–	36,294
Profit and loss (charge)/credit	3,186	593	(638)	(10,752)	4,675	–	(2,936)
Available-for-sale investments	–	(146)	–	–	–	–	(146)
Movement on deferred tax arising on outstanding share options	(1,837)	–	–	–	–	–	(1,837)
Exchange differences	–	–	–	(205)	–	–	(205)
At 31 December 2007 (prior to offsetting)	14,664	678	4,606	2,669	8,553	–	31,170
Offsetting of deferred tax liabilities							(11,937)
At 31 December 2007 (after offsetting)							19,233
At 1 January 2006 (Restated)	10,574	(1,096)	5,214	11,988	2,633	6,646	35,959
Amounts acquired with subsidiary undertakings	–	–	–	1,935	–	–	1,935
Profit and loss (charge)/credit	2,342	–	30	(5,010)	1,027	–	(1,611)
Available-for-sale investments	–	1,327	–	–	–	–	1,327
Movement on deferred tax arising on outstanding share options	399	–	–	–	–	–	399
Transfer	–	–	–	6,646	–	(6,646)	–
Recognition of pre- acquisition losses	–	–	–	687	–	–	687
Change in accounting policy relating to provisions for sabbaticals	–	–	–	–	218	–	218
Exchange differences	–	–	–	(2,620)	–	–	(2,620)
At 31 December 2006 (restated – prior to offsetting)	13,315	231	5,244	13,626	3,878	–	36,294
Offsetting of deferred tax liabilities							(16,586)
At 31 December 2006 (restated – after offsetting)							19,708

7 Tax continued

Deferred tax liabilities

	Amounts relating to intangible assets arising on acquisition £000	Other £000	Total £000
At 1 January 2007	21,378	–	21,378
Movement in respect on amortisation of intangible assets	(7,579)	–	(7,579)
Exchange differences	(227)	–	(227)
At 31 December 2007 (prior to offsetting)	13,572	–	13,572
Offsetting of deferred tax assets			(11,937)
At 31 December 2007 (after offsetting)			1,635
At 1 January 2006	29,791	757	30,548
Amount acquired with subsidiary undertakings	3,282	–	3,282
Movement in respect on amortisation of intangible assets	(8,735)	–	(8,735)
Transfer to current tax liabilities	–	(757)	(757)
Exchange differences	(2,960)	–	(2,960)
At 31 December 2006 (prior to offsetting)	21,378	–	21,378
Offsetting of deferred tax assets (restated)			(16,586)
At 31 December 2006 (after offsetting)			4,792

The deferred tax liability due after more than one year prior to offsetting is £7,213,000 (2006: £13,783,000).

8 Dividends

	2007 £000	2006 £000
Final 2005 paid at 0.50 pence per share	–	6,918
Interim 2006 paid at 0.40 pence per share	–	5,449
Final 2006 paid at 0.60 pence per share	8,013	–
Interim 2007 paid at 0.80 pence per share	10,534	–

In addition, the directors are proposing a final dividend in respect of the financial year ended 31 December 2007 of 1.2 pence per share which will absorb an estimated £15.3 million of shareholders' funds. It will be paid on 21 May 2008 to shareholders who are on the register of members on 2 May 2008.

9 Earnings per share

Basic earnings per share is calculated by dividing the earnings attributable to ordinary shareholders by the weighted average number of ordinary shares in issue during the year, excluding those held in the ESOP and treasury stock which are treated as cancelled.

For diluted earnings per share, the weighted average number of ordinary shares in issue is adjusted to assume conversion of all dilutive potential ordinary shares. The Company had two categories of dilutive potential ordinary shares during the year: those being share options granted to employees and directors where the exercise price is less than the average market price of the Company's ordinary shares during the year and the awards made under the Company's Restricted Stock Unit (RSU), Deferred Annual Bonus Plan (DAB) and Long Term Incentive Plan (LTIP) schemes. For 2007 and 2006 no shares that were allocated for awards under the LTIP were included in the diluted EPS calculation as the performance criteria could not be measured until the conclusion of the performance period.

Reconciliations of the earnings and weighted average number of shares used in the calculations are shown on the face of the income statement.

10 Cash and cash equivalents

	2007 £000	2006 £000
Cash at bank and in hand	8,162	40,477
Short-term bank deposits	41,347	50,266
	49,509	90,743

The effective interest rate on short-term deposits was 5.6% (2006: 4.7%) and these deposits have an average maturity of 11 days (2006: 38 days).

Short-term marketable securities There is a readily available market for these investments. Unrealised gains and losses on these investments are recognised directly in equity via the revaluation reserve. The Group recognises an impairment charge when the decline in fair value below cost is judged to be other than temporary. At 31 December 2007, the fair value is equal to cost (2006: £6,000 less than cost).

Cash and cash-equivalents The carrying amount approximates to fair value because of the short-term maturity of these instruments, being no greater than three months.

11 Accounts receivable

	2007 £000	2006 £000
Trade debtors (including receivables from related parties – see note 27)	45,249	48,276
Less: Provision for impairment of trade debtors	(1,504)	(2,556)
Trade debtors, net	43,745	45,720
Amounts recoverable on contracts	24,487	23,832
Current accounts receivable	68,232	69,552

Movements in the Group's provision for impairment of trade receivables are as follows:

	2007 £000	2006 £000
At 1 January	(2,556)	(2,173)
Charged/credited to income statement	(215)	(932)
Utilised/reclassification	1,253	377
Foreign exchange	14	172
At 31 December	(1,504)	(2,556)

The other classes within current accounts receivable do not contain impaired assets. See also note 19 for further disclosure regarding the credit quality of the Group's gross trade receivables.

12 Prepaid expenses and other assets

	2007 £000	2006 £000
Other receivables	2,033	2,733
Prepayments and accrued income	11,056	9,496
Current prepaid expenses and other assets	13,089	12,229
Plus: non-current prepayments and accrued income	2,860	1,328
Total prepaid expenses and other assets	15,949	13,557

13 Inventories

	2007 £000	2006 £000
Finished goods	2,673	2,020
Less: Provision for obsolescence of inventories	(334)	(87)
	2,339	1,933

14 Available-for-sale financial assets

	Short-term investments £000	Short-term marketable securities £000	Listed short-term investments £000	Total £000
At 1 January 2007	18,600	19,151	–	37,751
Reclassification from long-term investments	–	–	1,885	1,885
Cash invested in the year	20,009	8,916	–	28,925
Assets maturing in the year	(38,372)	(26,311)	–	(64,683)
Impairment charge to income statement	–	–	(1,174)	(1,174)
Revaluation through equity	–	7	469	476
Exchange differences	(5)	(181)	–	(186)
At 31 December 2007	232	1,582	1,180	2,994

	Short-term investments £000	Short-term marketable securities £000	Total £000
At 1 January 2006	23,990	8,835	32,825
Cash invested in the year	75,266	56,764	132,030
Assets maturing in the year	(80,656)	(45,260)	(125,916)
Revaluation through equity	–	22	22
Exchange differences	–	(1,210)	(1,210)
At 31 December 2006	18,600	19,151	37,751

	Listed long-term investments £000	Other long-term investments £000	Total £000
Net book value			
At 1 January 2007	1,885	1,970	3,855
Reclassification to short-term investments	(1,885)	–	(1,885)
Additions	–	2,657	2,657
Impairment charge to income statement	–	(926)	(926)
At 31 December 2007	–	3,701	3,701

	Listed long-term investments £000	Other long-term investments £000	Total £000
Net book value			
At 1 January 2006	6,995	1,805	8,800
Additions	–	165	165
Revaluation through equity	(1,589)	–	(1,589)
Disposals	(3,521)	–	(3,521)
At 31 December 2006	1,885	1,970	3,855

Investments in listed companies

The fair value of listed investments is determined with reference to prices quoted on the London Stock Exchange at 31 December 2007. At present the Group's only listed investment is an 8.1% holding in Superscape Group plc (Superscape), the cost and market value of which as at 31 December 2007 were £2,652,000 and £1,180,000 respectively (2006: £2,652,000 and £1,885,000 respectively). This investment was made in order to broaden the scope of the Group's collaboration with Superscape in the area of 3D technology for wireless devices. Superscape was acquired by Glu Mobile Inc. in 2008 for 10 pence per share, this being the value that the Group permanently impaired its investment to as at 31 December 2007.

At 1 January 2006, the Group owned a less than 1% holding in CSR plc, a company that develops Bluetooth solutions. The cost and market value of this investment as at 1 January 2006 were £688,000 and £3,521,000 respectively. During 2006, the Group divested its holding in CSR plc.

14 Available-for-sale financial assets continued

Other long-term investments

Those unlisted companies in which the Group has invested are early-stage development enterprises, which are generating value for shareholders through research and development activities, and most do not currently report profits. The directors do not consider it possible to estimate with precision the fair value of the Group's investments in these companies (carrying value at 31 December 2007: £3,701,000; 2006: £1,970,000) as they are, by definition, not traded on an organised market and are unique in their activities. However, based on recent fundraising transactions by these companies and, where possible, following review of relevant financial information prepared by the companies, the directors are of the opinion that the fair value of these investments approximates to carrying value. Provisions have been made against other investments to reflect any impairment in value.

Included in other investments are the Group's less than 1% investment in the share capital of Palmchip Corporation (a private fabless chip company based in California); a less than 1% investment in the share capital of Pixim Inc. (also a private fabless chip company based in California); and a 1.4% holding in Reciva Limited, an internet radio company based in the UK. The Group also has an investment in the preference share capital of CoWare Inc., a company which develops system-on-chip software for a wide range of applications, which confers no voting rights. As a result of CoWare Inc.'s recent funding round, this investment was judged to be permanently impaired as at 31 December 2007 – resulting in a charge to the income statement of £926,000.

During 2005 the Group made an investment via convertible loan notes in Luminary Micro Inc. (Luminary), a private fabless semiconductor company based in Austin which develops pioneering ARM architecture-based SoC products. In 2006, the loan notes converted to preference shares and the Group made a further investment of £165,000 via preference shares. The Group's investment in the preference shares of Luminary confers no voting rights.

In 2007, the Group invested £2,534,000 in W&W Communications Inc. (an unlisted US company) by way of a convertible loan note. This note earns interest at 10% per annum, and will convert to a maximum equity holding of 14.99% upon further fundraising by the company. In 2007, the Group also acquired a minority stake in Embest Info & Tech Co. Ltd (Embest) for £123,000. Based in China, Embest is a niche developer of embedded hardware and software.

Available-for-sale financial assets include the following:

	2007 £000	2006 £000
Short-term investments – UK	–	18,372
Listed equity securities – UK	1,180	–
Short-term investments – Korea	232	228
Unlisted short-term marketable securities – US	1,582	19,151
Total current financial assets	2,994	37,751
Listed equity securities – UK	–	1,885
Unlisted equity securities – UK	50	50
Unlisted equity securities – China	123	–
Unlisted equity securities – US	994	1,920
Convertible loan notes – US	2,534	–
Total non-current financial assets	3,701	3,855
Total financial assets	6,695	41,606

Available-for-sale financial assets are denominated in the following currencies:

	2007 £000	2006 £000
Sterling	1,230	20,307
US dollars	5,233	21,071
Korean won	232	228
Total financial assets	6,695	41,606

15 Property, plant and equipment

	Freehold buildings £000	Leasehold improvements £000	Computer equipment £000	Fixtures, fittings and motor vehicles £000	Assets under construction £000	Total £000
Cost						
At 1 January 2007	190	18,054	18,445	4,676	–	41,365
Additions	–	609	2,692	618	742	4,661
Disposals	–	(2,979)	(4,194)	(1,433)	–	(8,606)
Exchange differences	–	153	135	17	16	321
At 31 December 2007	190	15,837	17,078	3,878	758	37,741
Aggregate depreciation						
At 1 January 2007	64	16,266	11,805	2,934	–	31,069
Charge for the year	8	1,032	3,804	648	–	5,492
Disposals	–	(2,761)	(4,161)	(1,371)	–	(8,293)
Exchange differences	–	24	98	15	–	137
At 31 December 2007	72	14,561	11,546	2,226	–	28,405
Net book value						
At 31 December 2007	118	1,276	5,532	1,652	758	9,336

	Freehold buildings £000	Leasehold improvements £000	Computer equipment £000	Fixtures, fittings and motor vehicles £000	Total £000
Cost					
At 1 January 2006	190	20,058	17,950	4,183	42,381
Acquisitions	–	87	80	11	178
Transfers to other intangible assets	–	–	(551)	–	(551)
Additions	–	1,083	5,088	1,018	7,189
Disposals	–	(3,037)	(3,377)	(190)	(6,604)
Exchange differences	–	(137)	(745)	(346)	(1,228)
At 31 December 2006	190	18,054	18,445	4,676	41,365
Aggregate depreciation					
At 1 January 2006	57	17,868	12,993	2,460	33,378
Transfers to other intangible assets	–	–	(385)	–	(385)
Charge for the year	7	1,496	3,034	748	5,285
Disposals	–	(3,009)	(3,369)	(132)	(6,510)
Exchange differences	–	(89)	(468)	(142)	(699)
At 31 December 2006	64	16,266	11,805	2,934	31,069
Net book value					
At 31 December 2006	126	1,788	6,640	1,742	10,296

16 Goodwill

	£000
At 1 January 2006	474,338
Acquisitions (restated at fair value on completion of review carried out during post-acquisition investigative period):	
Falanx	9,400
Soisic	1,530
Exchange differences (restated)	(57,589)
At 31 December 2006 (restated)	427,679
Revision to consideration – KEG	(65)
Revision to consideration – KSI	(37)
Exchange differences	(6,742)
At 31 December 2007	420,835

During the fourth quarter of 2007, the Group tested its balance of goodwill for impairment in accordance with IAS 36, "Impairment of assets". No impairment charge was recorded as a result of this annual impairment test.

Goodwill is allocated to the Group's CGUs according to business segment. The carrying amounts of goodwill by CGU at 31 December 2007 are summarised below:

	Processor Division £000	Physical IP Division £000	Systems Design Division £000	Group £000
Goodwill relating to Artisan	95,805	300,370	–	396,175
Goodwill relating to Falanx	9,400	–	–	9,400
Goodwill relating to Axys	–	–	6,117	6,117
Goodwill relating to KEG and KSI	–	–	5,372	5,372
Goodwill relating to Soisic	–	1,680	–	1,680
Goodwill relating to other acquisitions	2,060	–	31	2,091
	107,265	302,050	11,520	420,835

The recoverable amount for each CGU has been measured based on a value in use calculation.

Processor Division (PD)

The Processor Division encompasses those resources that are centred around microprocessor cores, including specific functions such as graphics IP, fabric IP, embedded software IP and configurable digital signal processing (DSP) IP.

The key assumptions in the value in use calculations were:

Period over which the directors have projected cash flows A ten-year forecast period is used with an assumed terminal growth rate after 2017 of 3% per annum. It is considered appropriate to use a ten-year forecast period to properly reflect the period over which the benefits of the acquisition of Artisan to the Processor Division are expected to accrue. It is expected that it will take between four and seven years from acquisition before a meaningful proportion of ARM's larger semiconductor Partners are licensing physical IP from the Group, with royalties being generated from these licences a further two to four years later, i.e. a total period of six to 11 years.

Forecast revenue growth Revenue is forecast to grow by an amount consistent with the Group's five-year plan as well as analysts' expectations. These have proved to be reliable guides in the past and the directors believe that these estimates are appropriate.

Revenue attributable to the benefits afforded by owning the PIPD unit The directors believe that revenue will accrue to the Processor Division as a result of the ownership of the Physical IP Division for the following reasons:

- The development of faster and more power-efficient microprocessors as a result of collaboration between PD and PIPD engineering teams. This is expected to generate more PD licensing deals at higher prices;
- The potential for PD to win more microprocessor licensing business as a result of ARM being able to offer both processor and physical IP in-house; and
- The improvement in PD operating margins as a result of being able to transfer a number of engineering tasks to the Bangalore design centre acquired with Artisan.

Operating margins Operating margins have been assumed to remain consistent with current operating margins over the period of the calculation.

16 Goodwill continued

Discount rate Future cash flows are discounted in line with ARM's estimated weighted average cost of capital of approximately 10% pre-tax.

The directors are confident that the amount of goodwill allocated to the Processor Division is appropriate and that the assumptions used in estimating its fair value are appropriate. Whilst it is conceivable that a key assumption in the calculation could change, the directors believe that no reasonably foreseeable changes to key assumptions would result in an impairment of goodwill, such is the margin by which the estimated fair value exceeds the carrying value.

Physical IP Division (PIPD)

The Physical IP Division is concerned with the building blocks necessary for translation of a circuit design into actual silicon.

The key assumptions in the value in use calculations were:

Period over which the directors have projected cash flows A ten-year forecast period is used with an assumed terminal growth rate after 2017 of 3% per annum. It is considered appropriate to use a ten-year forecast period to properly reflect the period over which the benefits of the acquisitions of Artisan and Soisic are expected to accrue. It is expected that it will take between four and seven years from acquisition before the majority of ARM's larger semiconductor Partners are licensing physical IP from the Group, with royalties being generated from these licences a further two to four years later, i.e. a total period of six to 11 years.

Forecast revenue growth Revenue is forecast to grow by approximately 17% per annum in the first five years, falling to 8% per annum by 2017 to reflect the uncertainty of forecasting revenues in the years further in the future. In assessing the appropriate valuation of Artisan in 2004, the directors assumed revenue growth of approximately 20% per annum was achievable in the Artisan stand-alone business based on process geometry shrinks bringing more licensing opportunities across a broader range of foundries and based on the significant increase in the usage of Artisan IP in 2003 and 2004 which is yet to generate royalties.

Licence revenues decreased by 13% year-on-year in 2007, with the order backlog at the end of the year being approximately 9% down on the level at the beginning of the year. Royalty revenue was down 7%. During 2007, a significant proportion of engineering resource was deployed to accelerate the technology portfolio rather than working on the conversion of order backlog into short-term revenue. The directors believe that this investment in the technology portfolio will not only bring growth in future years to the Physical IP Division but also contribute significantly to the success of the Processor Division as the synergistic benefits of the combined technologies begin to accrue. Therefore the directors have confidence that the overall forecast growth rate attributable to the Physical IP Division is achievable.

Operating margins Operating margins are assumed to increase gradually over time with growth towards 40% by 2013. In 2007, PIPD's operating margin as a standalone business was estimated at 5%, reflecting both lower licensing revenues and additional R&D investment in order to accelerate the development of leading edge products. This is expected to increase significantly in future years as licence revenues from leading edge products gather pace and royalties increase at effectively 100% margins. Costs are expected to grow broadly in line with licence revenue growth.

This timescale is consistent with ARM's experience in developing the processor licensing and royalty model. ARM has signed approximately 500 processor licences over the last 17 years with less than half of these yielding royalties thus far. As royalty revenues are a function of cumulative licensing, royalty growth gathers momentum as the licensing base grows – ARM processor royalties have increased from \$38 million in 2002 to \$177 million in 2007.

Discount rate Future cash flows are discounted in line with ARM's estimated weighted average cost of capital of approximately 10% pre-tax.

The directors are confident that the amount of goodwill allocated to the Systems Design Division is appropriate and that the assumptions used in estimating its fair value are appropriate. Whilst it is conceivable that a key assumption in the calculation could change, the directors believe that no reasonably foreseeable changes to key assumptions would result in an impairment of goodwill, such is the margin by which the estimated fair value exceeds the carrying value.

Systems Design Division (SDD)

The Systems Design Division is concerned with the tools and models used to create and debug software and system-on-chip (SoC) designs.

The key assumptions in the value in use calculations were:

Period over which the directors have projected cash flows A five-year forecast period is used with an assumed terminal growth rate after 2012 of 3% per annum. It is considered appropriate to use a five-year forecast period to properly reflect the weighted average period over which the benefits of the acquisitions of Axys, KEG and KSI are expected to accrue.

Forecast revenue growth Revenue is forecast to grow by an amount consistent with the Group's five-year plan as well as analysts' expectations. These have proved to be reliable guides in the past and the directors believe that these estimates are appropriate.

Operating margins Operating margins are assumed to grow by an amount consistent with the Group's five-year plan.

16 Goodwill continued

Discount rate Future cash flows are discounted in line with ARM's estimated weighted average cost of capital of approximately 10% pre-tax.

The directors are confident that the amount of goodwill allocated to SDD is appropriate and that the assumptions used in estimating its fair value are appropriate. Whilst it is conceivable that a key assumption in the calculation could change, the directors believe that no reasonably foreseeable changes to key assumptions would result in an impairment of goodwill, such is the margin by which the estimated fair value exceeds the carrying value.

17 Other intangible assets

	Software £000	Patents and licenses £000	In-process research and development £000	Developed technology £000	Existing agreements and customer relationships £000	Core technology £000	Trademarks £000	Order backlog £000	Total £000
Cost									
At 1 January 2007	8,457	14,102	4,768	29,509	42,692	11,802	3,707	1,635	116,672
Additions	783	2,549	–	–	–	–	–	–	3,332
Disposals	(800)	–	–	–	–	–	–	–	(800)
Exchange differences	51	–	(81)	84	(627)	(198)	(63)	(27)	(861)
At 31 December 2007	8,491	16,651	4,687	29,593	42,065	11,604	3,644	1,608	118,343
Aggregate amortisation									
At 1 January 2007	4,783	13,478	1,503	10,481	15,526	4,771	1,582	1,635	53,759
Charge for the year	1,744	476	1,002	6,697	8,344	2,304	848	–	21,415
Disposals	(796)	–	–	–	–	–	–	–	(796)
Exchange differences	54	–	(21)	(43)	(180)	(62)	(20)	(27)	(299)
At 31 December 2007	5,785	13,954	2,484	17,135	23,690	7,013	2,410	1,608	74,079
Net book value									
At 31 December 2007	2,706	2,697	2,203	12,458	18,375	4,591	1,234	–	44,264

	Software £000	Patents and licenses £000	In-process research and development £000	Developed technology £000	Existing agreements and customer relationships £000	Core technology £000	Trademarks £000	Order backlog £000	Total £000
Cost									
At 1 January 2006	36,530	14,102	4,365	23,477	46,941	13,455	4,225	1,864	144,959
Acquisitions (Falanx)	2	–	–	4,267	990	–	–	–	5,259
Acquisitions (Soisic)	–	–	–	4,283	–	–	–	–	4,283
Acquisitions (PowerEscape)	–	–	992	–	–	–	–	–	992
Additions	1,370	–	–	–	–	–	–	–	1,370
Transfers from PPE	551	–	–	–	–	–	–	–	551
Disposals	(29,774)	–	–	–	–	–	–	–	(29,774)
Exchange differences	(222)	–	(589)	(2,518)	(5,239)	(1,653)	(518)	(229)	(10,968)
At 31 December 2006	8,457	14,102	4,768	29,509	42,692	11,802	3,707	1,635	116,672
Aggregate amortisation									
At 1 January 2006	32,717	12,984	694	5,420	7,976	2,749	812	1,864	65,216
Charge for the year	1,610	494	947	6,009	8,940	2,515	926	–	21,441
Transfers from PPE	385	–	–	–	–	–	–	–	385
Disposals	(29,774)	–	–	–	–	–	–	–	(29,774)
Exchange differences	(155)	–	(138)	(948)	(1,390)	(493)	(156)	(229)	(3,509)
At 31 December 2006	4,783	13,478	1,503	10,481	15,526	4,771	1,582	1,635	53,759
Net book value									
At 31 December 2006	3,674	624	3,265	19,028	27,166	7,031	2,125	–	62,913

17 Other intangible assets continued

Refer to note 22 for the methods and significant assumptions applied in estimating the fair value of other intangible assets acquired as part of business combinations. Included within the net book value of other intangible assets at 31 December 2007 are significant amounts relating to intangibles that were acquired with Artisan in 2004. £4,066,000 (2006: £8,363,000) relates to the carrying value of developed technology, £16,083,000 (2006: £21,850,000) relates to the carrying value of existing royalty agreements and £4,591,000 (2006: £7,030,000) relates to the carrying value of core technology. At 31 December 2007, these items have remaining useful economic lives of one, three and two years respectively.

18 Accrued and other liabilities

	2007 £000	2006 Restated £000
Accruals	18,941	29,648
Other taxation and social security	3,028	1,446
Other payables	6,205	8,492
	28,174	39,586

19 Financial instruments

(a) Financial instruments by category

The accounting policies for financial instruments have been applied to the line items below:

Financial assets

	Loans and receivables £000	Assets at fair value through the income statement £000	Available- for-sale £000	Total £000
At 31 December 2007				
Cash and cash equivalents	49,509	–	–	49,509
Short-term investments	–	232	–	232
Short-term marketable securities	–	1,582	–	1,582
Trade receivables (gross of impairment provision)	45,249	–	–	45,249
Available-for-sale investments – listed	–	–	1,180	1,180
Total current financial assets	94,758	1,814	1,180	97,752
Non-current available-for-sale investments – unlisted	–	–	3,701	3,701
Total financial assets	94,758	1,814	4,881	101,453
At 31 December 2006				
Cash and cash equivalents	90,743	–	–	90,743
Short-term investments	–	18,600	–	18,600
Short-term marketable securities	–	19,151	–	19,151
Fair value of currency exchange contracts	–	439	–	439
Trade receivables (gross of impairment provision)	48,276	–	–	48,276
Total current financial assets	139,019	38,190	–	177,209
Available-for-sale investments – unlisted	–	–	1,970	1,970
Available-for-sale investments – listed	–	–	1,885	1,885
Total non-current financial assets	–	–	3,855	3,855
Total financial assets	139,019	38,190	3,855	181,064

19 Financial instruments continued
Financial liabilities

	2007 £000	2006 £000
Liabilities at fair value through the income statement at 31 December:		
Trade and other payables, excluding embedded derivatives	2,230	1,826
Forward currency arrangements	496	–
Embedded derivatives (included in accrued and other liabilities)	220	1,620
Total financial liabilities	2,946	3,446

(b) Credit quality of financial assets

Trade receivables

On a quarterly basis, all trade receivables more than three months overdue are considered for impairment on a line-by-line basis. Either a provision is made or the lack thereof is justified, with review by senior members of the Group's finance team.

	2007 £000	2006 £000
Trade receivables (gross of impairment provision):		
Under 90 days	42,154	41,784
Fully provided for	1,504	2,556
Over 90 days but not provided for	1,591	3,936
Total	45,249	48,276

As shown above, at 31 December 2007 and 31 December 2006 trade receivables more than three months overdue but not provided for amounted to £1.6 million and £3.9 million respectively. Of these amounts, £0.7 million (2006: £1.5 million) of cash had been collected by 14 March 2008 (15 March 2007); £0.4 million (2006: £1.9 million) was owed by very large customers; and £0.1 million (2006: £0.2 million) was owed by customers with less than £50,000 overdue in total. For the remainder, repayment schedules have been agreed with the customers concerned. These will be monitored on a quarterly basis per the control outlined above. No further analysis has been provided here on the quality of these debts as they are not felt to pose a material threat to the Group's future results.

Highly liquid financial assets

As at 31 December 2007, 91% (2006: 95%) of the Group's cash and cash equivalents; short-term bank deposits; and short-term marketable securities were held with institutions that had either an AA rating or, in the case of UK building societies, had over £1 billion in assets.

Derivative financial assets

As at 31 December 2006, all derivative financial assets were based on contracts held with AA-rated institutions. At 31 December 2007, the Group had no such assets.

20 Called-up share capital

	2007 £000	2006 £000		
Authorised				
2,200,000,000 ordinary shares of 0.05 pence each (2006: 2,200,000,000)	1,100	1,100		
	2007	2006		
	Number of shares (000)	Value £000	Number of shares (000)	Value £000
Issued and fully paid				
At 1 January	1,389,908	695	1,386,103	693
Shares cancelled	(55,719)	(28)	—	—
Allotted under employee incentive schemes	9,867	5	3,805	2
At 31 December	1,344,056	672	1,389,908	695

During 2007, the aggregate consideration received on issue of new share capital allotted under employee incentive schemes was £5.5 million (2006: £2.1 million).

21 Own shares held

	Own share held for future cancellation £000	Treasury stock £000	ESOP £000	Total £000
At 1 January 2007	57,897	–	348	58,245
Purchase of own shares	–	120,419	–	120,419
Appropriation for future share cancellations	8,142	–	–	8,142
Cancellation of shares	(66,039)	–	–	(66,039)
Issuance of shares	–	(30,767)	–	(30,767)
At 31 December 2007	–	89,652	348	90,000
At 1 January 2006	–	14,877	1,438	16,315
Purchase of own shares	–	18,622	–	18,622
Appropriation for future share cancellations	57,897	–	–	57,897
Issuance of shares	–	(33,499)	(1,090)	(34,589)
At 31 December 2006	57,897	–	348	58,245

During the year £128,561,000 (2006:£76,519,000) of shares were repurchased, representing 94.5 million (2006: 63.6 million) shares. Share repurchase transactions in respect of 55,719,000 shares carried out between 19 May 2006 and 21 February 2007 took place at a time when ARM Holdings plc (Company only) had no distributable reserves and accordingly such shares have not been properly acquired in accordance with the Companies Act 1985, and are not available for re-issue or cancellation. ARM Holdings plc made an application to the Court during 2007 to cancel these shares pursuant to a special resolution passed at the 2007 AGM.

At 31 December 2007, a total of 65.2 million shares (2006: no shares) were held as Treasury stock; no shares (2006: 49.5 million shares) were held for cancellation; and 1.2 million shares (2006: 1.2 million shares) were held within the ESOP. At 31 December 2007, own shares held have a nominal value of 0.05 pence (2006: 0.05 pence) and in total represent 4.9% (2006: 3.6%) of called-up share capital.

22 Acquisitions

There were no acquisitions during 2007.

Falanx Microsystems AS

On 30 May 2006, the Group purchased the entire share capital of Falanx Microsystems AS (Falanx), a graphics IP company incorporated in Norway for total consideration of £13.4 million, comprising £13.3 million cash consideration and £0.1 million of related acquisition expenses. This purchase has been accounted for as an acquisition.

Falanx develops graphics accelerator IP and software for semiconductor system-on-chip (SoC) vendors that deliver high-quality multimedia images without compromising performance, power consumption or system cost. The acquisition fits the ARM strategy of enabling users to create SoCs seamlessly in their design process. The Mali Graphics Processor Unit (GPU) is a combination of hardware and software that enables industry-leading 3D graphics and video on mobile phones, portable media players, set-top boxes, handheld gaming devices and automotive systems, providing the Group with full control over the development of its future 3D graphics solutions. For the reasons given above, combined with the ability to hire the entire workforce of Falanx and synergistic benefits that may arise, the Group paid a premium on the Falanx acquisition, giving rise to goodwill.

All intangible assets were recognised at their respective fair values. The residual excess over the net assets acquired is recognised as goodwill in the financial statements.

At 31 December 2006, the accounting for the Falanx acquisition was determined on a provisional basis because the fair values assigned to the acquiree's identifiable assets and liabilities were only provisional. At 31 December 2007, final adjustments to these provisional values were recognised as a result of completing work on the fair values of assets and liabilities acquired. These adjustments were recognised as if they had occurred at the date of acquisition.

22 Acquisitions continued

	Carrying value pre-acquisition £000	Final fair value* £000
Cash and cash equivalents	24	24
Receivables	219	197
Property, plant and equipment	60	60
Other intangible assets	2	5,259
Payables	(319)	(314)
Tax	(287)	(287)
– Deferred tax asset	543	543
– Deferred tax liability	–	(1,472)
Net assets acquired	242	4,010
Goodwill		9,400
Consideration		13,410

* During 2007, the provisional fair values of Falanx's accounts receivable and other creditors were finalised resulting in a reduction in net assets acquired of £17,000. As a result, goodwill increased by £17,000 during the year.

Consideration satisfied by:

	£000
Cash consideration paid	13,280
Expenses	130
	13,410

The outflow of cash and cash equivalents on the acquisition of Falanx is calculated as follows:

	£000
Cash consideration paid	13,280
Expenses paid	130
Cash acquired	(24)
Net cash outflow	13,386

The intangible assets acquired as part of the acquisition of Falanx can be analysed as follows:

	£000
Computer software	2
Developed technology	4,267
Customer relationships	990
Total	5,259

The methods and significant assumptions involved in valuing these identifiable intangible assets are described below:

Developed technology Developed technology of £4.3 million comprises internally-developed software and hardware technologies. Falanx employs a number of unique pieces of software that have been internally developed, allowing them to be highly bespoke and continually adapted. Internally developed hardware technologies comprise the Mali family of graphics processors which are controlled by Falanx through numerous patents. At the date of acquisition, both internally-developed software and hardware technologies were complete and had reached technological feasibility. Any costs incurred in the future will relate to ongoing maintenance of the technologies and will be expensed as incurred. To estimate the fair value of the internally-developed software the replacement cost approach was used with a post-tax discount rate of 14.9%. To estimate the fair value of the internally-developed hardware, a discounted cash flow method, specifically the income approach, was used with a post-tax discount rate of 15.4%. Developed technologies are being amortised over an estimated useful life of three to five years.

Customer relationships The customer base of £1.0 million represented the fair value of existing customer contracts. To estimate their fair value, a discounted cash flow method, specifically the income approach, was used with reference to the terms of the contracts and management's estimates of the level of revenue which will be generated from the customer relationships. A post-tax discount rate of 14.9% was used for the valuation. Customer relationships are being amortised over an estimated useful life of three years.

22 Acquisitions continued

Soisic SA acquisition

On 30 October 2006, the Group purchased the entire share capital of Soisic SA (Soisic), a silicon-on-insulator (SOI) IP company incorporated in France for total consideration of £5.8 million, comprising £3.1 million cash consideration, £2.4 million contingent consideration and £0.3 million of related acquisition expenses. This purchase has been accounted for as an acquisition.

With this acquisition, the Group is making an investment in new technologies related to physical IP to enhance its leadership position in providing customers access to the higher performance and lower power offered by SOI process technologies. Soisic develops a similar set of products to the Physical IP Division, specifically standard cells, static random access memory (SRAM) compilers and input/output (I/O) cells, however, based on SOI design rules and process models. Integrating this capability with ARM's widely-used physical IP opens the possibility for SoC designers to access SOI technology, which currently is used only in full custom designs, such as high-performance microprocessors.

The Group is investing in this area to be at the forefront of the design technologies needed to exploit the potential advantages of SOI as its usage grows in mobile, home and enterprise SoC and ASIC applications. For the reasons given above, combined with the ability to hire the entire workforce of Soisic and synergistic benefits that may arise, the Group paid a premium on the Soisic acquisition, giving rise to goodwill.

All intangible assets were recognised at their respective fair values. The residual excess over the net assets acquired is recognised as goodwill in the financial statements.

At 31 December 2006, the accounting for the Soisic acquisition was determined on a provisional basis because the fair values assigned to the acquiree's identifiable assets and liabilities were only provisional. At 31 December 2007, a final adjustment was made to these provisional values as a result of completing work on the fair values of assets and liabilities acquired. This adjustment related to pre-acquisition losses from which the Group expects to derive future tax benefits and was recognised as if it had occurred at the date of acquisition.

	Carrying value pre-acquisition £000	Final fair value* £000
Receivables	273	273
Property, plant and equipment	117	117
Other intangible assets	–	4,283
Payables	(1,415)	(1,415)
Tax		
– Current tax asset	303	303
– Deferred tax asset	–	2,075
– Deferred tax liability	–	(1,413)
Net (liabilities) assumed/assets acquired	(722)	4,223
Goodwill		1,530
Consideration		5,753

* During 2007, the provisional fair values in respect of deferred tax were finalised resulting in an increase in net assets of £683,000 and a corresponding reduction in goodwill.

Consideration satisfied by:

	£000
Cash consideration paid (including net debt of £22,000)	1,843
Retentions*	1,268
Contingent cash consideration**	2,342
Expenses	300
	5,753

* Retentions represent consideration held back to cover possible future liabilities.

** The contingent consideration will be determined based on Soisic's future revenue in the first 1.5 years post-acquisition.

The outflow of cash and cash equivalents on the acquisition of Soisic is calculated as follows:

	£000
Cash consideration paid (excluding net debt of £22,000)	1,821
Expenses paid	300
Bank overdraft acquired	53
Net cash outflow	2,174

22 Acquisitions continued

The intangible assets acquired as part of the acquisition of Soisic can be analysed as follows:

	£000
Developed technology	4,283
Total	4,283

The methods and significant assumptions involved in valuing these identifiable intangible assets are described below:

Developed technology Developed technology of £4.3 million represents primarily SOI wafers from 16nm up to 65nm. At the date of acquisition the technology was complete and had reached technological feasibility. Any costs incurred in the future will relate to the ongoing maintenance of the technology and will be expensed as incurred. To estimate the fair value of the technology, a discounted cash flow method, specifically the excess profit method, was used with a post-tax discount rate of 30%. Developed technology is being amortised over an estimated useful life of five years.

PowerEscape Inc.

On 21 June 2006, the Group purchased certain assets of PowerEscape Inc., a private company incorporated in the US, for total consideration of £0.6 million, comprising £0.5 million cash consideration and £0.1 million of related acquisition expenses.

The PowerEscape team, which has been integrated into the Group's Systems Design Division, will focus on adding innovative profiling and analysis features to the Group's portfolio of market-leading development tools.

All intangible assets were recognised at their respective fair values. No goodwill has been recognised on this acquisition.

At 31 December 2006, the accounting for the PowerEscape acquisition was determined on a provisional basis because the fair values assigned to the acquiree's identifiable assets and liabilities were only provisional. At 31 December 2007, no adjustments to these provisional values were recognised as a result of completing work on the fair values of assets and liabilities acquired and so these provisional values became the final fair values for the assets and liabilities acquired.

	Carrying value pre-acquisition £000	Final fair value £000
Property, plant and equipment	1	1
Other intangible assets	–	992
Tax		
– Deferred tax liability	–	(397)
Net assets acquired	1	596
Goodwill		–
Consideration		596

Consideration satisfied by:

	£000
Cash consideration paid	540
Expenses	56
	596

The outflow of cash and cash equivalents on the acquisition of PowerEscape is calculated as follows:

	£000
Cash consideration paid	540
Expenses paid	56
Net cash outflow	596

The intangible assets acquired as part of the acquisition of PowerEscape can be analysed as follows:

	£000
In-process research and development	992
Total	992

The methods and significant assumptions involved in valuing these identifiable intangible assets are described below:

22 Acquisitions continued

In-process research and development In-process research and development of £1.0 million reflects certain research projects that had not yet reached technological feasibility and commercial viability. The fair value assigned to in-process research and development was estimated using the discounted cash flow method with a post-tax discount rate of approximately 20%.

As part of the purchase agreement, the results of PowerEscape for the year ended 31 December 2005 and for the period from 1 January 2006 until acquisition are not disclosable in this annual report. The results of the Group would not have been significantly different had the acquisition of PowerEscape occurred on 1 January 2006.

23 Share-based payments

The Group has several share option schemes in current operation, whereby options over shares in the Company can be granted to employees and directors. The different schemes are described below, but all options are granted with a fixed exercise price equal to the market price of the shares under option at the date of grant, except for those options within the SAYE and ESPP schemes as detailed below. Furthermore, from 2006, the Company has issued Restricted Stock Units (RSUs) to employees instead of options which are actual share awards on vesting rather than options to buy shares at a fixed exercise price. Whilst the Company reserves the right to award options to employees going forward, the majority of awards to employees will be in RSUs.

Under the UK Inland Revenue Executive Approved Share Option Plan (the "Executive Scheme"), the Company may grant options to employees meeting certain eligibility requirements. Options under the Executive Scheme are exercisable between three and ten years after their issue, after which time the options expire.

Under the Company's Unapproved Scheme (the "Unapproved Scheme"), for which it has not sought approval from the UK tax authorities, options are exercisable one to seven years after their issue, after which time the options expire. The Company also operates the US ISO Scheme, which is substantially the same as the Unapproved Scheme, the main difference being that the options are exercisable one to five years after their issue. Under both of these schemes options are exercisable as follows: 25% maximum on first anniversary, 50% maximum on second anniversary, 75% maximum on third anniversary, 100% maximum on fourth anniversary. Various options to directors under the Unapproved Scheme have certain performance criteria attached, which if met are exercisable after three years, otherwise they will become exercisable after seven years.

There are further schemes for our French and Belgian employees (the "French Scheme" and the "Belgian Scheme"). In the French Scheme, options are exercisable between four and seven years after their issue, whilst in the Belgian Scheme, options are exercisable from 1 January following the third anniversary after their issue, up to seven years from issue.

Upon the acquisition of Artisan in 2004, the Company assumed the share schemes of Artisan existing at acquisition. The schemes remained substantially the same as prior to the acquisition, other than the options became options to purchase shares in ARM Holdings plc instead of Artisan Components Inc. The number and value of options were amended in line with the conversion ratio as detailed in the merger agreement. The schemes assumed were the "1993 Plan", the "1997 Plan", the "2000 Plan", the "2003 Plan", the "Director Plan", the "Executive Plan" and the "ND00 Plan".

Under each plan, there are multiple vesting templates and vesting periods. The majority of the options were already vested upon acquisition, and the most common template was 25% vesting after one year, and then 6.25% vesting each quarter thereafter, until 100% vest after four years. Some options vest on a monthly basis, and some vest over five years. All options lapse ten years from the date of grant.

The Company also offers savings-related share option schemes (SAYE) for all employees and executive directors of the Group. The number of options granted is related to the value of savings made by the employee. The period of savings is three or five years except for employees of ARM Inc. where the period is two years. The option price for grants made in 2007 was set at 80% of the market share price prior to the grant, but in previous years was set at 85%, and the right to exercise normally only arises for a six-month period once the savings have been completed except for ARM Inc. where the right to exercise normally only arises for a three-month period once the savings have been completed. In 2007, the Company commenced a new savings-related option scheme for US employees, namely the Employee Share Purchase Plan (ESPP). The number of options granted is related to the value of savings made by the employee. The period of savings is six months, with the option price being at 85% of the lower of the market share price at the beginning and end of the scheme.

The main RSU awards (to employees in all jurisdictions other than France) vest similarly to the unapproved scheme above, namely 25% on each anniversary over four years. RSU awards to our French employees vest 50% after two years, and then a further 25% after three and four years.

Additionally, the Company operates a Deferred Annual Bonus plan (DAB). Under the DAB, which is for directors and selected senior management within the Group, participants are required to defer 50% of any related annual bonus into shares on a compulsory basis. These shares will be deferred for three years, and then a further matching award will be made depending on the achievement of an EPS performance condition over that time. The Company also operates the Long Term Incentive Plan (LTIP), also for directors and selected senior management, whereby share awards are made and vest depending on the Company's TSR performance compared to two comparator groups over the three-year performance period.

23 Share-based payments continued

As disclosed in note 5, staff expenses arising from these share-based compensation schemes of £16.8 million (2006: £17.4 million) were charged to the income statement in the year. This is in line with the Group's policies for recognition and measurement of the costs associated with these remuneration schemes as outlined in note 1.

The fair value of options granted was estimated on the date of grant using the Black-Scholes option pricing model. The following assumptions for each option grant during 2006 and 2007 were as follows:

Grant date	22 Jun 2007	1 Feb 2006	1 Feb 2006	1 Feb 2006	1 Feb 2006
Scheme	SAYE	Performance	Unapproved	ISO	French
Share price at grant date	£1.38	£1.325	£1.325	£1.325	£1.325
Exercise price	£1.104	£1.325	£1.325	£1.325	£1.325
Number of employees	208	6	44	29	1
Shares under option	1,065,813	2,445,284	2,313,098	1,068,269	85,000
Vesting period (years)	3–5	3	1–4	1–4	4
Expected volatility	32%–43%	40%	40%	40%	40%
Expected life (years)	3–5	4	2–5	1–4	5
Risk free rate	5.5%	4.0%	4.0%	4.0%	4.0%
Dividend yield	1.45%	0.7%	0.7%	0.7%	0.7%
Fair value per option	£0.48–£0.65	£0.46	£0.33–£0.51	£0.23–£0.46	£0.51
Grant date	1 Feb 2006	4 May 2006	4 May 2006	4 May 2006	1 Feb 2006
Scheme	Belgian	Unapproved	ISO	French	Belgian
Share price at grant date	£1.325	£1.36	£1.36	£1.36	£1.325
Exercise price	£1.325	£1.36	£1.36	£1.36	£1.325
Number of employees	2	47	28	3	2
Shares under option	22,500	350,333	294,500	13,250	22,500
Vesting period (years)	3.9	1–4	1–4	4	3.9
Expected volatility	40%	40%	40%	40%	40%
Expected life (years)	4	2–5	1–4	5	4
Risk free rate	4.0%	4.0%	4.0%	4.0%	4.0%
Dividend yield	0.7%	0.7%	0.7%	0.7%	0.7%
Fair value per option	£0.46	£0.33–£0.53	£0.23–£0.47	£0.53	£0.46
Grant date	20 Jun 2006	1 Sep 2006	1 Sep 2006	1 Sep 2006	20 Nov 2006
Scheme	SAYE	Unapproved	ISO	Belgian	Unapproved
Share price at grant date	£1.2075	£1.1875	£1.1875	£1.1875	£1.16
Exercise price	£1.2064	£1.1875	£1.1875	£1.1875	£1.16
Number of employees	298	16	8	2	8
Shares under option	2,249,806	119,750	77,500	5,000	20,000
Vesting period (years)	2–5	1–4	1–4	3.3	1–4
Expected volatility	40%	40%	40%	40%	40%
Expected life (years)	2–5	2–5	1–4	4	2–5
Risk free rate	4.0%	4.5%	4.5%	4.5%	5.0%
Dividend yield	0.7%	0.7%	0.7%	0.7%	0.7%
Fair value per option	£0.38–£0.53	£0.30–£0.47	£0.21–£0.42	£0.42	£0.29–£0.47

23 Share-based payments continued

The fair value of RSUs, LTIP and DAB awards granted was estimated on the date of grant using the Black-Scholes option pricing model. As all are share awards with no exercise price, all awards have been deemed to have an exercise price of £0.0000001 in the Black-Scholes model. The following assumptions for each grant during 2006 and 2007 were as follows:

Grant date	8 Feb 2007	8 Feb 2007	8 Feb 2007	8 Feb 2007	4 Jun 2007
Scheme	DAB	RSU	French RSU	LTIP	RSU
Share price at grant date	£1.28	£1.28	£1.28	£1.28	£1.425
Number of employees	28	1,461	37	31	95
Shares awarded	901,183	7,955,505	192,924	2,770,967	366,170
Vesting period (years)	–	1–4	2–4	3	1–4
Expected volatility	33%	29%–38%	29%–38%	33%	29%–36%
Expected life (years)	3	1–4	2–4	3	1–4
Risk free rate	5.25%	5.25%	5.25%	5.25%	5.5%
Dividend yield	0.7%	0.7%	0.7%	0.7%	1.4%
Fair value per option	£1.25	£1.245–£1.271	£1.245–£1.262	£1.253	£1.347–£1.405
Grant date	4 Jun 2007	13 Aug 2007	13 Aug 2007	12 Nov 2007	12 Nov 2007
Scheme	French RSU	RSU	French RSU	RSU	French RSU
Share price at grant date	£1.425	£1.5152	£1.5152	£1.34	£1.34
Number of employees	11	54	2	97	8
Shares awarded	37,294	194,642	13,477	284,356	25,947
Vesting period (years)	2–4	1–4	2–4	1–4	2–4
Expected volatility	29%–36%	28%–34%	30%–34%	29%–33%	29%–33%
Expected life (years)	2–4	1–4	2–4	1–4	2–4
Risk free rate	5.5%	5.75%	5.75%	5.75%	5.75%
Dividend yield	1.4%	1.32%	1.32%	1.49%	1.49%
Fair value per option	£1.347–£1.386	£1.437–£1.495	£1.437–£1.476	£1.262–£1.32	£1.262–£1.301
Grant date	8 May 2006	8 May 2006	8 May 2006	1 Sep 2006	1 Sep 2006
Scheme	RSU	French RSU	LTIP	RSU	French RSU
Share price at grant date	£1.365	£1.365	£1.365	£1.1875	£1.1875
Number of employees	1,167	28	28	108	2
Shares awarded	6,282,180	164,292	2,436,871	623,402	2,852
Vesting period (years)	1–4	2–4	2.75	1–4	2–4
Expected volatility	40%	40%	40%	40%	40%
Expected life (years)	1–4	2–4	2.75	1–4	2–4
Risk free rate	4.0%	4.0%	4.0%	4.5%	4.5%
Dividend yield	0.7%	0.7%	0.7%	0.7%	0.7%
Fair value per option	£1.327–£1.355	£1.327–£1.346	£1.339	£1.155–£1.179	£1.155–£1.171
Grant date	20 Nov 2006	20 Nov 2006			
Scheme	RSU	French RSU			
Share price at grant date	£1.16	£1.16			
Number of employees	152	18			
Shares awarded	890,676	189,445			
Vesting period (years)	1–4	2–4			
Expected volatility	40%	40%			
Expected life (years)	1–4	2–4			
Risk free rate	5.0%	5.0%			
Dividend yield	0.7%	0.7%			
Fair value per option	£1.128–£1.152	£1.128–£1.144			

The expected volatility was primarily based upon historical volatility adjusted for past one-time events that are not expected to re-occur. The expected life is the expected period to exercise.

A reconciliation of option and share award movements over the year to 31 December 2007 is shown below. Share awards do not have an exercise price and therefore the reconciliation below shows only the number of awards, with no corresponding weighted average exercise prices.

23 Share-based payments continued

	2007			2006		
	Options Number	Weighted average exercise price	RSUs/ LTIP/DAB Number	Options Number	Weighted average exercise price	RSUs/ LTIP/DAB Number
Outstanding at 1 January	111,923,736	£1.093	15,665,056	143,023,990	£1.014	7,760,881
Granted	1,065,813	£1.104	12,742,465	9,064,290	£1.250	10,589,718
Additional vesting	–	–	–	–	–	1,672,009
Forfeited	(3,480,686)	£1.230	(3,604,445)	(8,491,783)	£1.499	(558,985)
Lapsed	(3,429,172)	£4.848	–	(1,016,500)	£3.350	–
Exercised	(30,850,202)	£0.612	(2,119,532)	(30,656,261)	£0.583	(3,798,567)
Outstanding at 31 December	75,229,489	£1.113	22,683,544	111,923,736	£1.093	15,665,056
Exercisable at 31 December	55,652,780	£1.120	–	74,533,736	£1.118	–

The following options over ordinary shares were in existence at 31 December:

2007					
Exercise price (£)	Number outstanding	Weighted average exercise price (£)	Weighted average remaining life Expected	Weighted average remaining life Contractual	
Outstanding options:					
0.1125 – 0.45	14,608,232	0.32	2.10	3.11	
0.46 – 0.9475	14,142,469	0.63	4.22	5.48	
1.005 – 1.055	18,110,574	1.05	1.86	3.56	
1.0575 – 1.25	13,713,481	1.23	1.72	2.95	
1.325 – 7.738	14,654,733	2.34	1.99	2.78	
Total	75,229,489	1.11	2.35	3.57	
Outstanding RSU/LTIP/DAB awards:					
0.00 (RSUs)	13,845,565	–	1.58	1.58	
0.00 (LTIP)	7,943,979	–	1.10	1.10	
0.00 (DAB)	894,000	–	2.13	2.13	
Total	22,683,544	–	1.43	1.43	
2006					
Exercise price (£)	Number outstanding	Weighted average exercise price (£)	Weighted average remaining life Expected	Weighted average remaining life Contractual	
Outstanding options:					
0.026 – 0.40	15,662,942	0.25	0.97	4.24	
0.405 – 0.50	21,310,841	0.45	1.32	4.13	
0.51 – 0.9475	17,465,042	0.71	1.10	5.96	
1.005 – 1.224	25,943,761	1.07	2.84	4.37	
1.25 – 7.738	31,541,150	2.18	2.45	3.52	
Total	111,923,736	1.09	1.91	4.31	
Outstanding RSU/LTIP awards:					
0.00 (RSUs)	7,893,640	–	1.96	1.96	
0.00 (LTIP)	7,771,416	–	1.05	1.05	
Total	15,665,056	–	1.51	1.51	

24 Capital and other financial commitments

	2007 £000	2006 £000
Contracts placed for future capital expenditure not provided in the financial statements	276	525

25 Operating lease commitments – minimum lease payments

At 31 December 2007, the Group had commitments under non-cancellable operating leases as follows:

	2007			2006		
	Land and buildings £000	Other £000	Total £000	Land and buildings £000	Other £000	Total £000
Commitments under non-cancellable operating leases expiring:						
Within one year	1,465	18	1,483	5,209	11,564	16,773
Later than one year and less than five years	5,041	50,076	55,117	12,253	14,520	26,773
After five years	17,130	292	17,422	9,107	15	9,122
At 31 December	23,636	50,386	74,022	26,569	26,099	52,668

26 Financial contingencies

Legal claims

Nazomi In May 2002, Nazomi Communications, Inc. (Nazomi) filed suit against ARM alleging willful infringement of US Patent No. 6,332,215. ARM answered the complaint in July 2002 denying infringement. Following an original ruling in ARM's favour, Nazomi appealed and received a supplementary "Markman" hearing in 2005 that resulted in a decision that supported the original ruling. On 13 February 2007, Nazomi again appealed and, on 21 February 2008 the Court of Appeals for the Federal Circuit upheld the District Court's claim construction and affirmed the District Court's grant of summary judgment in favour of ARM. The period for any further appeal by Nazomi has now passed and accordingly this litigation is now concluded with judgment in favour of ARM.

Technology Properties Limited In October 2005, Technology Properties Limited, Inc. (TPL) filed suit, in the United States District Court for the Eastern District of Texas (Marshall Division), against certain companies in the Fujitsu, Matsushita NEC and Toshiba groups of companies alleging infringement of TPL's US Patents No.'s. 5,809,336; 5,784,584 and 6,598,148 (the "Litigation"). All of the defendants are licensees of various ARM technologies. It was revealed as part of the preliminary infringement contentions in the Litigation, filed in July 2006, that certain ARM technology is alleged to infringe a single claim in US Patent No 5,784,584 (the "'584 Patent"). In September 2006, ARM filed a motion to intervene in the Litigation and that motion has been granted. ARM is now a defendant party in the Litigation. The claim construction (or "Markman") hearing took place in May 2007. Based on the claim construction delivered by the District Court, TPL filed a motion stipulating that the accused ARM technology does not infringe the '584 Patent with a request that final judgment be entered to that effect. TPL subsequently filed notice to appeal the claim construction to the Court of Appeals for the Federal Circuit. Based on independent legal advice, ARM is confident that the Court of Appeals will uphold the claim construction ruling delivered by the District Court.

Based on independent legal advice, ARM does not expect any significant liability to arise in respect of these proceedings, except in relation to legal costs, for which £0.2 million has been accrued at 31 December 2007 (2006: £1.0 million).

Guarantees It is common industry practice for licensors of technology to offer to indemnify their licensees for loss suffered by the licensee in the event that the technology licensed is held to infringe the intellectual property of a third party. Consistent with such practice, the Group provides such indemnification to its licensees but subject, in all cases, to a limitation of liability. The obligation for the Group to indemnify its licensees is subject to certain provisos and is usually contingent upon a third party bringing an action against the licensee alleging that the technology licensed by the Group to the licensee infringes such third party's intellectual property rights. The indemnification obligations typically survive any termination of the licence and will continue in perpetuity.

The Group does not provide for any such guarantees unless it has received notification from the other party that they are likely to invoke the guarantee. The provision is made if both of the following conditions are met: (i) information available prior to the issuance of the financial statements indicates that it is probable that a liability had been incurred at the date of the financial statements; and (ii) the amount of the liability can be reasonably estimated. Any such provision is based upon the directors' estimate of the expected costs of any such claim.

Contingent consideration Acquisition-related contingent consideration is disclosed in note 22.

27 Related party transactions

During the year, the Group paid royalty fees of £81,000 (2006: £124,000) and made cross-licence payments of £nil (2006: £nil) to Superscape Group plc (Superscape), a company in which Mike Inglis, an executive director of the Group, was a non-executive director during the year. Amounts owed to Superscape at 31 December 2007 and 2006 were £nil. In addition, in 2007 the Group received royalty fees of £14,000 (2006: £19,000) and licence fees of £nil (2006: £nil) from Superscape. At 31 December 2007, £nil (2006: £17,000) was owed by Superscape.

Also in 2007, the Group received licence fees of £4,000 (2006: £3,085,000), support and maintenance income of £32,000 (2006: £37,000) and evaluation tools fees of £123,000 (2006: £82,000) from CSR plc, a company in which John Scarisbrick, a non-executive of the Group, was an executive director during the year. Amounts owed by CSR plc at 31 December 2007 were £31,000 (2006: £14,000).

During 2007, the Group received funding for SOI technology development of £1,507,000 (2006: £319,000) from SOI TEC Silicon On Insulator Technologies SA (Soitec). Furthermore, the Group paid £181,000 to Soitec during the year in relation to license income from the two parties' ongoing collaborative agreement to develop SOI technology. Soitec is an SOI IP company in which Doug Dunn, Group Chairman, is a non-executive director. At 31 December 2007, £nil (2006: £383,000) is owed by Soitec. Amounts owed to Soitec at 31 December 2007 and 2006 were £nil.

There were no other related party transactions during 2007 or 2006 which require disclosure.

Key management compensation is disclosed in note 4.

28 Post-balance sheet events

After the year-end, the directors declared payment of a final dividend in respect of 2007 of 1.2 pence per share. Subject to shareholder approval, the final dividend will be paid on 21 May 2008 to shareholders on the register on 2 May 2008. The final dividend has not been recognised as a distribution during the year ended 31 December 2007.

29 Principal subsidiaries and associates

Details of principal subsidiary undertakings are shown below. Not all subsidiaries are included as the list would be excessive in length.

Name of undertaking	Country of registration	Principal activity	Proportion of total nominal value of issued shares held
ARM Limited	England and Wales	Marketing, research and development of RISC-based microprocessors	100*
ARM Inc.	US	Marketing and development of RISC-based microprocessors; and marketing, research and development of physical IP components	100
ARM KK	Japan	Marketing of RISC-based microprocessors	100
ARM Korea Limited	South Korea	Marketing of RISC-based microprocessors	100
ARM France SAS	France	Development of RISC-based microprocessors and of silicon-on-insulator IP	100
ARM Belgium NV	Belgium	Development of data engine microprocessors	100
ARM Norway AS	Norway	Marketing, research and development of graphics IP	100
ARM Germany GmbH	Germany	Marketing of RISC-based microprocessors and development of integrated processor modelling solutions	100
Keil Elektronik GmbH	Germany	Marketing, research and development of microcontroller tools	100
ARM Embedded Technologies Pvt. Ltd.	India	Marketing, research and development of RISC-based microprocessors and physical IP	100
ARM Physical IP Asia Pacific Pte. Ltd.	Singapore	Marketing of physical IP	100
ARM Taiwan Limited	Taiwan	Marketing of RISC-based microprocessors	99.9
ARM Consulting (Shanghai) Co. Ltd.	PR China	Marketing of RISC-based microprocessors	100

* The Company itself owns less than 1% of the share capital of ARM Limited, the remaining shares are held indirectly through ARM Finance UK Limited and ARM Finance Two UK Limited. Both ARM Finance UK Limited and ARM Finance Two UK Limited are 100% owned within the Group.

Nominees of the Company hold 100% of the ordinary share capital of ARM Employee Benefit Trustee Ltd, a company which acts as trustee to the Group's ESOP.

30 Summary of significant differences between US GAAP and IFRS

- (i) **Goodwill** Under both IFRS and US GAAP, goodwill is not subject to amortisation, but is tested at least annually for impairment. As permitted by IFRS 1, the Group's goodwill under IFRS has been frozen at the amount recorded under UK GAAP as at 1 January 2004. Under US GAAP, following the provisions of SFAS 142, "Goodwill and other intangible assets", the carrying value of goodwill was frozen at the amount recorded under previous US GAAP as at 1 January 2002. Under both previous US GAAP and UK GAAP, goodwill was amortised over its useful economic life. Thus, while ongoing accounting policies in respect of goodwill are similar under US GAAP and IFRS, the difference in the dates of transition means that different amounts of goodwill are recorded.

Under US GAAP, certain costs to be incurred on restructuring on business combination are treated as a fair value adjustment in the balance sheet acquired. Under IFRS, these costs are expensed post-acquisition. Additionally, under US GAAP, tax benefits arising from the exercise of options issued as part of the consideration for a business combination become a deduction to goodwill, only to the extent that those benefits do not exceed the fair value of the consideration relating to those options at the appropriate tax rate. Any excess tax benefits are a deduction to equity. Under IFRS, the full tax benefit is a deduction to equity.

Where provisional assessments of the fair values of assets and liabilities acquired on acquisition are refined, adjustments to fair values are recorded as prior year adjustments to goodwill under IFRS. Under US GAAP, such revisions are recorded as amendments to goodwill in the subsequent year.

- (ii) **Recognition and amortisation of intangibles** The Group has taken advantage of the exemption under IFRS 1 not to apply IFRS retrospectively to business combinations occurring before 1 January 2004. This means that for business combinations occurring before this date, the previously reported UK GAAP treatment has continued to be followed. Under previous UK GAAP, intangible assets were recognised separately from goodwill only where they could be sold separately without disposing of a business of the entity. This separability criterion does not apply under either IFRS or US GAAP. Thus, a number of intangible assets which are required to be recognised separately from goodwill under both IFRS 3 and SFAS 142 were subsumed within goodwill under UK GAAP. Under both US GAAP and IFRS, such intangible assets are amortised over their useful economic lives. Except in relation to in-process research and development (see below), there is no difference in accounting policy for intangible assets recognised as a result of business combinations entered into after 1 January 2004.
- (iii) **In-process research and development** Under IFRS, in-process research and development projects purchased as part of a business combination may meet the criteria set out in IAS 38, "Intangible assets", for recognition as intangible assets other than goodwill and are amortised over their useful economic lives commencing when the asset is brought into use. Under US GAAP, in-process research and development is immediately written-off to the income statement. This accounting policy difference gives rise to an associated difference in deferred tax.
- (iv) **Valuation of consideration on business combination** Under both IFRS and US GAAP, the fair value of consideration in a business combination includes the fair value of both equity issued and any share options granted as part of that combination. Under IFRS, any equity issued is valued at the fair value as of the date of completion, whilst under US GAAP, the equity is valued at the date the terms of the combination were agreed to and announced. For options, under US GAAP, the fair value is based upon the total number of options granted, both vested and unvested, whilst under IFRS the fair value only includes those that have vested, together with a pro-rata value for partially vested options. Furthermore, where there is contingent consideration for an acquisition, under IFRS this is recognised as part of the purchase consideration if the contingent conditions are expected to be satisfied, whilst under US GAAP it is only recognised if the conditions have actually been met, other than to the extent necessary to eliminate any potential negative goodwill under US GAAP.
- (v) **Deferred compensation** Under US GAAP, the intrinsic value of unvested share options issued by an acquirer as part of a business combination in exchange for unvested share options of the acquiree is recorded as a debit balance within shareholders' funds. This amount is charged to the income statement over the vesting period of the share options in accordance with FIN 28. Under IFRS, no such adjustment to shareholders' funds is made on acquisition. Following the adoption of FAS No. 123 (revised 2004) (FAS 123(R)), "Share-based payment", the unamortised balance has been transferred to additional paid-in capital.
- (vi) **Compensation charge in respect of share-based payments** The Company issues equity-settled share-based payments to certain employees. In accordance with IFRS 2, equity-settled share-based payments are measured at fair value at the date of grant, using the Black-Scholes pricing model. The fair value, determined at the grant date of the equity-settled share-based payments, is expensed on a straight-line basis over the vesting period, based on the Company's estimate of the number of shares that will eventually vest.

Under US GAAP, the Company also expenses share-based payments, including employee stock-options, based on their fair value in accordance with FAS 123(R). Some awards made by the Company are liability-classified awards under FAS 123(R) as either: (i) there is an obligation to settle a fixed monetary amount in a variable number of shares; or (ii) the award is indexed to a factor other than performance, market or service condition. The fair value of these awards is remeasured at each period end until the award has vested. Once the award has vested, or for (i) above when number of shares becomes fixed, the award becomes equity-classified.

30 Summary of significant differences between US GAAP and IFRS continued

(vii) *Deferred tax on UK and US share options* In the US and the UK, the Group is entitled to a tax deduction for the amount treated as employee compensation under US and UK tax rules on exercise of certain employee share options. The compensation is equivalent to the difference between the option exercise price and the fair market value of the shares at the date of exercise.

Under IFRS, deferred tax assets are recognised and are calculated by comparing the estimated amount of tax deduction to be obtained in the future (based on the Company's share price at the balance sheet date) with the cumulative amount of the compensation expense recorded in the income statement. If the amount of estimated future tax deduction exceeds the cumulative amount of the remuneration expense at the statutory tax rate, the excess is recorded directly in equity, against the profit and loss reserve. In accordance with the transitional provisions of IFRS 2, no compensation charge is recorded in respect of options granted before 7 November 2002 or in respect of those options which have been exercised or have lapsed before 31 December 2004. Nevertheless, tax deductions have arisen and will continue to arise on these options. The tax effects arising in relation to these options are recorded directly in equity, against retained earnings.

Under US GAAP, deferred tax assets are recognised by multiplying the compensation expense recorded by the prevailing tax rate in the relevant tax jurisdiction. Where, on exercise of the relevant option, the tax benefit obtained exceeds the deferred tax asset in relation to the relevant options, the excess is recorded in additional paid-in capital. Where the tax benefit is less than the deferred tax asset, the write-down of the deferred tax asset is recorded against additional paid-in capital to the extent of previous excess tax benefits recorded in this account, with any remainder recorded in the income statement.

(viii) *Employer taxes on share-based remuneration* Under IFRS, employer's taxes that are payable on the exercise or vesting of share-based remuneration are provided for over the vesting period of the related option or award. Under US GAAP, such taxes are accounted for when the option or award is exercised or vests respectively.

(ix) *Accrued legal costs* Under IFRS, future legal fees that the Group is expecting to incur on current cases are accrued when the obligating event giving rise to the legal costs has occurred. Under US GAAP, such costs are charged to the income statement in the period in which the costs are incurred.

(x) *Sabbatical leave* The Company has adopted EITF 06-2 from 1 January 2007 in accounting for its provisions for employee sabbatical leave. To harmonise the accounting treatment under both GAAPs, the Company has also provided for sabbatical leave under IFRS. EITF 06-2 requires the opening provision at the beginning of the year to be charged directly to reserves, whilst under IFRS, the prior year results have been restated.

(xi) *FIN 48 adoption* On 1 January 2007, the Company adopted FIN 48, "Accounting for Uncertainty in Income Taxes". Under US GAAP, the cumulative effect of the change was a credit of £838,000 to retained earnings.

(xii) *Available-for-sale investment impairment* Accounting for impairments to available-for-sale investments is similar under both US GAAP and IFRS. However, an investment which was deemed to have suffered an other-than-temporary impairment in a prior period under US GAAP (with a corresponding charge being recognised in the income statement) was accounted for as a temporary impairment under IFRS (with the corresponding charge being recognised directly in reserves). In 2007, a further other-than-temporary impairment was made under both GAAPs with the result that the cumulative other-than-temporary impairments are now equal. Consequently a greater charge was made through the current year IFRS income statement, as the current year charge under IFRS includes the amount previously deemed to be temporary under IFRS but other-than-temporary under US GAAP.

α) Reconciliation of IFRS profit to US GAAP net income

	Note	2007 £000	2006 Restated £000
Profit for the financial year as reported under IFRS		35,250	48,156
Adjustments for:			
Amortisation of intangibles	(ii),(iii)	969	914
Write-off of in-process research and development	(iii)	–	(595)
Deduct: US GAAP compensation charge in respect of all share-based payments	(vi)	(15,979)	(21,787)
Add: IFRS compensation charge in respect of all share-based payments	(vi)	16,786	17,437
Employer's taxes on share options (net of tax)	(viii)	855	8
Provision for sabbatical leave (net of tax)	(x)	–	432
Provision for legal costs (net of tax)	(ix)	(609)	715
Provision against available-for-sale investment	(xii)	938	–
Tax on UK and US share options	(vii)	(3,708)	(2,204)
Tax difference on amortisation of intangibles	(ii),(iii)	(400)	(378)
Tax difference on share-based remuneration	(vii)	3,517	2,569
Other tax differences	(xi)	(838)	–
Foreign exchange on contingent consideration	(iv)	61	(104)
Net income as reported under US GAAP		36,842	45,163

30 Summary of significant differences between US GAAP and IFRS continued

b) Reconciliation of shareholders' equity from IFRS to US GAAP

	Note	2007 £000	2006 Restated £000
Shareholders' funds as reported under IFRS		579,162	660,926
Adjustments for:			
Utilisation of restructuring provision	(i)	1,368	1,368
Cumulative difference on amortisation of goodwill	(i)	2,713	2,713
Cumulative difference on amortisation of intangibles	(ii)	2,324	1,355
Cumulative write-off of in-process research and development	(iii)	(4,692)	(4,692)
Valuation of equity consideration on acquisition	(iv)	(82,435)	(82,435)
Valuation of option consideration on acquisition	(iv)	17,476	17,476
Deferred compensation on acquisition	(v)	(9,579)	(9,579)
Liability-classified share awards	(vi)	(1,649)	(2,416)
Employer's taxes on share-based remuneration	(viii)	1,277	38
Provision for legal costs (net of tax)	(ix)	106	715
Provision for sabbatical leave (net of tax)	(x)	–	2,278
Cumulative difference on deferred tax	(ii),(iii),(viii)	(1,426)	(642)
Deferred tax on share-based payments	(vii)	(8,768)	(8,911)
Portion of tax benefit arising on exercise of options issued on acquisition taken to goodwill under US GAAP	(i)	(4,844)	(4,844)
Foreign exchange on valuation of intangible assets and deferred tax	(ii),(iii)	2,707	1,358
Foreign exchange on valuation of contingent consideration	(iv)	–	(61)
Shareholders' equity as reported under US GAAP		493,740	574,647

c) Reconciliation of goodwill from IFRS to US GAAP

	Note	2007 £000	2006 Restated £000
Goodwill as reported under IFRS		420,835	427,679
Adjustments for:			
Amendments to provisional fair values	(i)	–	687
Valuation of restructuring provision on acquisition	(i)	1,235	1,235
Cumulative difference on amortisation of goodwill	(i)	2,713	2,713
Separately identifiable intangible assets	(ii)	(302)	(302)
Cumulative write-off of in-process research and development	(iii)	(150)	(150)
Valuation of equity consideration on acquisition	(iv)	(82,435)	(82,435)
Valuation of option consideration on acquisition	(iv)	17,476	17,476
Contingent consideration	(iv)	(1,339)	(3,117)
Portion of tax benefit arising on exercise of options issued on acquisition taken to goodwill under US GAAP	(i)	(4,248)	(4,248)
Deferred tax on capitalised in-process research and development	(iii)	(1,570)	(1,570)
Deferred compensation on acquisition	(v)	(9,579)	(9,579)
Foreign exchange on revaluation of goodwill	(i),(ii)	2,027	854
Goodwill as reported under US GAAP		344,663	349,243

Selected consolidated financial data/US GAAP

The following selected financial data should be read in conjunction with, and is qualified in its entirety by reference to, the financial statements of ARM Holdings plc ("the Company"), expressed in sterling, set forth on pages 104 to 132 of this report.

Selected consolidated financial data – US GAAP

	2003 £000	2004 £000	2005 £000	2006 £000	2007 £000
Revenues	128,070	152,897	232,439	263,254	259,160
Cost of revenues	(11,022)	(11,799)	(27,847)	(30,877)	(27,958)
Operating expenses	(99,785)	(109,587)	(156,675)	(187,357)	(188,364)
Income from operations	17,263	31,511	47,917	45,020	42,838
Interest, net	4,801	6,944	5,317	6,758	5,402
Profit on disposal of available-for-sale security	–	–	–	5,270	–
Minority interest	(105)	–	–	–	–
Income before income tax and cumulative effect of change in accounting policy	21,959	38,455	53,234	57,048	48,240
Provision for income taxes	(8,943)	(10,478)	(11,354)	(9,438)	(11,398)
Net income before cumulative effect of change in accounting policy	13,016	27,977	41,880	47,610	36,842
Cumulative effect of change in accounting policy	–	–	–	(2,447)	–
Net income	13,016	27,977	41,880	45,163	36,842
Diluted earnings per common share	1.3p	2.7p	2.9p	3.2p	2.7p
Research and development as a percentage of revenues	37.6%	33.0%	26.5%	28.7%	28.1%
Capital expenditure	£3,605	£5,036	£6,064	£8,559	£5,444
Cash, cash equivalents, short-term investments and marketable securities	£159,786	£142,817	£160,902	£128,494	£51,323
Shareholders' equity	£188,075	£552,327	£649,050	£574,647	£493,740
Total assets	£222,997	£637,937	£716,093	£652,703	£556,665
Employees at year-end (number)	740	1,171	1,324	1,659	1,728

The following discussion should be read in conjunction with the consolidated financial statements and notes thereto. The matters addressed in this operating and financial review and prospects, with the exception of the historical information presented, contain forward-looking statements involving risks and uncertainties.

Overview ARM designs the technology that lies at the heart of advanced digital products, from wireless, networking and consumer entertainment solutions to imaging, automotive, security and storage devices. ARM's comprehensive product offering includes 16/32-bit RISC microprocessors, data engines, graphics processors, digital libraries, embedded memories, peripherals, software and development tools, as well as analog functions and high-speed connectivity products. The Company licenses this technology to semiconductor companies which, in turn, manufacture, market and sell microprocessors and related products. ARM has developed an innovative, intellectual property-centred and market-driven business model in which it neither manufactures nor sells the products incorporating ARM technology, but concentrates on the research and development, design and support of the ARM architecture and supporting development tools and software. Combined with the company's broad Partner community, they provide a total system solution that offers a fast, reliable path to market for leading electronics companies.

Operating results

The Company has remained both profitable and cash generative (before investing activities). On operating profits of £42.8 million, cash inflows from operating activities were £62.7 million, resulting in cash being returned to shareholders through dividends and share buybacks of £147.1 million and a year-end cash, cash equivalents, short-term investments and marketable securities balance of £51.3 million.

The table below sets forth, for the periods indicated, the percentage of total revenues represented by certain items reflected in the Company's consolidated statements of income.

	Year ended 31 December		
	2005 %	2006 %	2007 %
Revenues			
Product revenues	93.7	93.9	93.7
Service revenues	6.3	6.1	6.3
Total revenues	100.0	100.0	100.0
Cost of revenues			
Product costs	9.4	9.1	8.3
Service costs	2.6	2.6	2.5
Total cost of revenues	12.0	11.7	10.8
Gross profit	88.0	88.3	89.2
Operating expenses			
Research and development	26.5	28.7	28.1
Sales and marketing	15.6	16.8	17.9
General and administrative	17.7	18.5	19.3
Restructuring costs	–	–	0.4
In-process research and development	0.1	0.2	–
Amortization of intangibles purchased through business combination	7.5	7.0	7.0
Total operating expenses	67.4	71.2	72.7
Income from operations	20.6	17.1	16.5
Interest, net	2.3	2.6	2.1
Profit on disposal of available-for-sale security	–	2.0	–
Income before income tax and cumulative effect of change in accounting policy	22.9	21.7	18.6
Provision for income taxes	4.9	3.6	4.4
Net income before cumulative effect of change in accounting policy	18.0	18.1	14.2
Cumulative effect of change in accounting policy, net of tax	–	0.9	–
Net income	18.0	17.2	14.2

Total revenues Total revenues were £259.2 million, a decrease of 1.6% from £263.3 million in 2006, which was an increase of 13% from £232.4 million in 2005. Dollar revenues were \$514.3 million in 2007, an increase of 6% from \$483.6 million in 2006, which was an increase of 16% from \$418.7 million in 2005. The actual average dollar exchange rate in 2006 was \$1.98 compared with \$1.84 in 2006. This had the effect of reducing total reported revenues by approximately £20.7 million.

Product revenues Product revenues consist of license fees, sales of development systems and royalties. Product revenues for 2005, 2006 and 2007 were £217.7 million, £247.2 million and £242.7 million, representing 94% of total revenues in each year. Product revenues in US dollars, being the primary currency of revenues generated, grew from \$392.2 million in 2005 to \$454.5 million in 2006 and \$482.3 million in 2007.

License revenues increased from £104.2 million in 2005 to £110.6 million in 2006, and were £110.7 million in 2007 representing approximately 45%, 42% and 42% of total revenues in 2005, 2006 and 2007 respectively. License revenues in US dollars grew from \$187.0 million in 2005 to \$202.5 million in 2006 and \$217.9 million in 2007.

Processor Division (PD) dollar license revenues have grown by 12% and 18% in 2006 and 2007 respectively. The portfolio of licensable products comprises a rich mix of proven ARM technology, such as the ARM7, ARM9 and ARM11 families of products and newer technology such as the Cortex family of products and the Mali graphics processors.

62 new licenses were signed in 2007 compared to 65 in 2006 and 71 in 2005. Revenues from Cortex family products accounted for 31% of PD license revenues in 2007, compared to 26% in 2006. Cortex products started generating revenue in 2005. ARM11 family products accounted for 23% of PD license revenues in 2007, compared to 22% in 2006 and 21% in 2005. 23 companies became new ARM Partners in 2007, bringing the total number of semiconductor Partners to 210 at the end of 2007. This total number of semiconductor Partners was net of those companies that have signed licenses with ARM in the past but have since been acquired by other companies or who no longer have access to ARM technology for other reasons.

During 2007, 14 Cortex family licenses were signed, including three lead Partners for the next-generation Cortex-A9 processor, bringing the accumulated total of Cortex family licenses to 37, signed by 28 semiconductor companies. Three licenses for ARM's Mali graphics processors were signed in 2007, bringing the accumulated total of Mali licenses to five. Nine semiconductor companies are now licensed to design products using ARM's graphics technology.

In addition, 2007 saw four large semiconductor companies underline their long term commitment to ARM technology by signing subscription licenses, which allow them access to a broad range of ARM processor technology. The term of these licenses is fixed and ranges between three and five years.

License revenues from non-core products, covering items such as platforms, peripherals, embedded trace modules, embedded software, data engines, models and sub-systems were £10.8 million in 2007, compared to £10.9 million in 2006 and £11.1 million in 2005 representing approximately 13% of processor license revenues in 2007, 14% in 2006 and 16% in 2005.

In 2007 ARM maintained progress in achieving the long-term strategic goal of providing ARM's physical IP to leading Integrated Device Manufacturers (IDM) and Fabless semiconductor companies and continued to sign synergistic licenses that have been enabled by the combination of ARM and Artisan. Synergistic deals include, in management's determination, both instances of physical IP being licensed to ARM Partners and instances of contracts being won against the competition due to both processor and physical IP being available from ARM.

Licensing momentum for ARM's 65nm physical IP products continued to grow, with ten new licenses signed in 2007. By the end of 2007, ARM had signed a total of 32 65nm licenses with 15 companies and had signed eight licenses for physical IP with four Foundries at the most advanced process of 45nm. ARM's Physical IP Division (PIPD) reported license revenues of £27.3 million in 2007, representing approximately 25% of total license revenues.

During 2007 the combination of ARM and Artisan has continued to provide benefits other than synergistic license revenues. In addition to the benefits to the Cortex family of processors, including the development of the new 12-track Advantage™ libraries in 65nm enabling higher performance, and the high-performance ARM1176JZF-S™ implementation, the combination has enabled the development of lower power processors with lower leakage, a new compact ARM11 MPCore™ dual processor delivering greater performance at lower power and development work on 45nm physical IP which will influence and optimize the design of future processors.

Revenues from the sale of development systems increased from £25.6 million in 2005 to £28.8 million in 2006 and fell to £27.9 million in 2007 representing approximately 11% of total revenues in each year. Development systems revenues in US dollars grew from \$46.5 million in 2005 to \$53.0 million in 2006 and \$55.6 million in 2007. This growth has been generated by working with customers on longer term relationships for the supply of RealView® Developer Tools for software development, continued momentum behind the RealView tools for ESL customers and a healthy market place for tools to support the ever-broadening portfolio of ARM microprocessors. The Systems Design Division (SDD) has continued to enter into more multi-year contracts for larger product volumes which improves the visibility of business going forward and builds a good customer base from which to drive new innovation.

Product revenues continued

Royalties are either set as a percentage of the licensee's average selling price (ASP) per chip or, less frequently, as a fixed amount and are recognized when the Company receives notification from the customer of product sales. In effect, this means that it is normally in the quarter following the shipments that data is received and so royalty data for a year reflects actual shipments made from the beginning of October of the previous year to the end of September of the current year. As the penetration of ARM technology-based chips grows across a wide range of end-market applications, the range of ASPs gets wider. The average royalty rate (ARR) earned by ARM in any one reporting period is dependent on the mix of the ASPs of the chips shipped in that period. In 2007, significant unit volume growth was driven by products which incorporate chips with lower ASPs including ultra low cost handsets, smartcards, microcontrollers and Bluetooth chips. As a result, the ARR in 2007 was 6.1 cents compared to 6.7 cents in 2006 and 7.9 cents in 2005. Unit volume growth more than compensated for this reduction in ARR and dollar royalty revenues grew by 8% year-on-year.

Royalties increased from £87.8 million in 2005 to £107.8 million in 2006 and fell to £104.1 million in 2007, representing 38%, 41% and 40% of total revenues in 2005, 2006 and 2007 respectively. US dollar royalty revenues grew from \$158.7 million in 2005 to \$199.0 million in 2006 and \$208.8 million in 2007. Royalty revenues in 2007 comprised £88.0 million from PD and £16.1 million from PIPD. PD volume shipments increased from 1.7 billion units in 2005 to 2.5 billion in 2006, with the increase in volumes coming from all market segments. Total unit shipments in 2007 of 2.9 billion represented an increase of 18% compared to 2006. Unit shipments in the mobile segment grew by 19% year-on-year and in the non-mobile segments by 15%. Growth in the non-mobile segments was achieved across a broad range of product applications including smartcards, microcontrollers, automotive, connectivity devices, hard disk drives and many others.

The Company expects royalty revenues to grow year-on-year although they may be subject to significant fluctuations from quarter to quarter. The total number of Partners shipping ARM technology-based products at the end of 2007 was 89 after taking into account corporate activity within the ARM partnership. 15 companies are paying meaningful royalties for physical IP products at the end of the year.

Service revenues Service revenues consist of revenues from support, maintenance and training and design consulting services. Service revenues increased from £14.7 million in 2005 to £16.1 million in 2006 and further to £16.4 million in 2007, representing 6% of total revenues in each year. Service revenues in US dollars, being the primary currency of revenues generated grew from \$26.5 million in 2005 to \$29.1 million in 2006 and \$32.0 million in 2007.

Geographic analysis Operating in a global environment, the geographic destinations of the Company's revenues fluctuate from period to period depending upon the country in which its customers are located. The pattern of revenues in 2007 was 42% from North America, 16% from Japan, 25% from Asia Pacific, excluding Japan, and 17% from Europe. In 2006, 42% of revenues came from North America, 26% from Japan, 16% from Asia Pacific, excluding Japan, and 16% from Europe. In 2005, revenues from North America represented 43%, Japan 18%, Asia Pacific, excluding Japan, 25%, and Europe 14%.

Product costs Product costs are limited to variable costs of production such as the costs of manufacture of development systems, amortization of third-party technology licenses, cross-license payments to collaborative Partners and time of engineers on PIPD projects. Product costs were £21.8 million in 2005, £24.2 million in 2006 and £21.5 million in 2007, representing 9%, 9% and 8% of total revenues in 2005, 2006 and 2007 respectively. In 2005 and 2006, the proportion of development systems costs was approximately a quarter, PIPD direct costs of approximately two-thirds and the balance third-party licenses and cross-license payments. In 2007, development systems costs made up approximately 20% of total product costs, PIPD direct costs approximately 70% and the balance on third-party licenses and cross license payments. Product gross margin in 2007 was 91%, compared to 90% in both 2006 and 2005. Included within product costs in 2005 are £2.5 million of deferred stock-based compensation relating to options assumed on the Artisan acquisition.

Service costs Service costs include the costs of support and maintenance services to licensees of ARM technology as well as the costs directly attributable to consulting work performed for third parties. Service costs increased from £6.1 million in 2005 to £6.7 million in 2006, and were £6.5 million in 2007. The gross margins earned on service revenues were approximately 59% in 2005, 58% in 2006 and 61% in 2007. Costs increased in 2006 as the business invested more in the engineering departments, a proportion of which is allocated to services costs. This has continued into 2007 with a slight reduction in costs due to reduced stock-based compensation costs being allocated to service costs; included within service costs in 2006 and 2007 are FAS 123R stock-based compensation costs of £1.1 million and £1.0 million respectively.

Research and development costs Research and development costs increased from £61.6 million in 2005 to £75.5 million in 2006 and were £72.7 million in 2007, representing 27%, 29% and 28% of total revenues in 2005, 2006 and 2007 respectively. Costs in 2006 and 2007 included £10.6 million and £9.3 million of share-based compensation charges in accordance with FAS 123R and in 2005 included £1.6 million of deferred share-based compensation respectively in accordance with previously applicable standards. Excluding these charges, R&D costs were 26%, 25% and 24% of total revenues in 2005, 2006 and 2007 respectively reflecting the operating leverage in the business. Continued investment in research and development remains an essential part of the Company's strategy since the development of new products to license is key to its ongoing success.

Research and development costs continued

Average engineering headcount increased from 783 in 2005 to 961 in 2006, with the increase coming from organic growth, predominantly in India, but also from the Falanx and Soisic acquisitions. Average engineering headcount increased further to 1,163 in 2007, mainly from the large number of hires towards the end of 2006 as well as measured growth in 2007. Again, this growth was predominantly in India, demonstrating ARM's gradual shift of engineering resource to lower cost regions. Staff costs increased in line with these headcount figures and mix of geographic locations, but bonuses payable on the achievement of financial performance targets in 2006 were higher than those in 2005 and 2007.

Sales and marketing Sales and marketing expenditure increased from £36.2 million in 2005 to £44.2 million in 2006 and £46.4 million in 2007, representing 16% of total revenues in 2005, 17% in 2006 and 18% in 2007. Costs in 2006 and 2007 included £3.7 million and £3.2 million of FAS 123R compensation charges respectively and in 2005 included £2.1 million of deferred stock-based compensation. The proportion of sales and marketing costs to revenue in 2005, 2006 and 2007 excluding these charges were 15%, 15% and 17% respectively. Average headcount in this area increased from 286 in 2005 to 302 in 2006 to 312 in 2007. Overall sales and marketing costs have increased in 2007 as further investment is made in customer support as well as due to increased staff bonuses based on a record bookings year.

General and administrative General and administrative costs were £41.1 million in 2005, £48.6 million in 2006 and £50.0 million in 2007, representing 18%, 18% and 19% of total revenues respectively. Excluding £3.5 million of deferred stock-based compensation in 2005 and £2.9 million and £2.6 million of FAS 123R compensation costs in 2006 and 2007, general and administrative costs were 16%, 17% and 18% of total revenues in 2005, 2006 and 2007 respectively.

General and administrative average headcount in 2007 was 226, up from 165 in 2005 and 209 in 2006. The increases year-on-year have partly come from the acquisitions but also organic growth to strengthen the infrastructure of the Company as it continually expands.

Unrealized future foreign exchange gains on certain committed but not yet invoiced future revenue streams of £1.4 million (2006: losses of £0.9 million; 2005: gains of £2.1 million) were recorded in 2007 in accordance with FAS 133, with other foreign exchange charges of £2.3 million in 2005 and gains of £3.6 million and £0.2 million in 2006 and 2007 respectively. The gain in 2006 was mainly as a result of the revaluation of an intra-group dollar loan. See "Foreign Currency Fluctuations" below. Furthermore, in 2007 there was a write-down in the carrying value of the Company's investment in Superscape Group plc of £1.2 million. Other increases in the last few years include additional recruitment and training costs for the growth in number of employees in the Company, increased IT costs to continually develop the ARM internal network as the number of offices and people grow and increased administrative costs relating to Sarbanes-Oxley compliance work.

Restructuring costs During 2007, the Company closed one of its design centres in the US resulting in restructuring costs of £1.0 million, primarily related to accrued rents, write-off of leasehold improvements and staff severance costs.

In-process research and development During 2004, the Company purchased Artisan Components Inc. (now ARM Inc.). Those intangible assets that were still in development (known as in-process research and development) were charged directly to the income statement, amounting to £3.2 million. A further £0.3 million of Artisan in-process research and development was charged to the income statement in 2005 as the final valuation of intangibles was completed. In 2006, the Company acquired the trade and certain assets of PowerEscape, resulting in £0.6 million of in-process research and development being charged to the income statement. All acquired in-process research and development from the Artisan and PowerEscape acquisitions are progressing as expected.

Amortization of intangible assets Various licenses to use third-party technology have been signed over the past several years, with their values being capitalized and amortized over the useful economic period that the Company is expected to gain benefit from them (generally between three and ten years). Licenses totalling £5.9 million were purchased during 2001 to 2005, with a further license for £2.5 million being purchased in 2007. Amortization of these licenses amounted to £0.4 million in 2007 (2006: £0.4 million; 2005: £0.5 million). At 31 December 2007, the net book value of these assets was £2.7 million which will be amortized over the next ten years.

Following the out-of-court settlement of the Company's litigation against picoTurbo, Inc. in December 2001, picoTurbo assigned its intellectual property rights to the Company for a payment of £7.5 million. This has been amortized over four years and £1.5 million was charged to the income statement in 2002 and £2.0 million in 2003, 2004 and 2005. The asset was fully written-down in 2005 and thus there was no further amortization charge in 2006 or 2007. The Company also purchased a patent for £0.7 million in 2002 which is being amortized over five years. The amortization charge was £0.1 million in 2005, 2006 and 2007 and was fully written-down by the end of 2007.

During 2003, the Company purchased Adelante Technologies NV (now ARM Belgium NV). Included with the assets purchased were £0.3 million of intangible assets comprising developed technology and customer relationships which are being amortized over five years and two years respectively. The amortization charge for the assets during 2005 and 2004 was £0.1 million in each year, but was less than £0.1 million in 2006 and 2007. This will become fully written-down during 2008.

Amortization of intangible assets continued

During 2004, the Company purchased Axys Design Automation Inc and Artisan Components Inc. (now ARM Inc.) Intangibles acquired and capitalized as part of these business combinations (including developed and core technology, customer relationships and trademarks) totalled £1.9 million and £70.9 million respectively and are being amortized over five years and between one and six years respectively (see note 6 for further details). The total charge during 2005 was £0.4 million and £16.5 million for Axys and Artisan respectively, during 2006 was £0.4 million and £14.6 million and during 2007 was £0.3 million and £13.3 million respectively.

During 2005, the Company purchased Keil Elektronik GmbH and Keil Software Inc. Intangibles acquired and capitalized consisted of developed technology, customer relationships and tradenames and totalled £8.7 million. These are being amortized between two and five years and the amortization was £0.4 million in 2005, £2.5 million in 2006 and £2.4 million in 2007.

During 2006, the Company purchased Falanx Microsystems AS, a graphics IP company in Norway. Intangibles acquired and capitalized consisted of developed technology and customer relationships and totalled £5.3 million. These are being amortized over three to five years and the charge in 2006 was £0.7 million and in 2007 was £1.2 million. The Company also purchased Soisic SA, an IP company based in France and the US. Intangibles acquired and capitalized were all developed technology and totalled £4.3 million. This is being amortized over five years with £0.1 million being charged in 2006 and £0.9 million in 2007.

Interest Interest receivable increased from £5.3 million in 2005 to £6.8 million in 2006, but decreased in 2007 to £5.4 million. The growth in interest in 2006 was due to higher average cash balances and increasing interest rates. The fall in 2007 was a result of the increased cash outflow during the year on share buybacks and dividends, resulting in lower average cash balances. The Company invested cash balances over periods of up to one year during 2007, although typically were for periods of less than six months.

Profit on disposal of available-for-sale security In 2006, the Company disposed of its investment in CSR plc for cash proceeds of £5.6 million and realised a profit of £5.3 million. The Company made no profit or loss on its disposal of a minority investment in Zeevo Inc. in 2005.

Income before income tax and cumulative effect of change in accounting policy Income before income tax was £53.2 million in 2005, £57.0 million in 2006 and £48.2 million in 2007, representing 23%, 22% and 19% of total revenues respectively. The margin fell in 2006 due to increased intangible amortization relating to business combinations following the acquisitions of the two Keil businesses, increased investment throughout the business in additional headcount as well as the negative impact of foreign exchange with the weakening of the US dollar in the year. This weakening of the dollar continued further in 2007 and was the primary reason for the drop in margin in 2007.

Tax charge The Company's effective tax rates were 21.3% in 2005, 16.5% in 2006 and 23.6% in 2007. The effective tax rate in 2005 was lower than the blended tax rates from the relevant tax jurisdictions due to additional costs being allowable for research and development tax credits, benefits arising from the structuring of the Artisan acquisition and additional deferred tax credits arising from employee share options. It fell further in 2006 due to a non-recurring tax credit arising from a tax-deductible foreign exchange loss and continued benefits from the structuring of the Artisan acquisition. The rate returned to a higher level in 2007 (without the non-recurring foreign exchange loss in 2006) but was still benefiting from the aforementioned items.

Cumulative effect of change in accounting policy On 1 January 2006, the Company adopted FAS 123R as detailed in the Accounting for share-based payments in the significant accounting policies in note 1. The transitional rules detailed in FAS 123R required the Company to make a remeasurement adjustment for compensation cost for liability awards that has been recognized in 2006 as a cumulative effect of change in accounting policy in the income statement. The charge in 2006, net of tax, was £2,447,000.

Liquidity and capital resources The Company's operating activities provided net cash of £47.2 million, £66.1 million and £62.7 million in 2005, 2006 and 2007 respectively.

Accounts receivable increased by £21.2 million in 2005 and a further £19.0 million in 2006, but decreased by £0.3 million in 2007. The increase in 2005 and 2006 was partly due to growth in revenues, but largely to do with timing of invoicing in the respective periods. In the final week of 2006, there was significantly more invoicing to customers than in the final week of 2005 resulting in a large increase in receivables. Invoicing in the corresponding period in 2007 was at a similar level to 2006. Despite this, days' sales outstanding improved from 54 at 31 December 2005 to 43 at 31 December 2006 and were 49 at 31 December 2007. Included within accounts receivable are amounts recoverable on contracts as discussed within deferred revenue below. Prepaid expenses fell by £1.4 million in 2005 and a further £0.5 million in 2006, but increased by £2.6 million in 2007. The fall in 2005 and 2006 reflected the amortization of a technology license agreement representing prepaid royalties to be released over several years. The increase in 2007 was mainly due to a four-year agreement for EDA tools, where, for commercial reasons, monies were paid upfront. Inventory has increased to £2.3 million in 2007 reflecting growth in the development systems business. There have been no other significant movements in other current assets.

Liquidity and capital resources continued

Accounts payable fell by £1.9 million in 2005 and a further £0.7 million in 2006, but increased by £0.4 million in 2007, reflecting the timing of receipt of supplier invoices in the respective years. Accrued liabilities fell by £5.6 million in 2005, increased by £2.1 million in 2006 and fell again by £8.4 million in 2007. These fell in 2005 as payments on a technology license agreement were made and accrued employee compensation was lower in 2005 than in 2004. The main increase in 2006 was as a result of increased staff bonus and sales commission provisions following a then record bookings quarter in the final quarter of 2006. The fall in 2007 was due to lower staff and sales bonuses in 2007 compared to 2006, reduced FAS 133 provision for embedded derivatives on uninvoiced but committed future billings, reduced accrued payables on acquisition consideration, as well as the timing of invoicing on some large EDA lease contracts resulting in lower accruals.

At 31 December 2007, the Company recorded approximately £27.5 million of deferred revenues which represented cash or receivables scheduled to be recognized as revenues in varying amounts after 31 December 2007. At 31 December 2006, the Company recorded approximately £31.5 million of deferred revenues. Deferred revenues are an element of customer backlog, and represent amounts invoiced to customers not yet recognized as revenues in the income statement. Similarly, the Company recorded £24.5 million of amounts recoverable on contracts (AROC) at 31 December 2007, compared to £23.8 million at 31 December 2006. AROC represents amounts that have been recognized as revenue in the income statement but are yet to be invoiced to customers. Both deferred revenue and AROC fluctuate due to the maturity profile of ARM's products, and invoicing milestones within contracts.

The Company believes that, given its current level of business, it has sufficient working capital for the foreseeable future.

Cash flow from operations has been used to fund the working capital requirements of the Company as well as capital expenditure. Cash outflow from capital expenditure in 2007 was £5.4 million, compared with £8.6 million in 2006 and £6.1 million in 2005. Capital expenditure increased in 2005 and 2006 with staff levels increasing and general operational assets being replaced. In 2007, the Company purchased a technology license for £2.5 million, as noted above, which will be amortized over ten years.

In 2005, the Company made final payments relating to acquisition costs for Artisan of £14.4 million, as well as £1.7 million of contingent consideration in respect of the Axys acquisition as a result of performance conditions being achieved. A further £4.3 million (net of cash acquired) was paid for the acquisitions of Keil Elektronik GmbH and Keil Software Inc.

In 2006, the Company acquired Falanx Microsystems AS and Soisic SA for cash consideration paid in the year of £13.4 million and £2.1 million respectively. Additionally in 2006, a further £1.1 million was paid for Keil (acquired in 2005) and £0.6 million for the trade and certain assets of PowerEscape.

In 2007, whilst no acquisitions were made, the Company did make additional payments for the Keil businesses of £1.8 million representing retentions and contingent consideration, as well as £1.5 million for Soisic relating to escrow payments and contingent consideration. Further payments on both Keil and Soisic are expected in 2008.

The Company envisages making further strategic investments in the future, in situations where the Company can broaden its product portfolio, where it can obtain skilled engineering resources and where the potential for furthering ARM technology-based design wins is improved significantly.

In 2005, £0.3 million was invested via convertible loan notes in Luminary Micro Inc., an unlisted company. A further £0.2 million was invested in Luminary in 2006. In 2007, £2.5 million was invested via convertible loan notes in W&W Communications Inc., an unlisted US company. This loan note earns interest at 10% per annum and will convert to a maximum holding of 14.99% upon further fundraising by the Company.

The Company sold its investment in CSR plc in 2006 for £5.6 million.

During 2005, the Company initiated a share buyback program to supplement dividends in returning surplus funds to shareholders. During 2005, the Company bought back over 13.9 million shares at a total cost of £16.2 million and during 2006, the Company bought back 63.6 million shares at a total cost of £76.5 million. This was accelerated further in 2007 with 94.5 million shares being repurchased at a total cost of £128.6 million. Dividends totalling £18.5 million were also paid to shareholders during the year (2006: £12.4 million; 2005: £10.4 million). In aggregate, the Company has returned over £270 million since 2004 through buybacks and dividends. Share option exercises in 2007 gave rise to £18.9 million cash inflow to the Company compared to £17.9 million in 2006 and £13.9 million in 2005.

Cash, cash equivalents, short- and long-term investment and marketable securities balances at 31 December 2007 were £51.3 million compared to £128.5 million at 31 December 2006 and £160.9 million at 31 December 2005.

Foreign currency fluctuations The Company's earnings and liquidity are affected by fluctuations in foreign currency exchange rates, principally the US dollar rate, as most of the Company's revenues and cash receipts are denominated in US dollars while a high proportion of its costs are in sterling.

The Company reduces this US dollar/sterling risk where possible by currency hedging. Due to the high value and timing of receipts on individual licenses and the requirement to settle certain expenses in US dollars, the Company reviews its foreign exchange exposure on a transaction-by-transaction basis. It then hedges this exposure using forward contracts for the sale of US dollars, which are negotiated with major UK clearing banks. The average size of each forward contract was \$4.3 million in 2005, \$3.9 million in 2006 and \$4.2million in 2007. The Company also uses currency options as a further translation instrument for limited proportions of its dollar exposure. The fair values of the financial instruments outstanding at 31 December 2005, 2006 and 2007 are disclosed in note 15 to the financial statements. The settlement period of the forward contracts outstanding at 31 December 2007 was between 8 January 2008 and 26 March 2008. The settlement period of the option contracts outstanding at 31 December 2007 was between 23 January 2008 and 5 January 2009.

Quantitative and qualitative information on market risk During the preceding fiscal year, the Company was exposed to foreign currency exchange risk inherent in its sales commitments, anticipated sales, anticipated purchases and assets and liabilities denominated in currencies other than sterling. ARM transacts business in approximately eight foreign currencies worldwide, of which the most significant to the Company's operations were the US dollar, the Indian rupee, the euro and the Japanese yen for 2007. Generally, the Company is a net receiver of US dollars, and therefore benefits from a weaker sterling and is adversely affected by a stronger sterling relative to the dollar. It is a net payer of other foreign currencies but at a significantly lower level than the US dollar receivables. The Company has performed a sensitivity analysis at 31 December 2007, 2006 and 2005, using a modeling technique that measures the changes in the fair values arising from a hypothetical 10% adverse movement in the levels of foreign currency exchange rates relative to sterling with all other variables held constant. The analysis covers all of the Company's foreign currency contracts offset by the underlying exposures. The foreign currency exchange rates used were based on market rates in effect at 31 December 2007, 2006 and 2005. The sensitivity analysis indicated that a hypothetical 10% adverse movement in foreign currency exchange rates would result in a loss in the fair values of ARM's foreign exchange derivative financial instruments, net of exposures, of £11.5 million at 31 December 2007 (2006: £8.9 million, 2005: £3.9 million).

Risk factors The Company operates in the intensely competitive semiconductor industry which is characterized by price erosion, rapid technological change, short product life cycles, cyclical market patterns and heightened foreign and domestic competition. The Company believes that its future operating results will continue to be subject to quarterly variations based upon a wide variety of factors. These include the timing of entering into agreements with new licensees, the mixture of license fees, royalties and fees from services, the introduction of new technology by the Company, the timing of orders from, and shipments to, systems companies of ARM core-based microprocessors from the Company's semiconductor Partners and sudden technological change in the microprocessor industry.

Other risks include the reliance on semiconductor Partners, dependence upon systems companies, patent protection, attraction and retention of employees, management of growth, competition and vulnerability to general economic conditions. Risk factors are more fully discussed in the Company's annual report on Form 20-F.

Consolidated statements of income/US GAAP

For the years ended 31 December

	2005 £000	2006 £000	2007 £000
Revenues			
Product revenues	217,711	247,194	242,726
Service revenues	14,728	16,060	16,434
Total revenues	232,439	263,254	259,160
Cost of revenues			
Product costs	(21,754)	(24,156)	(21,475)
Service costs	(6,093)	(6,721)	(6,483)
Total cost of revenues	(27,847)	(30,877)	(27,958)
Gross profit	204,592	232,377	231,202
Operating expenses			
Research and development	(61,633)	(75,498)	(72,744)
Sales and marketing	(36,234)	(44,198)	(46,393)
General and administrative	(41,082)	(48,643)	(49,964)
Restructuring costs	–	–	(1,037)
In-process research and development	(335)	(595)	–
Amortization of intangibles purchased through business combination	(17,391)	(18,423)	(18,226)
Total operating expenses	(156,675)	(187,357)	(188,364)
Income from operations	47,917	45,020	42,838
Interest, net	5,317	6,758	5,402
Profit on disposal of available-for-sale security	–	5,270	–
Income before income tax and cumulative effect of change in accounting policy	53,234	57,048	48,240
Provision for income taxes	(11,354)	(9,438)	(11,398)
Net income before cumulative effect of change in accounting policy	41,880	47,610	36,842
Cumulative effect of change in accounting policy, net of tax	–	(2,447)	–
Net income	41,880	45,163	36,842
Basic earnings (before cumulative effect of change in accounting policy) per common share	3.1p	3.5p	2.8p
Basic earnings (after cumulative effect of change in accounting policy) per common share	3.1p	3.3p	2.8p
Diluted earnings (before cumulative effect of change in accounting policy) per common share	2.9p	3.4p	2.7p
Diluted earnings (after cumulative effect of change in accounting policy) per common share	2.9p	3.2p	2.7p

All activities relate to continuing operations.

The accompanying notes are an integral part of the financial statements.

Consolidated statements of comprehensive income/US GAAP

For the years ended 31 December

	2005 £000	2006 £000	2007 £000
Net income	41,880	45,163	36,842
Realized gain on available-for-sale security, net of tax of £850,000	–	(2,375)	–
Unrealized holding losses on available-for-sale securities, net of tax of £146,000 (2006: £477,000; 2005: £981,000)	(2,316)	(1,090)	(608)
Currency translation adjustment	58,561	(68,128)	(6,777)
Total comprehensive income/(loss)	98,125	(26,430)	29,457

Consolidated balance sheets/US GAAP

At 31 December

	2006 £000	2007 £000
Assets		
Current assets:		
Cash and cash equivalents	90,743	49,509
Short-term investments	18,600	232
Marketable securities	19,151	1,582
Accounts receivable, net of allowances for doubtful debts of £1,504,000 (2006: £2,556,000) (see footnote 10)	69,552	68,232
Inventory: finished goods	1,933	2,339
Income taxes receivable	5,761	6,552
Prepaid expenses and other assets	12,668	13,089
Investments	–	1,180
Total current assets	218,408	142,715
Deferred income taxes	9,872	11,309
Prepaid expenses and other assets	1,328	2,860
Property and equipment, net	13,970	12,042
Goodwill	349,243	344,663
Other intangible assets	56,027	39,375
Investments	3,855	3,701
Total assets	652,703	556,665
Liabilities and shareholders' equity		
Current liabilities:		
Accounts payable	1,826	2,230
Income taxes payable	5,572	3,704
Personnel taxes	1,408	1,751
Accrued liabilities (see footnote 11)	33,021	25,670
Deferred revenue	31,485	27,543
Total current liabilities	73,312	60,898
Deferred income taxes	4,744	2,027
Total liabilities	78,056	62,925
Commitments and contingencies (see footnote 13)		
Shareholders' equity		
Ordinary shares: £0.0005 par value; 2,200,000,000 authorized (2006: 2,200,000,000); 1,344,055,696 issued (2006: 1,389,907,834)	695	672
Additional paid-in capital	446,005	367,680
Treasury stock, at cost: 66,402,610 ordinary shares (2006: 50,701,434)	(58,245)	(90,000)
Retained earnings	197,874	234,455
Accumulated other comprehensive income:		
Unrealized holding gain on available-for-sale securities, net of tax asset of £85,000 (2006: £231,000)	394	(214)
Cumulative translation adjustment	(12,076)	(18,853)
Total shareholders' equity	574,647	493,740
Total liabilities and shareholders' equity	652,703	556,665

The accompanying notes are an integral part of the financial statements.

Consolidated statements of cash flows/US GAAP

For the years ended 31 December

	2005 £000	2006 £000	2007 £000
Cash flows from operating activities			
Net income	41,880	45,163	36,842
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization of tangible and intangible assets	28,060	25,812	25,939
Write-off in-process research and development	335	595	–
Profit on disposal of available-for-sale security	–	(5,270)	–
Stock option compensation	9,727	21,788	15,979
Excess tax benefits from share-based compensation	–	(3,682)	(2,546)
Provision for doubtful accounts	722	932	215
Provision for slow-moving inventories	22	65	247
Amount written off investments	337	–	1,162
Loss on disposal of property, plant and equipment	16	63	317
Changes in operating assets and liabilities:			
Accounts receivable	(21,247)	(18,986)	260
Inventory	(519)	(508)	(653)
Prepaid expenses and other current assets	1,446	454	(2,647)
Accounts payable	(1,931)	(672)	404
Income taxes payable	(3,093)	(12,758)	(867)
Deferred revenue	(2,043)	11,071	(3,877)
Accrued liabilities and other creditors	(5,569)	2,056	(8,424)
Personnel taxes	(963)	(71)	343
Net cash provided by operating activities	47,180	66,052	62,694
Cash flows from investing activities:			
Purchase of equipment	(5,956)	(7,476)	(4,093)
Purchase of leasehold improvements	(108)	(1,083)	(1,351)
Sale of equipment	37	31	–
Purchase of patent and licenses	–	–	(2,549)
Purchase of investments	(274)	(165)	(2,657)
Sale of investments/available-for-sale securities	96	5,567	–
(Purchase)/maturity of short-term investments	(569)	(4,926)	35,937
Purchase of subsidiaries and businesses, net of cash acquired	(20,304)	(17,270)	(3,357)
Net cash (used in)/provided by investing activities	(27,078)	(25,322)	21,930
Cash flows from financing activities:			
Cash received on issue of new share capital on exercise of share options	13,083	2,106	5,509
Proceeds received on issuance of shares from treasury stock	838	15,754	13,383
Excess tax benefits from share-based compensation	–	3,682	2,546
Purchase of own shares	(16,211)	(76,519)	(128,561)
Payment of dividends	(10,436)	(12,367)	(18,547)
Net cash used in financing activities	(12,726)	(67,344)	(125,670)
Effect of foreign exchange on cash and cash equivalents	10,140	(10,720)	(188)
Net increase/(decrease) in cash and cash equivalents	17,516	(37,334)	(41,234)
Cash and cash equivalents at beginning of the period	110,561	128,077	90,743
Cash and cash equivalents at end of the period	128,077	90,743	49,509
Supplemental disclosure of cash flow information:			
Cash paid for income taxes	14,447	21,147	12,265
Cash received on interest	5,444	6,636	5,607

The accompanying notes are an integral part of the financial statements.

Consolidated statements of changes in shareholders' equity/US GAAP

	Ordinary shares Number	Amount £000	Additional paid-in capital £000	Deferred compen- sation £000	Treasury stock £000	Retained earnings* £000	Accumulated other comprehensive income		Total £000
							Unrealized holding gain £000	Cumulative translation adjustment £000	
Balances, 31 December 2004	1,350,786,975	675	414,133	(12,083)	(7,485)	153,421	6,175	(2,509)	552,327
Shares issued on exercise of options	35,315,705	18	13,065	–	–	–	–	–	13,083
Net income	–	–	–	–	–	41,880	–	–	41,880
Dividends	–	–	–	–	–	(10,436)	–	–	(10,436)
Tax effect of disqualifying dispositions	–	–	370	–	–	–	–	–	370
Deferred compensation arising on share schemes	–	–	3,290	(3,290)	–	–	–	–	–
Tax benefits on exercise of options issued as part consideration for a business combination	–	–	1,227	–	–	–	–	–	1,227
Amortization of deferred compensation	–	–	–	9,727	–	–	–	–	9,727
Reversal of unearned compensation	–	–	(1,242)	1,242	–	–	–	–	–
Issuance of shares from treasury	–	–	(5,591)	–	7,381	(952)	–	–	838
Purchase of own shares	–	–	–	–	(16,211)	–	–	–	(16,211)
<i>Accumulated other comprehensive income:</i>									
Unrealized holding losses on available-for-sale securities (net of tax of £981,000)	–	–	–	–	–	–	(2,316)	–	(2,316)
Currency translation adjustment	–	–	–	–	–	–	–	58,561	58,561
Balances, 31 December 2005	1,386,102,680	693	425,252	(4,404)	(16,315)	183,913	3,859	56,052	649,050
Shares issued on exercise of options	3,805,154	2	2,104	–	–	–	–	–	2,106
Net income	–	–	–	–	–	45,163	–	–	45,163
Dividends	–	–	–	–	–	(12,367)	–	–	(12,367)
Tax effect of option exercises	–	–	3,682	–	–	–	–	–	3,682
Netting of deferred compensation**	–	–	(4,404)	4,404	–	–	–	–	–
Amortization of deferred compensation	–	–	19,371	–	–	–	–	–	19,371
Issuance of shares from treasury	–	–	–	–	34,589	(18,835)	–	–	15,754
Purchase of own shares	–	–	–	–	(76,519)	–	–	–	(76,519)
<i>Accumulated other comprehensive income:</i>									
Realized gain on available-for-sale security (net of tax of £850,000)	–	–	–	–	–	–	(2,375)	–	(2,375)
Unrealized holding losses on available-for-sale securities (net of tax of £477,000)	–	–	–	–	–	–	(1,090)	–	(1,090)
Currency translation adjustment	–	–	–	–	–	–	–	(68,128)	(68,128)
Balances, 31 December 2006	1,389,907,834	695	446,005	–	(58,245)	197,874	394	(12,076)	574,647

	Ordinary shares Number	Amount £000	Additional paid-in capital £000	Deferred compen- sation £000	Treasury stock £000	Retained earnings* £000	Accumulated other comprehensive income		Total £000
							Unrealized holding gain £000	Cumulative translation adjustment £000	
Balances, 31 December 2006	1,389,907,834	695	446,005	–	(58,245)	197,874	394	(12,076)	574,647
Shares issued on exercise of options	9,866,862	5	5,504	–	–	–	–	–	5,509
Net income	–	–	–	–	–	36,842	–	–	36,842
Dividends	–	–	–	–	–	(18,547)	–	–	(18,547)
First time adoption of EITF 06-2, net of tax***	–	–	–	–	–	(2,278)	–	–	(2,278)
First-time adoption of FIN 48	–	–	–	–	–	838	–	–	838
Tax effect of option exercises	–	–	2,546	–	–	–	–	–	2,546
Amortization of deferred compensation	–	–	15,350	–	–	–	–	–	15,350
Conversion of liability award to equity award	–	–	1,396	–	–	–	–	–	1,396
Issuance of shares from treasury	–	–	–	–	30,767	(17,384)	–	–	13,383
Purchase of own shares	–	–	–	–	(128,561)	–	–	–	(128,561)
Cancellation of shares	(55,719,000)	(28)	–	–	66,039	(66,011)	–	–	–
Cancellation of share premium account	–	–	(103,121)	–	–	103,121	–	–	–
<i>Accumulated other comprehensive income:</i>									
Unrealized holding losses on available-for-sale securities (net of tax of £146,000)	–	–	–	–	–	–	(608)	–	(608)
Currency translation adjustment	–	–	–	–	–	–	–	(6,777)	(6,777)
Balances, 31 December 2007	1,344,055,696	672	367,680	–	(90,000)	234,455	(214)	(18,853)	493,740

* The amount of shareholders' equity available for distribution to shareholders is the amount of profits determined under UK GAAP in the statutory accounts of the parent company. At 31 December 2007, such distributable profits amounted to £334,156,000.

** FAS123R requires that deferred stock-based compensation on the date of adoption be netted against additional paid-in capital.

*** In accordance with EITF 06-2, the cumulative provision for employee sabbatical leave as at 1 January 2007 is charged directly to retained earnings.

The accompanying notes are an integral part of the financial statements.

1 The Company and a summary of its significant accounting policies

The business of the Company ARM Holdings plc and its subsidiary companies (ARM or "the Company") design reduced instruction set computing (RISC) microprocessors, physical IP and related technology and software, and sell development systems, to enhance the performance, cost-effectiveness and power-efficiency of high-volume embedded applications. The Company licenses and sells its technology and products to leading international electronics companies, which in turn manufacture, market and sell microprocessors, application-specific integrated circuits (ASICs) and application-specific standard processors (ASSPs) based on the Company's architecture to systems companies for incorporation into a wide variety of end products. By creating a network of Partners, and working with them to best utilize the Company's technology, the Company is establishing its architecture as a RISC processor for use in many high-volume embedded microprocessor applications, including digital cellular phones, modems and automotive functions and for potential use in many growing markets, including smart cards and digital video. The Company also licenses and sells Development Systems direct to systems companies and provides consulting and support services to its licensees, systems companies and other systems designers. The Company's principal geographic markets are Europe, the US and Asia Pacific.

Incorporation and history ARM is a public limited company incorporated under the laws of England and Wales. The Company was formed on 16 October 1990, as a joint venture between Apple Computer (UK) Limited, and Acorn Computers Limited, and operated under the name Advanced RISC Machines Holdings Limited until 10 March 1998, when its name was changed to ARM Holdings plc. Its initial public offering was on 17 April 1998.

Group undertakings include ARM Limited (incorporated in the UK), ARM Inc. (incorporated in the US), ARM KK (incorporated in Japan), ARM Korea Limited (incorporated in South Korea), ARM France SAS (incorporated in France), ARM Belgium NV (incorporated in Belgium), ARM Germany GmbH (incorporated in Germany), Keil Elektronik GmbH (incorporated in Germany), ARM Norway AS (incorporated in Norway), ARM Embedded Technologies Pvt Limited (incorporated in India), ARM Physical IP Asia Pacific Pte. Limited (incorporated in Singapore), ARM Taiwan Limited (incorporated in Taiwan) and ARM Consulting (Shanghai) Co. Limited (incorporated in PR China). All entities are 100% owned.

Basis of preparation The accompanying consolidated financial statements have been prepared under the historical cost convention and in accordance with accounting principles generally accepted in the United States (US GAAP). The Company maintains its accounting records and prepares its financial statements in UK sterling.

Use of estimates The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from these estimates.

Principles of consolidation The consolidated financial statements incorporate the financial statements of the Company and all its subsidiaries. Intra-group transactions, including sales, profits, receivables and payables, have been eliminated on consolidation. The results of subsidiaries acquired in the year are included in the income statement from the date they are acquired. On acquisition, all of the subsidiaries' assets and liabilities that exist at the date of acquisition are recorded at their fair values reflecting their condition at that date.

Investments Publicly traded investments are classed as available-for-sale in accordance with Statement of Financial Accounting Standards No.115, "Accounting for certain investments in debt and equity securities" (FAS 115), and are carried at fair value. Unrealized holding gains or losses on such securities are included, net of related taxes, in other comprehensive income. Other-than-temporary impairment losses and realized gains and losses of such securities are reported in earnings. Equity securities that are not publicly traded are recorded at cost less permanent diminution in value; at 31 December 2007 and 2006, the estimated fair value of these investments approximated their recorded basis, based on estimates determined by management.

Intangible assets Purchased patents and licenses to use technology are capitalized and amortized on a straight-line basis over a prudent estimate of the time that the Company is expected to benefit from them.

Although an independent valuation is made of any intangible assets purchased as part of a business combination, management is primarily responsible for determining the fair value of intangible assets. Such assets are capitalized and amortized over a period of one to six years, being a prudent estimate of the time that the Company is expected to benefit from them, with the exception of in-process research and development which is written off immediately.

Goodwill Goodwill represents the excess of the fair value of the consideration paid on acquisition of a business over the fair value of the assets, including any intangible assets identified and liabilities acquired.

Goodwill is tested for impairment at least annually. Annual impairment reviews in 2006 and in 2007 determined, primarily with reference to cash flow forecasts, that there was no indication of impairment with respect to goodwill. The estimates of future cash flows involve considerable management judgment and are based on assumptions about expected future operating performance. The actual cash flows could differ from management's estimates due to changes in business conditions, operating performance and economic conditions.

1 The Company and a summary of its significant accounting policies continued

Goodwill continued

In accordance with FAS 131 "Disclosures about Segments of an Enterprise and Related Information", the Company has identified its operating segments based on the information used by the Chief Operating Decision Maker in monitoring the business. For the purposes of assessing the carrying value of goodwill for impairment, goodwill has been allocated to reporting units. Based on the nature and extent of discrete information available to management, the Company believes that, for ARM, each operating segment consists of a single reporting unit. Goodwill has been allocated to the three reporting units as shown in note 9.

Impairment charges The Company reviews goodwill for impairment annually or more frequently if events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. It also reviews long-lived assets and identifiable intangibles for impairment if an event occurs that indicates that the carrying amount may not be recoverable. If the sum of the expected future cash flows (undiscounted and without interest charges) of the long-lived assets is less than the carrying amount of such assets, an impairment loss would be recognized, and the assets would be written down to their estimated fair value.

Revenue recognition Revenue consists of license fees received under the terms of license agreements with customers to enable them to use the Company's intellectual property (IP), which is often customized to each customer's manufacturing process. The Company receives royalties on sales by the Company's customers of products containing ARM technology. It also supplies off-the-shelf software tools and IP, bought-in boards and toolkits, training and consultancy services.

The Company primarily earns revenues from licensing its IP to leading electronics companies which in turn manufacture, market and sell microprocessors, ASICs and ASSPs based on the Company's architecture to systems companies for incorporation into a wide variety of end products. The Company's IP consists of software and related documentation which enables a customer to design and manufacture microprocessors and related technology and software. Most licenses are designed to meet the specific requirements of each customer and are generally not time limited in their application. In general, the time between the signing of a license and final validation of the customer's ARM technology-compliant product is between six and 15 months. Specified upgrades or modifications to the licensed IP are not provided. Following validation of the customer's ARM technology-compliant product, the Company has no further obligations under the license agreement.

In accordance with SOP 81-1, "Accounting for performance of construction-type and certain production type contracts," when license agreements include deliverables that require "significant production, modification or customization," contract accounting is applied. Revenues from license fees are recognized based on the percentage-of-completion method over the period from signing of the license to validation of the customer's ARM technology-compliant product and the completion of all outstanding obligations. The amount of revenue recognized is based on the total license fees under the license agreement, or that portion of the total license fees which is determined to be fixed or determinable in arrangements involving extended payment terms and the percentage-of-completion achieved. Those amounts that are not deemed fixed or determinable at the outset of the arrangement are recognized as the payments become due. Where an arrangement is for multiple elements, each requiring significant production, modification or customization, the Company evaluates whether the bifurcation criteria of SOP 81-1 are met, and if so, the total arrangement fee is allocated accordingly. The percentage-of-completion is measured by monitoring progress using records of actual time incurred to date in the project, compared with the total estimated project requirement. Revenues are recognized only when collectability is probable. Estimates of total project requirements are based on prior experience of customization, delivery and validation of the same or similar technology and are reviewed and updated regularly by management. Under the percentage-of-completion method, provisions for estimated losses on uncompleted contracts are recognized in the period in which the likelihood of such losses is determined.

Agreements that include rights to unspecified future products (as opposed to unspecified upgrades and enhancements) are accounted for using subscription accounting, revenue from the arrangement being recognized ratably over the term of the arrangement, or an estimate of the economic life of the products offered if no term is specified, beginning with the delivery of the first product.

In accordance with SOP 97-2, "Software revenue recognition," where agreements involve elements that do not require "significant production, modification or customization," the Company recognizes license revenue when a signed contract or other persuasive evidence of an arrangement exists, the product has been shipped or electronically delivered, the license fee is fixed or determinable and collection of the resulting receivable is probable. Where agreements include multiple elements, the revenue recognition criteria for each element are typically met within the same accounting period, i.e. on delivery of the elements. If an element that is essential to the functionality of the delivered elements is undelivered at a period end, the Company determines whether it has sufficient vendor specific objective evidence (VSOE) of fair value in order to make an allocation amongst the elements. For the majority of its products and services, with the exception of post-contract support (PCS), certain development systems products and certain services undertaken by the Company, the Company does not believe it has sufficient VSOE of fair value to make such allocations. Accordingly, no revenue is recognized on an arrangement where deliverables other than PCS and the aforementioned development systems products and services remain undelivered.

1 The Company and a summary of its significant accounting policies continued

Revenue recognition continued

License fees are considered fixed or determinable if they are not dependent on customers completing specific milestones and they are not subject to extended payment terms, i.e. the payment terms do not extend over a substantial period when compared to the payment terms in similar license arrangements and when compared with the licensed products' life cycle. If all the fees in an arrangement are deemed to be fixed or determinable, the Company recognizes revenue when all other revenue recognition criteria have been met. The excess of revenue recognized in respect of such fees over fees invoiced is recorded as an accrued revenue asset. Where an arrangement includes fees that are not deemed fixed or determinable, revenue from the arrangement is recognized as the payments become due and the excess of fees invoiced over revenue recognized in respect of such fees is recorded as a deferred revenue liability.

PCS consists of the right to receive services and/or unspecified product upgrades/enhancements that are offered on a when-and-if-available basis. PCS is generally priced separately from the initial licensing fee in a contract and revenue is allocated to PCS based on VSOE of fair value. VSOE of fair value is determined with reference to contractual renewal rates. If no renewal rates are specified, the entire fee under the arrangement is amortised and recognised ratably over the contractual PCS period. Where renewal rates are specified, PCS revenue is recognised ratably over the term of the PCS arrangement.

Certain products have been co-developed by the Company and a collaborative partner, with both parties retaining the right to sell licenses to the product. In those cases where the Company makes sales of these products and considers itself to be the principal under EITF 99-19, "Reporting Revenue Gross as a Principal versus Net as an Agent," the total value of the license is recorded as revenue and the amount payable to the collaborative partner is recorded as cost of sales. Where the collaborative partner makes sales of these products, the Company records as revenue the commission it is due when informed by the collaborative partner that a sale has been made and cash has been collected.

Sales of boards and toolkits are recognized upon delivery. While some arrangements with distributors provide very limited rights of return, the Company's history is that actual returns are negligible and accordingly no provisions are deemed necessary.

Services, such as consulting and training, are typically sold in stand-alone arrangements. Where they are sold in conjunction with other deliverables and they are not considered essential to the functionality of those other deliverables, they are accounted for separately based on VSOE, if VSOE has been established. Revenue for these services is recognized as the services are performed and collectability is probable. If VSOE for the services does not exist or the services are deemed to be essential to the functionality of the other deliverables in the arrangement, the entire arrangement fee is recognized as the services are performed. The excess of fees invoiced over revenue recognized in respect of such fees is recorded as a deferred revenue liability.

Revenues from consulting projects, which are typically of a short duration, are recognized when the service has been provided and all obligations to the customer under the consulting agreement have been fulfilled. For longer term and more complex consulting projects, typically containing several project milestones, where significant modification to ARM technology-based IP is required, revenues are recognized on a percentage-of-completion basis as milestones are achieved. This method approximates to percentage-of-completion based on labor inputs.

Royalty revenues are earned on sales by the Company's customers of products containing ARM technology. Revenues are recognized when the Company receives notification from the customer of product sales, or receives payment of any fixed royalties. Notification is typically received in the quarter following shipment of product by the customer.

Where the Company enters into more than one agreement with the same customer in the same, short time frame, an assessment is made to establish whether the group of agreements is so closely related that they effectively form a single multiple-element arrangement. The factors considered in making this assessment include, but are not limited to:

- Whether the different elements are closely interrelated or interdependent in terms of design, technology, or function;
- Whether the fee for one or more of the agreements is subject to a refund or forfeiture or other concession if one of the other contracts is not completed satisfactorily;
- Whether one or more elements in one agreement are essential to the functionality of an element in another agreement;
- Whether payment terms under one agreement coincide with performance criteria of another agreement; and
- Whether the negotiations are conducted jointly with two or more parties to do what in essence is a single project.

Research and development All ongoing research and development expenditure is expensed in the period in which it is incurred. Costs include salaries of engineers and associated staff, relevant EDA tools costs and other directly related expenditure, such as contractors, as well as an allocation of facilities costs. The facilities costs for each office are allocated according to the proportion of employees in engineering functions within these offices. Any collaborative agreements whereby a third party agrees to partially fund the Company's research and development is recognised over the period of the agreement as a credit within research and development costs.

1 The Company and a summary of its significant accounting policies continued

Grants Grants in respect of specific research and development projects are receivable from the European Commission, a European organization which funds certain research and development activities on application to it for the purposes of furthering research and development activities within the European Union. The Company retains significant rights to IP developed under projects which are funded under these arrangements. Grants received are typically intended to cover 50% of expected project costs. Grant income is recognized over the period of the project in line with the costs incurred. Unconditional undertakings have been received from the European Commission to provide the funding, and there is no obligation to refund any amounts already received. Amounts receivable under these arrangements in the year ended 31 December 2007 were £289,000 (2006: £467,000; 2005: £nil) and were netted against related research and development costs.

Pension costs The Company contributes to defined contribution plans substantially covering all employees in Europe and the US and to government pension schemes for employees in Japan, South Korea, Taiwan, PR China and Israel. The Company contributes to these plans based upon various fixed percentages of employee compensation and such contributions are expensed as incurred. The amount of contributions expensed by the Company for the years ended 31 December 2005, 2006 and 2007 were £3,371,000, £3,840,000 and £4,327,000 respectively.

Loss contingencies The Company accrues an estimated loss contingency when it is probable that a liability has been incurred and the amount of the loss can be reasonably estimated.

Fair value of financial instruments The Company's financial instruments consist principally of cash and cash equivalents, short-term investments and marketable securities, accounts receivable and foreign currency exchange contracts. The Company believes all of the financial instruments carrying values approximate to fair value due to their nature and respective durations.

Cash equivalents The Company considers all highly liquid investments with original maturity dates of three months or less to be cash equivalents.

Short-term investments and marketable securities The Company considers all highly liquid investments with original maturity dates of greater than three months but less than one year to be either short-term investments (when invested on deposit with major clearing banks) or short-term marketable securities (when custodied with major financial institutions). Any investments with a maturity date of greater than one year are classified as long-term marketable securities.

Allowance for doubtful debts Allowance is made for doubtful debts following reviews of individual customer circumstances by management.

Inventory Inventory is stated at the lower of cost and net realizable value. In general, cost is determined on a first-in-first-out basis and includes transport and handling costs. Where necessary, provision is made for obsolete, slow-moving and defective inventory.

Property and equipment The cost of property and equipment is their purchase cost, together with any incidental costs of acquisition. Costs that are directly attributable to the development of new business application software and which are incurred during the period prior to the date that the software is placed into operational use, are capitalized. External costs and internal costs are capitalized to the extent they enhance the future economic benefit of the business.

Depreciation is calculated so as to write off the cost of property and equipment, less their estimated residual values, on a straight-line basis over the expected useful economic lives of the assets concerned. The principal economic lives used for this purpose are:

Freehold buildings	25 years
Leasehold improvements	Five years or term of lease, whichever is shorter
Computers and software	Three to five years
Fixtures and fittings	Five to ten years
Motor vehicles	Four years

Provision is made against the carrying value of property and equipment where an impairment in value is deemed to have occurred.

Operating leases Costs in respect of operating leases are charged on a straight-line basis over the lease term.

Currency translation The Company's functional currency is the currency of the primary economic environment in which the Company operates.

The assets and liabilities of subsidiaries with functional currencies other than sterling are translated into sterling at rates of exchange ruling at the balance sheet date. Statements of income of overseas subsidiaries are translated at the monthly exchange rates during the year. Translation differences are taken to the cumulative translation adjustment.

1 The Company and a summary of its significant accounting policies continued

Currency translation continued

The Company utilizes forward exchange contracts and currency options to manage the exchange risk on actual transactions related to accounts receivable, denominated in a currency other than the functional currency of the business. The Company's forward exchange contracts do not subject the Company to risk from exchange rate movements because the gains and losses on such contracts offset losses and gains, respectively, on the transactions being hedged. Because the Company does not meet the criteria for hedge accounting, the forward and option contracts and the related accounts receivable are recorded at fair value at each period end. All recognized gains and losses resulting from the settlement of the contracts are recorded within general and administrative costs in the income statement. The fair value of derivative instruments are disclosed within either prepaid expenses and other assets or accrued liabilities on the balance sheet and within net cash provided by operating activities in the cash flow statement. The Company does not enter into foreign exchange contracts for the purpose of hedging anticipated transactions.

Other transactions denominated in foreign currencies have been translated into sterling at actual rates of exchange ruling at the date of transaction. Monetary assets and liabilities denominated in foreign currencies have been translated at rates ruling at the balance sheet date. Exchange differences have been included in general and administrative costs.

From time to time, the Company enters into contracts denominated in a currency (typically US dollars) that is neither the functional currency of the Company nor the functional currency of the customer. In accordance with FAS 133, "Accounting for derivative instruments and hedging activities", where there are unpaid amounts on such contracts, the Company carries such derivatives at fair value. The resulting gain or loss is recognized in the income statement under general and administrative costs. For the year ended 31 December 2007 the gain on exchange is £1,400,000 (2006: loss of £898,000; 2005: gain of £2,101,000).

Income taxes Income taxes are computed using the liability method. Under this method, deferred income tax assets and liabilities are determined based on temporary differences between the financial reporting and tax bases of assets and liabilities and are measured using enacted tax rates and laws that will be in effect when the differences are expected to reverse. Valuation allowances are established against deferred tax assets where it is more likely than not that some portion or all of the asset will not be realized.

The Company applies the "with and without" approach with respect to the allocation of net operating losses and other reliefs due to share-based compensation costs. Under this approach a benefit is recorded in additional paid-in capital only to the extent that the amount of available net operating losses generated for operations can be offset against the current year taxable income.

In July 2006 the FASB issued Interpretation, or FIN, No. 48, "Accounting for Uncertainty in Income Taxes – An Interpretation of FASB Statement No. 109", (FIN 48). FIN 48 provides detailed guidance for the financial statement recognition, measurement and disclosure of uncertain tax positions recognized in an enterprise's financial statements in accordance with FAS 109. Income tax positions must meet a more-likely-than-not recognition threshold at the effective date to be recognized upon the adoption of FIN 48 and in subsequent periods. The Company adopted FIN 48 effective 1 January 2007 and the provisions of FIN 48 have been applied to all income tax positions commencing from that date. Potential accrued interest and penalties related to unrecognized tax benefits within operations are recognized as an income tax expense. The cumulative effect of applying the provisions of FIN 48 has been reported as an adjustment to retained earnings as of 1 January 2007. Prior to 2007, tax contingencies were determined in accordance with FAS No. 5 "Accounting for contingencies" (FAS 5) and estimated tax liabilities were recorded to the extent the contingencies were probable and could be reasonably estimated.

Earnings per share Basic earnings per common share is computed based on the weighted average number of ordinary shares. Diluted earnings per common share is computed by including potential common shares where the effect of their inclusion would be dilutive. The diluted share base for the year ended 31 December 2007 excludes incremental shares of approximately 8,786,000 (2006: 33,390,000; 2005: 39,614,000) related to employee stock options and awards. These shares are excluded due to their antidilutive effect as a result of the exercise price of these shares being higher than the market price. The ordinary equivalent shares for share options were determined using the treasury stock method.

Accounting for share-based payments Since 1 January 2006, the Company has applied FASB Statement No. 123 (revised 2004), "Share-Based Payment" (FAS 123R) in relation to accounting for share-based payments. Under FAS 123R, share-based compensation cost is measured at the grant date, based on the estimated fair value of the award, and is recognized as expense over the employee's requisite service period. The fair value of these awards is calculated using appropriate valuation techniques.

Some awards made by the Company are liability-classified awards under FAS 123R as (i) there is an obligation to settle a fixed monetary amount in a variable number of shares; or (ii) the awards are indexed to a factor other than performance, market or service condition. The fair value of these awards is re-measured at each period end until the award has vested. Once the award has vested, or for (i) above when the number of shares becomes fixed, the award becomes equity-classified. The transitional rules detailed in FAS 123R required the Company in 2006 to make a re-measurement adjustment for compensation cost for liability awards that had been recognised in that year as a cumulative effect of change in accounting policy in the income statement.

1 The Company and a summary of its significant accounting policies continued

Accounting for share-based payments continued

The Company adopted the provisions of FAS 123R using a modified prospective application. Accordingly, periods prior to adoption have not been revised for comparative purposes. The valuation provisions of FAS 123R apply to new awards and to awards that are outstanding on the effective date, which are subsequently modified or cancelled. Estimated compensation expense for awards outstanding at the effective date will be recognized over the remaining service period using the compensation cost calculated for pro forma disclosure purposes under FASB Statement No. 123, "Accounting for Stock-Based Compensation" (FAS 123).

On 10 November 2005, the FASB issued FASB Staff Position No. FAS 123(R)-3, "Transition Election Related to Accounting for Tax Effects of Share-Based Payment Awards." The Company elected to adopt the alternative transition method provided in this FASB Staff Position for calculating the tax effects of share-based compensation pursuant to FAS 123R. The alternative transition method includes a simplified method to establish the beginning balance of the additional paid-in capital pool (APIC pool) related to the tax effects of employee share-based compensation, which is available to absorb tax deficiencies which could be recognized subsequent to the adoption of FAS 123R.

For a summary of all the Company's share-based award schemes, please refer to the Shareholder's equity section in footnote 12.

The Company uses the Black-Scholes option pricing model to estimate the fair value of share-based payments. This model is consistent with that used for the Company's pro forma information required under FAS 123. The determination of the fair value using this model is affected by the share price at grant, as well as a number of other assumptions including expected volatility, expected life, risk-free interest rate and expected dividends.

Treasury stock Treasury stock represents the cost of shares in the Company held by the Company and the Employee Benefit Trust (ESOP).

During 2007, to supplement the payment of dividends to shareholders, the Company continued its rolling share buyback programme under the shareholder authority conferred at the 2007 Annual General Meeting. The quantum and frequency of share re-purchases is not predetermined and will take into account prevailing market conditions, the short- to medium-term cash needs of the business and the level of employee share-based remuneration going forward. In 2007, a total of 94,525,548 (2006: 63,600,000; 2005: 13,868,000) shares were re-purchased from the market at a cost of £128,561,000 (2006: £76,519,000; 2005: £16,211,000). At 31 December 2007, there were 65,201,176 (2006: 49,500,000) shares in the Company still held from these purchases with a market value of £80,849,000 (2006: £62,246,000).

The ESOP was set up on 16 April 1998 to facilitate the recruitment, retention and motivation of employees. Under the Company's Long Term Incentive Plan, 7,943,979 shares could be awarded from shares already issued within the ESOP and treasury stock held by the Company. The number of unearned shares within the ESOP at 31 December 2007 was 1,201,434 (2006: 1,201,434) with a market value of £1,490,000 (2006: £1,511,000).

All costs relating to the schemes are recognized in the income statement as they accrue and the ESOP has waived the right to receive dividends of over and above 0.01 pence per share on all shares held. For the purpose of earnings per share calculations, the shares are treated as canceled until such time as they vest unconditionally.

Employer's taxes on share options Employer's National Insurance in the UK and equivalent taxes in other jurisdictions are payable on the exercise of certain share options issued to employees in certain tax jurisdictions. In accordance with EITF 00-16 no provision has been made for the employer's taxes on these share options. These amounts are recognized in the consolidated income statement when payable.

Provision for accrued sabbatical leave The Company operates a sabbatical leave scheme for employees that have had at least four years' service. In accordance with EITF 06-2 "Accounting for Sabbatical Leave and Other Similar Benefits", a provision is created with a corresponding charge being made to the income statement over the period this leave is earned based on management's estimate of the leave that will eventually be taken. This provision is released to the income statement as employees either take the leave or cease to be employees of the Company. The Company adopted EITF 06-2 from 1 January 2007 and in accordance with the standard recorded the opening provision against retained earnings.

Recently issued accounting standards In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" (FAS 157), which provides guidance on how to measure assets and liabilities that use fair value. FAS 157 will apply whenever another US GAAP standard requires (or permits) assets or liabilities to be measured at fair value but does not expand the use of fair value to any new circumstances. FAS 157 will be effective for our financial statements for the year ending 31 December 2008. We are currently evaluating the potential impact this standard may have on our financial position and results of operations, but do not believe the impact of the adoption will be material. This is supplemented by FSP FAS 157-1 which defers the requirement to fair value non-financial assets and liabilities until ARM's fiscal year ending 31 December 2009.

1 The Company and a summary of its significant accounting policies continued

Recently issued accounting standards continued

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities, including an Amendment of FASB Statement No. 115" (FAS 159) which provides companies the irrevocable option to measure many financial assets and liabilities at fair value with the changes in fair value recognized in earnings. The accounting provisions of FAS 159 will be effective for the Company's financial year ending 31 December 2008. The Company is in the process of determining the effects, if any, the adoption of FAS 159 will have on its consolidated financial statements, but do not believe the impact of the adoption will be material.

In June 2007, the EITF issued the statement EITF 07-1, "Accounting for Collaborative Arrangements", which discusses the accounting for arrangements with third parties and whether transactions should be reported gross or net in the financial statements. We currently already apply the provisions of EITF 99-19, "Reporting Revenue Gross as a Principal versus Net as an Agent" and as such do not believe the impact of adoption will be material.

In December 2007 the FASB issued SFAS No. 141R, "Business Combinations" (FAS 141R), which amends principles and requirements for how the acquirer of a business recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any non-controlling interest in the acquiree. The statement also amends guidance for recognizing and measuring the goodwill acquired in the business combination and determines what information to disclose to enable users of the financial statement to evaluate the nature and financial effects of the business combination. FAS 141R will be effective for the Company's financial statements for the year ending 31 December 2009. Accordingly, any business combinations the Company engages in will be recorded and disclosed following existing GAAP until 1 January 2009. We expect FAS 141R will have an impact on the Company's consolidated financial statements when effective, but the nature and magnitude of the specific effects will depend upon the nature, terms and size of the acquisitions consummated after the effective date. We are still assessing the impact of this standard on our future consolidated financial statements.

In December 2007, the US Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin 110 (SAB 110) to amend the SEC's views discussed in Staff Accounting Bulletin 107 (SAB 107) regarding the use of the simplified method in developing an estimate of expected life of share options in accordance with FAS 123R. SAB 110 is effective for the Company beginning in the first quarter of 2008. We will continue to use the simplified method until we have the historical data necessary to provide a reasonable estimate of expected life in accordance with SAB 107, as amended by SAB 110.

Companies Act 1985 These financial statements do not comprise statutory accounts within the meaning of Section 240 of the Companies Act 1985 of Great Britain (the "Companies Act"). The Company's statutory accounts, which are its primary financial statements, are prepared in accordance with International Financial Reporting Standards (IFRSs) for consolidated accounts and accounting principles generally accepted in the United Kingdom (UK GAAP) for ARM Holdings plc company only accounts. They are prepared in compliance with the Companies Act and are presented in pounds sterling. Statutory accounts (upon which the auditors gave unqualified reports under Section 235 of the Companies Act and which did not contain statements under sub-sections 237(2) and (3) of the Companies Act) for the years ended 31 December 2005 and 2006 have been, and those for the year ended 31 December 2007 will be delivered to the Registrar of Companies for England and Wales. Dividends are required to be declared in sterling out of profits available for that purpose as determined in accordance with UK GAAP and the Companies Act.

2 Related party transactions

During the year, the Company paid royalty fees of £81,000 (2006: £124,000; 2005: £33,000) and made cross-licence payments of £nil (2006: £nil; 2005: £26,000) to Superscape Group plc (Superscape), a company in which Mike Inglis, an executive director of ARM, was a non-executive director during the year. Amounts owed to Superscape at 31 December 2007 and 2006 were £nil. In addition, in 2007 the Company received royalty fees of £14,000 (2006: £19,000; 2005: £2,000) and licence fees of £nil (2006: £nil; 2005: £11,000) from Superscape. At 31 December 2007, £nil (2006: £17,000) was owed by Superscape.

Also in 2007, the Company received licence fees of £4,000 (2006: £3,085,000; 2005: £321,000), support and maintenance income of £32,000 (2006: £37,000; 2005: £37,000) and evaluation tools fees of £123,000 (2006: £82,000; 2005: £17,000) from CSR plc, a company in which John Scarisbrick, a non-executive of ARM, was an executive director during the year. Amounts owed by CSR plc at 31 December 2007 were £31,000 (2006: £14,000).

During 2007, the Company received funding for SOI technology development of £1,507,000 (2006: £319,000; 2005: £nil) from SOI TEC Silicon On Insulator Technologies SA ("Soitec"). Furthermore, the Company paid £181,000 (2006: £nil; 2005: £nil) to Soitec during the year in relation to license income from the two parties' ongoing collaborative agreement to develop SOI technology. Soitec is an SOI IP company in which Doug Dunn, Company Chairman, is a non-executive director. At 31 December 2007, £nil (2006: £383,000) is owed by Soitec. Amounts owed to Soitec at 31 December 2007 and 2006 were £nil.

3 Income taxes

Income before income tax is analyzed as follows:

	Year ended 31 December		
	2005 £000	2006 £000	2007 £000
United Kingdom	47,930	19,886	54,950
Foreign	5,304	37,162	(6,710)
	53,234	57,048	48,240

The provision for income taxes consisted of:

	Year ended 31 December		
	2005 £000	2006 £000	2007 £000
Current			
United Kingdom	15,519	9,958	14,090
Foreign	1,430	6,138	4,676
Total current	16,949	16,096	18,766
Deferred			
United Kingdom	(1,241)	(5,476)	(2,536)
Foreign	(4,354)	(1,182)	(4,832)
Total deferred	(5,595)	(6,658)	(7,368)
Total provision for income taxes	11,354	9,438	11,398

Included in the income tax payable is a current tax benefit of £2,546,000 (2006: £3,682,000; 2005: £370,000) and a deferred tax credit of £nil (2006: £nil; 2005: £6,072,000) in relation to employee stock options. Such benefits are reflected as additional paid-in capital.

Also included in the provision for income taxes is utilization of the deferred tax liability in relation to acquired intangibles of £7,231,000 (2006: 6,264,000; 2005: £6,921,000).

Total income tax expense differs from the amounts computed by applying the UK statutory income tax rate of 30% for 2007, 2006 and 2005 to income before income tax as a result of the following:

	Year ended 31 December		
	2005* £000	2006* £000	2007 £000
UK statutory rate 30% (2006: 30%; 2005: 30%)	15,970	17,114	14,472
Research and development tax credits	(1,911)	(2,879)	(5,170)
Permanent differences – foreign exchange	–	(7,558)	(84)
Permanent differences – other**	(3,164)	(5,603)	(3,007)
Valuation allowances	112	3,394	4,824
Amortization of intangibles	(1,730)	(1,467)	(1,279)
Differences in statutory rates of foreign countries	(45)	613	(895)
Foreign withholding tax	1,444	2,450	912
Stock-based compensation expense	749	1,747	548
Other, net***	(71)	1,627	1,077
	11,354	9,438	11,398

* The 2005 and 2006 comparatives have been reclassified for comparability with 2007.

** Permanent differences comprise permanent adjustments and benefits resulting from re-structuring following the acquisition of Artisan.

*** Other, net comprises prior year adjustments and deferred tax adjustments.

3 Income taxes continued

Significant components of the deferred tax assets/(liabilities) are as follows:

	At 31 December	
	2006 £000	2007 £000
Deferred tax assets		
<i>Current</i>		
Stock compensation charge	5,016	6,447
Temporary difference on available-for-sale securities	231	678
Non-deductible accruals and reserves	1,766	7,562
Losses carried forward	12,816	7,101
	19,829	21,788
Valuation allowance	(3,838)	(6,612)
Net current deferred tax assets	15,991	15,176
<i>Non-current</i>		
Fixed asset temporary differences	5,244	4,610
R&D tax credits carried forward	6,178	5,149
	11,422	9,759
Valuation allowance	(2,211)	(2,962)
Net non-current deferred tax assets	9,211	6,797
Deferred tax liabilities		
<i>Non-current</i>		
Amounts relating to intangible assets arising on acquisition	(20,074)	(12,691)
Total non-current deferred tax liabilities	(20,074)	(12,691)
Net non-current deferred tax assets/(liabilities)	(10,863)	(5,894)

Disclosed on the balance sheet within:

	At 31 December	
	2006 £000	2007 £000
Assets	9,872	11,309
Liabilities	(4,744)	(2,027)
Net deferred tax assets/(liabilities)	5,128	9,282

Included in the amount of £12,691,000 (2006: £20,074,000) relating to intangible assets on acquisition is £6,735,000 (2006: £13,178,000) relating to liabilities that are expected to accrue after more than one year.

The valuation allowance for deferred tax assets increased by £3,525,000 in 2007 primarily due to non-deductible interest carryforwards of certain foreign subsidiaries, where management believes it is more likely than not that such amounts will not be realised. If or when recognised, the benefits relating to any reversal of the valuation allowance on deferred tax assets at 31 December 2007 will be accounted for as follows: £8,034,000 as a reduction of income tax expense and £1,540,000 as a reduction of goodwill.

The Company has net operating loss carryforwards for tax purposes and other deferred tax benefits that are available to offset against future taxable income. At 31 December 2007 the Company has US federal, US state, United Kingdom, Norwegian, French and Belgian net operating loss carryforwards of approximately £13.7 million, £14.2 million, £10.2 million, £1.9 million, £6.4 million and £1.3 million respectively. If unutilized, the US federal net operating loss will begin to expire in 2019 and the US state net operating loss will begin to expire in 2013.

In addition to the net operating losses the Company also had unutilized federal R&D tax credits of £5,737,000 which will begin to expire in 2012 and unutilized state R&D tax credits of £3,191,000 which have no expiration date.

The future use of the net operating losses carried forward in ARM Inc. may be restricted in the event of a purchase by a third party, whereby the level of losses to be utilized on an annual basis would be limited to 4% of the market value of ARM Inc. at the date of the transaction.

3 Income taxes continued

As a result of FAS 123R, the Company's deferred tax assets at 31 December 2007 do not include £2,713,000 of excess tax benefits from employee share option exercises in 2007 and £1,909,000 due to exercises in 2006 that are a component of the Company's research and development and net operating loss carryovers. Equity will be increased by £4,622,000 if and when such excess tax benefits are ultimately realized.

Undistributed earnings of the Company's foreign subsidiaries amounted to approximately £31,655,000 (2006: £31,809,000) at 31 December 2007. Those earnings are considered to be indefinitely reinvested and accordingly no UK income taxes have been provided thereon. If these earnings were to be remitted without offsetting tax credits in the UK, taxes would be approximately £7,981,000 (2006: £10,758,000).

On 1 January 2007, the Company adopted the provisions of FIN 48 "Accounting for Uncertainty in Income Taxes". As a result of applying the provisions of FIN 48, the Company recognised a decrease of £838,000 in the liability for unrecognised tax benefits, which was accounted for as an increase to the opening retained earnings. The Company's unrecognised tax benefits at 31 December 2007 relate to the UK and various foreign jurisdictions. The following table summarises the movements in unrecognised tax benefits:

	\$000
Balance at 1 January 2007	4,327
Increases related to current year tax positions	3,188
Decreases related to prior year tax positions	(232)
Balance at 31 December 2007	7,283

Included in the balance at 31 December 2007 are £3,175,000 of tax benefits that, if recognised, would reduce our annual effective tax rate. The Company recognised accrued interest of £131,000 related to these unrecognised tax benefits during 2007 in income tax expense. The Company does not expect its unrecognised tax benefits to change significantly over the next 12 months.

The tax years 2004 through to 2007 generally remain subject to examination by the UK tax authorities. In the US, the tax years 2001 through to 2007 generally remain subject to examination by federal and most state tax authorities.

4 Earnings per share

	Year ended 31 December 2005		
	Income £	Shares Number	Per share Amount
Net income	41,880,000		
Basic EPS:			
Income available to common stockholders	41,880,000	1,369,335,202	3.1p
Effect of dilutive securities:			
Share options and awards		57,701,294	
Diluted EPS:			
Income available to common stockholders plus assumed conversion	41,880,000	1,427,036,496	2.9p

	Year ended 31 December 2006		
	Income £	Shares Number	Per share Amount
Basic EPS:			
Net income before cumulative effect of change in accounting policy	47,610,000	1,366,816,499	3.5p
Cumulative effect of change in accounting policy	(2,447,000)		(0.2p)
Net income after cumulative effect of change in accounting policy	45,163,000		3.3p
Effect of dilutive securities:			
Share options and awards		37,934,830	
Diluted EPS:			
Net income before cumulative effect of change in accounting policy	47,610,000	1,404,751,329	3.4p
Cumulative effect of change in accounting policy	(2,447,000)		(0.2p)
Net income after cumulative effect of change in accounting policy	45,163,000		3.2p

4 Earnings per share continued

	Year ended 31 December 2007		
	Income £	Shares Number	Per share Amount
Net income	36,842,000		
Basic EPS:			
Income available to common stockholders	36,842,000	1,321,860,197	2.8p
Effect of dilutive securities:			
Share options and awards		44,523,595	
Diluted EPS:			
Income available to common stockholders plus assumed conversion	36,842,000	1,366,383,792	2.7p

5 Business risks and credit concentration

The Company operates in the intensely competitive semiconductor industry which has been characterised by price erosion, rapid technological change, short product life cycles, cyclical market patterns and heightened foreign and domestic competition. Significant technological changes in the industry could affect operating results.

Financial instruments that potentially subject the Company to concentrations of credit risk comprise principally cash, cash equivalents, short- and long-term investments and marketable securities and accounts receivable. The Company generally does not require collateral on accounts receivable, as many of the Company's customers are large, well-established companies. The Company has not experienced any significant losses related to individual customers or groups of customers in any particular industry or geographic area.

The Company markets and sells to a relatively small number of customers with individually large value transactions. At 31 December 2005, 2006 and 2007 no customers accounted for more than 10% of accounts receivable.

At 31 December 2006 and 2007, the Company's cash, cash equivalents, short-term investments and marketable securities were deposited with major clearing banks and building societies in the UK and US in the form of money market deposits and corporate bonds for varying periods up to two years.

6 Acquisitions

There were no acquisitions in 2007, but the following acquisitions were made in 2005 and 2006.

Falanx Microsystems AS

On 30 May 2006, the Company purchased the entire share capital of Falanx Microsystems AS (Falanx), a graphics IP company incorporated in Norway for total consideration of \$25.1 million (£13.4 million), comprising \$24.9 million cash consideration and \$0.2 million of related acquisition expenses.

Falanx developed graphics accelerator IP and software for semiconductor system-on-chip (SoC) vendors that delivered high-quality multimedia images without compromising performance, power consumption or system cost. The acquisition fits the ARM strategy of enabling users to create SoCs seamlessly in their design process. The Mali Graphics Processor Unit (GPU) is a combination of hardware and software that enables industry-leading 3D graphics and video on mobile phones, portable media players, set-top boxes, handheld gaming devices and automotive systems, providing the Company with full control over the development of its future 3D graphics solutions.

The purchase price was allocated to the tangible and intangible assets acquired and liabilities assumed on the basis of their estimated fair values on the acquisition date.

The operating results for Falanx have been included in these financial statements for the period from 30 May 2006 to 31 December 2006 in the 2006 comparatives and for the entire year in 2007. The acquisition was accounted for under FAS 141.

6 Acquisitions continued

The following table sets out the provisional fair values of the assets acquired and liabilities assumed at the date of acquisition as reported in the 2006 annual report:

	Fair value to Company £000
Assets	
Cash and cash equivalents	24
Accounts receivable, net	118
Other debtors	101
Deferred tax asset	543
Property and equipment, net	62
Total assets acquired	848
Liabilities	
Accounts payable and other creditors	(238)
Accrued liabilities and deferred revenue	(368)
Total liabilities assumed	(606)
Net assets acquired	242

The intangible assets recognized, apart from goodwill, represented contractual or other legal rights of Falanx and those intangible assets of Falanx that could be clearly identified. These intangibles were identified and valued through interviews and analysis of data provided by Falanx concerning development projects, their stage of development, the time and resources needed to complete them, and if applicable, their expected income generating ability. There were no other contractual or other legal rights of Falanx clearly identifiable by management, other than those identified below. The allocation of the purchase price to the tangible and identifiable intangible assets acquired and liabilities assumed was as follows:

	Useful estimated life (years)	£000
Fair value of net assets acquired		242
Intangible assets acquired:		
Developed technology	3–5	4,267
Customer relationships	3	990
Deferred tax liability		(1,472)
Goodwill		9,383
Purchase price		13,410

If the acquisition of Falanx had occurred on 1 January 2006, net income for the Company in 2006 would have been £0.8 million lower than reported, including the additional amortization of intangibles.

During 2007, the provisional fair values of Falanx's accounts receivable and other creditors were finalized resulting in a reduction in net assets acquired of £17,000. As a result, goodwill increased by £17,000 during the year.

Soisic SA

On 30 October 2006, the Company purchased the entire share capital of Soisic SA (Soisic), a silicon-on-insulator (SOI) IP company incorporated in France for consideration of €5.1 million (£3.4 million), comprising €4.7 million cash consideration and €0.4 million of related acquisition expenses.

With this acquisition, the Company is making an investment in new technologies related to physical IP to enhance its leadership position in providing customers access to the higher performance and lower power offered by SOI process technologies. Soisic develops a similar set of products to the ARM Physical IP Division, specifically standard cells, static random access memory (SRAM) compilers and input/output (I/O) cells, however, based on SOI design rules and process models. Integrating this capability with ARM's widely-used physical IP opens the possibility for system-on-chip (SoC) designers to access SOI technology, which currently is used only in full custom designs, such as high-performance microprocessors.

The Company is investing in this area to be at the forefront of the design technologies needed to exploit the potential advantages of SOI as its usage grows in mobile, home and enterprise SoC and ASIC applications.

The purchase price was allocated to the tangible and intangible assets acquired and liabilities assumed on the basis of their estimated fair values on the acquisition date. A further €8 million was potentially payable on the achievement of various post-acquisition financial milestones and will be accrued when the milestones have been achieved, other than as noted below, whereby a small portion of this contingent consideration was accrued at acquisition.

The operating results for Soisic have been included in these financial statements for the period from 30 October 2006 to 31 December 2006 in the 2006 comparatives and for the entire year in 2007. The acquisition was accounted for under FAS 141.

6 Acquisitions continued

The following table sets out the provisional fair values of the assets acquired and liabilities assumed at the date of acquisition as reported in the 2006 annual report:

	Fair value to Company £000
Assets	
Accounts receivable, net	165
Other debtors	411
Deferred tax asset	1,392
Property and equipment, net	117
Total assets acquired	2,085
Liabilities	
Cash overdraft	(53)
Accounts payable and other creditors	(949)
Accrued liabilities	(413)
Total liabilities assumed	(1,415)
Net assets acquired	670

The intangible assets recognized represented those intangible assets of Soisic that could be clearly identified. These intangibles were identified and valued through interviews and analysis of data provided by Soisic concerning development projects, their stage of development, the time and resources needed to complete them, and if applicable, their expected income generating ability. There were no other contractual or other legal rights of Soisic clearly identifiable by management, other than those identified below. The allocation of the purchase price to the tangible and identifiable intangible assets acquired and liabilities assumed was as follows:

	Useful estimated life (years)	£000
Fair value of net assets acquired		670
Intangible assets acquired:		
Developed technology	5	4,283
Deferred tax liability		(1,413)
Purchase price		3,540

The purchase price above includes £0.1 million of contingent consideration. Whilst the Company does not normally accrue this payable until earned, in line with FAS 141 it has been accrued to reduce any potential negative goodwill to nil.

If the acquisition of Soisic had occurred on 1 January 2006, net income for the Company would have been £2.5 million lower than reported, including the additional amortization of intangibles.

During 2007, a proportion of the financial milestones were achieved resulting in €1.3 million (£0.9 million) consideration being accrued in addition to the amount accrued in 2006. There was a corresponding increase to goodwill as a result. Furthermore, the provisional fair values in respect of deferred tax were finalized resulting in an increase in net assets of £0.7 million and a corresponding reduction in goodwill. The net impact of these items resulted in an increase to goodwill of £0.2 million.

PowerEscape Inc.

On 21 June 2006, the Company purchased certain assets of PowerEscape Inc., a private company incorporated in the US, for total consideration of \$1.1 million (£0.6 million), comprising \$1.0 million cash consideration and \$0.1 million of related acquisition expenses.

The PowerEscape team, which has been integrated into the Company's Development System Division, will focus on adding innovative profiling and analysis features to the Company's portfolio of market-leading development tools.

The Company has allocated £595,000 of the purchase price to in-process research and development which reflects certain research projects that have not yet reached technological feasibility and commercial viability or had no alternative future use at the time of the acquisition. In-process research and development has been written-off immediately to the income statement.

Keil Elektronik GmbH and Keil Software Inc.

On 27 October 2005, the Company purchased the entire share capital of Keil Elektronik GmbH (KEG), a company incorporated in Germany for total consideration of \$10.9 million (£6.1 million), comprising \$10.4 million cash consideration and \$0.5 million of related acquisition expenses. On the same day, the Company purchased the entire share capital of Keil Software Inc. (KSI), a US company, for total consideration of \$5.2 million (£2.9 million), comprising \$5.0 million cash consideration and \$0.2 million of related acquisition expenses.

6 Acquisitions continued

Keil Elektronik GmbH and Keil Software Inc. continued

The Company has identified the MCU market as a critical growth area for the Company's future business and with this acquisition, the Company will be able to accelerate progress in that market by offering a more complete solution. As the MCU applications shift from 8/16-bit to 32-bit solutions, the combination of the ARM Cortex-M3 processor, which is ideally suited for microcontroller applications, the RealView high-performance compiler, and Keil's complementary MCU tools for ARM, will enable new generations of ARM MCU solutions.

The purchase price was allocated to the tangible and intangible assets acquired and liabilities assumed on the basis of their estimated fair values on the acquisition date. A further \$2.3 million for KEG and \$1.0 million for KSI was potentially payable on the achievement of various post-acquisition financial milestones. The financial milestones relating to the first year post-acquisition were achieved in 2006 and are accrued at the year end. Further potential payments relating to the second year post-acquisition will be accrued when payable. Keil is a leading independent provider of software development tools for the microcontroller (MCU) market.

The acquisition was accounted for under FAS 141. The operating results for Keil have been included in these financial statements for the period 27 October 2005 to 31 December 2005 in the 2005 comparatives and for the entire year in 2006 and 2007.

The following table sets out the provisional fair values of the assets acquired and liabilities assumed at the date of acquisition as reported in the 2005 annual report:

Fair value to Company	KEG £000	KSI £000
Assets		
Cash and cash equivalents	2,911	32
Accounts receivable, net	477	169
Inventories	60	36
Other debtors	11	5
Property and equipment, net	12	–
Total assets acquired	3,471	242
Liabilities		
Accounts payable and other creditors	(1,593)	(19)
Accrued liabilities and deferred revenue	(2,280)	(62)
Total liabilities assumed	(3,873)	(81)
Net (liabilities assumed)/assets acquired	(402)	161

The intangible assets recognized, apart from goodwill, represented contractual or other legal rights of Keil and those intangible assets of Keil that could be clearly identified. These intangibles were identified and valued through interviews and analysis of data provided by Keil concerning development projects, their stage of development, the time and resources needed to complete them, and if applicable, their expected income generating ability. There were no other contractual or other legal rights of Keil clearly identifiable by management, other than those identified below. The allocation of the purchase price to the tangible and identifiable intangible assets acquired and liabilities assumed was as follows:

	Useful estimated life (years)	KEG £000	KSI £000
Fair value of net (liabilities)/assets acquired		(402)	161
Intangible assets acquired:			
Customer relationships	2–3	4,290	482
Developed technology	1–5	2,744	–
Trade names	5	–	1,175
Deferred tax liability		(2,673)	(663)
Goodwill		2,178	1,764
Purchase price		6,137	2,919

KEG made a profit after tax for the year ended 31 December 2004 of £1.0 million and for the period from 1 January 2005 until acquisition a profit after tax of £1.0 million. KSI made a loss after tax for the year ended 31 December 2004 of £95,000 and for the period from 1 January 2005 until acquisition a loss after tax of £40,000. The results of the Company would not have been significantly different had the acquisition of KEG and KSI occurred on the 1 January 2005.

During 2006 and 2007, a further \$2.1 million and \$0.8 million consideration became payable for KEG and KSI respectively following the achievement of various post-acquisition financial milestones, with a corresponding increase to total consideration and goodwill. In addition in 2006, the provisional fair values in respect of KEG's income tax liabilities were finalized resulting in an increase in the net assets acquired by £1.1 million. Due to this change in fair value, an additional £1.1 million of consideration was paid. As both consideration and net assets were increased by the same amount, there was no corresponding change to goodwill.

7 Investments and marketable securities

	Listed investments £000	Unlisted investments £000	Total investments £000
Cost			
At 1 January 2007	1,714	1,970	3,684
Additions	–	2,657	2,657
Impairment	(236)	(926)	(1,162)
At 31 December 2007	1,478	3,701	5,179
Aggregate movements in fair value			
At 1 January 2007	171	–	171
Unrealized holding losses	(469)	–	(469)
At 31 December 2007	(298)	–	(298)
Carrying value			
At 31 December 2007	1,180	3,701	4,881
At 31 December 2006	1,885	1,970	3,855

Listed investments comprise an investment in Superscape Group plc, the fair value of which at 31 December 2007 is £1,180,000 (2006: £1,885,000; 2005: £3,474,000). In 2008, Superscape was acquired by Glu Mobile Inc. for 10 pence per share, and therefore the Company's investment has been impaired to this carrying value through the income statement, with the further reduction in carrying value to 7.98 pence per share at 31 December 2007 going through equity. In 2006, the Company disposed of its investment in CSR plc for £5.6 million resulting in a profit of £5.3 million that was recognised in the 2006 income statement. The fair value of this investment at 31 December 2005 was £3,521,000.

In 2007, the Company invested £2,534,000 in W&W Communications Inc. by way of a convertible loan note. This note earns interest at 10% per annum, and may convert into equity to a maximum investment of 14.99%. Also during 2007, an investment of £123,000 was made in Embest Info and Tech Inc., an unlisted company based in China. In 2005, the Company invested £274,000 in Luminary Micro Inc., an unlisted company, and made a further investment of £165,000 in the company in 2006.

At 31 December 2007, the Company had £1,582,000 (2006: £19,151,000; 2005: £8,835,000) of short-term marketable securities. These represent both the fair market value and amortized cost of these securities.

8 Property and equipment

	2006 £000	2007 £000
Owned buildings	190	190
Leasehold improvements	18,054	15,837
Computers	18,445	17,078
Software	8,457	8,491
Fixtures, fittings and motor vehicles	4,676	3,878
Assets under construction	–	758
	49,822	46,232
Less: accumulated depreciation	(35,852)	(34,190)
Property and equipment, net	13,970	12,042

Depreciation charged to income for the years ended 31 December 2005, 2006 and 2007 was £7,750,000, £6,895,000 and £7,236,000 respectively. The net book value of software at 31 December 2007 was £2,706,000 (2006: £3,674,000) with depreciation charged in 2007 on software of £1,744,000 (2006: 1,610,000; 2005: £1,851,000).

9 Intangible assets

	Goodwill £000	Patents £000	Licenses £000	Developed technology £000	Existing agreements and customer relationships £000	Core technology £000	Trademarks £000	Order backlog £000	Total £000
Cost									
At 1 January 2007	352,563	8,196	5,906	29,676	42,827	11,802	3,707	1,635	456,312
Additions	–	–	2,549	–	–	–	–	–	2,549
Additions (Falanx)	17	–	–	–	–	–	–	–	17
Additions (Soisic)	205	–	–	–	–	–	–	–	205
Additions (KEG)	588	–	–	–	–	–	–	–	588
Additions (KSI)	186	–	–	–	–	–	–	–	186
Exchange differences	(5,576)	–	–	84	(627)	(198)	(63)	(27)	(6,407)
At 31 December 2007	347,983	8,196	8,455	29,760	42,200	11,604	3,644	1,608	453,450
Aggregate amortization									
At 1 January 2007	3,320	8,151	5,327	10,595	15,661	4,771	1,582	1,635	51,042
Charge for the year	–	45	431	6,730	8,344	2,304	848	–	18,702
Exchange differences	–	–	–	(43)	(180)	(62)	(20)	(27)	(332)
At 31 December 2007	3,320	8,196	5,758	17,282	23,825	7,013	2,410	1,608	69,412
Net book value At 31 December 2007	344,663	–	2,697	12,478	18,375	4,591	1,234	–	384,038
At 31 December 2006	349,243	45	579	19,081	27,166	7,031	2,125	–	405,270

Amortization charged to income for the years ended 31 December 2005, 2006 and 2007 was £20,310,000, £18,917,000 and £18,702,000 respectively.

Licenses to use technology are being amortized over periods of three to ten years. The amortization periods for licenses have been determined according to their estimated useful economic life.

Patents are being amortized over four to five years, developed and core technology (the main IP of the company existent at acquisition and generating revenue) over five years and customer relationships (relationships with customers which were generating revenue at acquisition) over two to six years, being the periods over which the Company is expected to derive benefit from them.

The estimated amortization expense of intangible assets in each of the next five years is set forth below:

	£000
2008	17,609
2009	11,179
2010	7,885
2011	1,363
2012	255
Thereafter	1,084

In accordance with FAS 142, goodwill is no longer amortized, and is tested for impairment at least annually.

The split of goodwill by segment is shown below. Additions in the year relating to Keil and Falanx have been allocated to the Systems Design and Processor divisions respectively. Additions to Soisic have been allocated between the Processor and Physical IP divisions. The foreign exchange difference arises as goodwill on Artisan, Axys and KSI is denominated in US dollars and on Soisic in euros and thus is subject to revaluation at the period-end rates. Changes in the carrying amount for the year are as follows:

9 Intangible assets continued

	Processor Division £000	Physical IP Division £000	Systems Design Division £000	Total £000
Balance at 1 January 2007	109,096	227,361	12,786	349,243
Additions (KEG)	–	–	588	588
Additions (KSI)	–	–	186	186
Additions (Falanx)	17	–	–	17
Additions (Soisic)	–	205	–	205
Exchange differences	(1,635)	(3,810)	(131)	(5,576)
Balance at 31 December 2007	107,478	223,756	13,429	344,663

10 Accounts receivable

Included within accounts receivable at 31 December 2007 are £24.5 million (2006: £23.8 million) of amounts recoverable on contracts.

11 Accrued liabilities

Included within accrued liabilities at 31 December 2007 are £5.1 million (2006: £8.8 million) for staff costs, £7.0 million (2006: £5.6 million) of accrued employee vacation and sabbatical leave and £1.9 million (2006: £3.2 million) representing unpaid consideration for acquisitions.

12 Share-based compensation

The board is authorized to issue options to acquire ordinary shares in the Company and awards of shares in the Company up to a maximum of 10% of the issued ordinary share capital in any five-year period. The exercise of options or vesting of share awards will be satisfied either out of newly issued share capital, or from shares held by the Company as treasury stock or within the ESOP. Treasury stock is purchased from the market and the quantum and timing of these purchases is at the discretion of the directors, and based on the share price and short-term cash requirements of the Company.

Under the UK Inland Revenue Executive Approved Share Option Plan (the "Executive Scheme"), the Company may grant options to employees meeting certain eligibility requirements. Options under the Executive Scheme are exercisable between three and ten years after their issue, after which time the options expire.

Under the Company's Unapproved Scheme (the "Unapproved Scheme"), for which it has not sought approval from the UK tax authorities, options are exercisable one to seven years after their issue, after which time the options expire. The Company also operates the US ISO Scheme, which is substantially the same as the Unapproved Scheme, the main difference being that the options are exercisable one to five years after their issue. Under both of these schemes options are exercisable as follows: 25% maximum on first anniversary, 50% maximum on second anniversary, 75% maximum on third anniversary, 100% maximum on fourth anniversary. Various options to directors under the Unapproved Scheme have certain performance criteria attached, which if met are exercisable after three years, otherwise they will become exercisable after seven years.

There are further schemes for the Company's French and Belgian employees (the "French Scheme" and the "Belgian Scheme"). In the French Scheme, options are exercisable between four and seven years after their issue, whilst in the Belgian Scheme, options are exercisable from 1 January following the third anniversary after their issue, up to seven years from issue.

From 2006, the Company has begun issuing Restricted Stock Units (RSUs) to employees instead of options as approved at the 2006 AGM. RSUs are actual share awards on vesting rather than options to buy shares at a fixed exercise price. The main RSU awards (to employees in all jurisdictions other than France) vest similarly to the unapproved scheme above, namely 25% on each anniversary over four years. RSU awards to the Company's French employees vest 50% after two years, and then a further 25% after three and four years. Whilst the Company reserves the right to award options to employees going forward, the majority of awards to employees will be in RSUs.

Additionally from 2006, the Company introduced the Deferred Annual Bonus plan (DAB). Under the DAB, which is for directors and selected senior management within the Company, participants are required to defer 50% of any related annual bonus into shares on a compulsory basis. These shares will be deferred for three years, and then a further matching award will be made depending on the achievement of an EPS performance condition over that time. The Company also operates the Long Term Incentive Plan (LTIP), also for directors and selected senior management, whereby share awards are made and vest depending on the Company's TSR performance compared to two comparator groups over the three-year performance period.

Upon the acquisition of Artisan in 2004, the Company assumed the share schemes of Artisan existing at acquisition. The schemes remained substantially the same as prior to the acquisition, other than the options became options to purchase shares in ARM Holdings plc instead of Artisan Components Inc. The number and value of options were amended in line with the conversion ratio as detailed in the merger agreement. The schemes assumed were the "1993 Plan", the "1997 Plan", the "2000 Plan", the "2003 Plan", the "Director Plan", the "Executive Plan" and the "ND00 Plan".

12 Share-based compensation continued

Under each plan, there are multiple vesting templates and vesting periods. The majority of the options were already vested upon acquisition, and the most common template was 25% vesting after one year, and then 6.25% vesting each quarter thereafter, until 100% vest after four years. Some options vest on a monthly basis, and some vest over five years. All options lapse ten years from the date of grant.

In 1998, the Company set up two savings-related share option schemes for all employees and executive directors of the Company. The number of options granted is related to the value of savings made by the employee. The period of savings is three or five years except for employees of ARM Inc. where the period is two years. The option price for grants made in 2007 is set at 80% of the market share price prior to the grant (and for grants made in 2006 and before set at 85%), and the right to exercise normally only arises for a six-month period once the savings have been completed except for ARM Inc. where the right to exercise normally only arises for a three-month period once the savings have been completed. The Company set up further savings-related option schemes in each year up to and including 2006 for all employees and executive directors of the Company, which have the same characteristics as those schemes set up in 1998. In 2007, a further scheme was created for non-US employees.

In 2007, the Company commenced a new savings-related option scheme for US employees, namely the Employee Share Purchase Plan (ESPP). The number of options granted is related to the value of savings made by the employee. The period of savings is six months, with the option price being at 85% of the lower of the market share price at the beginning and end of the scheme.

Activity under all share schemes is detailed below, including weighted average exercise prices for share options and weighted average grant-date fair values for share awards:

	Outstanding options		Outstanding RSUs/ LTIP/DAB awards	
	Options Number	Weighted average exercise price £	Awards Number	Weighted average grant-date fair value £
Balances, 31 December 2004	164,019,815	0.870	5,003,724	0.909
Granted in year	27,127,630	1.051	3,543,455	1.165
Lapsed in year	(11,027,172)	1.110	(786,298)	0.987
Exercised in year	(37,096,283)	0.374	–	–
Balances, 31 December 2005	143,023,990	1.014	7,760,881	1.018
Granted in year	9,064,290	1.250	10,589,718	1.310
Additional awards earned based on performance conditions	–	–	1,672,009	0.805
Lapsed in year	(9,508,283)	1.697	(558,985)	1.255
Options exercised/awards vested in year	(30,656,261)	0.583	(3,798,567)	0.805
Balances, 31 December 2006	111,923,736	1.093	15,665,056	1.236
Granted in year	1,065,813	1.104	12,742,465	1.264
Lapsed in year	(6,909,858)	3.026	(3,604,445)	1.099
Options exercised/awards vested in year	(30,850,202)	0.612	(2,119,532)	1.313
Balances, 31 December 2007	75,229,489	1.113	22,683,544	1.266

The total number of options exercisable at 31 December 2007 was 55,652,780 (2006: 74,533,736; 2005: 64,431,089).

The Company uses the historical price of the Company's stock for the expected volatility assumption, including some adjustments for non-recurring one-time events, consistent with the guidance in FAS 123R and the Securities and Exchange Commission's Staff Accounting Bulletin No. 107. Adjustments were made as the Company's assessment of future stock price trends were more representative of historical data excluding these events rather than including them. The expected life of options is based on known vesting dates and historical exercise patterns for the different schemes. The risk-free interest rate is based on observed interest rates appropriate for the terms of the share options. The dividend yield assumption is based on the Company's last declared dividend and expected payouts.

The fair value of the Company's restricted stock units and LTIP awards is based on the share price at date of grant, discounted for any dividends that will not be earned during the vesting period.

12 Share-based compensation continued

The fair values per share of share options granted have been estimated with the following weighted average assumptions:

	Options			RSUs/LTIP awards		
	2005	2006	2007	2005	2006	2007
Expected life (in years)	3.07	3.11	3.43	3.00	2.57	2.65
Volatility	50%	40%	34%	50%	40%	33%
Risk-free interest rate	4.00%	4.01%	5.50%	4.00%	4.13%	5.28%
Dividend yield	0.70%	0.70%	1.45%	0.70%	0.70%	0.75%
Weighted average fair value (£)	0.38	0.43	0.52	1.17	1.31	1.26

All of the options granted in 2007 were options within the SAYE scheme which have an exercise price that was 80% of the market price at date of grant (as noted above). The weighted average grant-date fair value of these SAYE options granted during 2007 was £0.52 (2006: £0.44; 2005: £0.40). The weighted-average exercise price of these SAYE options granted during 2007 was £1.104 (2006: £1.0264; 2005: £0.9095).

The following table presents details of the total stock-based compensation expense that is included in each functional line item of the Company's consolidated statements of income for the years ended 31 December. Note that the 2005 comparative income statement has been re-analyzed to absorb the stock-based compensation expenses into the functional line items rather than as a separate line as reported in the income statements in that year.

	2005* £000	2006 £000	2007 £000
Cost of revenues	2,489	1,098	959
Research and development costs	1,582	10,609	9,268
Sales and marketing costs	2,132	3,658	3,196
General and administrative costs	3,524	2,927	2,556
Cumulative effect of change in accounting policy	–	3,496**	–
Share-based payment expense	9,727	21,788	15,979
Tax benefit for share-based payment compensation expense	(1,799)	(4,181)**	(4,246)
Share-based payment expense, net of tax	7,928	17,607	11,733

* The amounts included in 2006 and 2007 reflect the adoption of FAS 123R. In accordance with the modified prospective transition method, the Company's consolidated statements of income for 2005 have not been restated to reflect, and do not include, the impact of FAS 123R.

** The cumulative effect of change in accounting policy arises as a re-measurement adjustment for liability-classified awards on cumulative share-based compensation for earlier years on adoption of FAS 123R. Included within tax benefits above is £1,049,000 relating to this cumulative effect of change in accounting policy.

The adoption of FAS 123R will continue to have a significant adverse impact on the Company's reported results of operations, although it should not have a material impact on its overall financial position. The amount of unearned stock-based compensation currently estimated to be expensed in the period from 2008 to 2012 related to unvested share-based payment awards at 31 December 2007 is £16.3 million (2006: £19.5 million). Of this amount, £9.7 million is estimated to be expensed in 2008, £4.9 million in 2009, £1.5 million in 2010 and £0.2 million in 2011. The weighted average period over which the unearned share-based compensation is expected to be recognised is approximately 1.0 years. If there are any cancellations or accelerated vestings, the Company may be required to accelerate or cancel some of the remaining compensation expense. The share-based compensation expense in future periods will be more than stated above to the extent that the Company grants additional options or awards after the balance sheet date. Furthermore, the estimated future compensation charge may be affected by any change to the fair value of liability-classified awards.

In accordance with the requirements of the disclosure-only alternative of FAS 123, the following table illustrates the effect on net income and earnings per share for 2005 had the Company applied the fair value recognition provisions of FAS 123 instead of the guidelines provided by APB 25.

12 Share-based compensation continued

	2005 £000
Net income:	
As reported	41,880
Deduct: Total stock-based compensation expense determined under fair value-based method for all awards, net of related tax effects	(20,120)
Add back: Total stock-based compensation expense determined under the intrinsic value-based method for all awards, net of related tax effects	7,928
Pro forma net income	29,688
Basic earnings per common share (pence):	
As reported	3.1p
Pro forma	2.2p
Diluted earnings per common share (pence):	
As reported	2.9p
Pro forma	2.1p

The total pre-tax intrinsic value of options exercised and share awards (LTIP, RSU and DAB) made in 2007 was £23.8 million (2006: £21.6 million) and £2.9 million (2006: £5.2 million) respectively. This intrinsic value represents the difference between the fair market value of the Company's shares on the date of exercise and the exercise price of each option. The total fair value of LTIP awards that vested in 2006 was £1.7 million; no LTIP awards vested in 2007 as all lapsed. The total fair value of RSU and DAB awards that vested in 2007 was £2.8 million (2006: nil vested). Based on the closing price of the Company's shares on 31 December 2007 of £1.24 per share, the total pre-tax intrinsic value of all outstanding options, RSUs, LTIP and DAB awards was £54.0 million (2006: closing price of £1.2575, total pre-tax intrinsic value of £67.3 million). The total pre-tax intrinsic value of all exercisable options at 31 December 2007 was £22.5 million (2006: £39.2 million).

The total cash received on the exercise of options in 2007 was £18.9 million (2006: £17.9 million). The total tax benefits realized from the exercise of options and share awards in the year was £8.9 million (2006: £9.0 million).

The following options over ordinary shares were in existence at 31 December:

Exercise price (£)	Options outstanding			Options exercisable		
	Number outstanding	Weighted average remaining life (years)	Weighted average exercise price (£)	Number outstanding	Weighted average remaining life (years)	Weighted average exercise price (£)
0.1125 – 0.45	14,608,232	3.11	0.32	14,608,232	3.11	0.32
0.46 – 0.9475	14,142,469	5.48	0.63	11,637,194	5.78	0.60
1.005 – 1.055	18,110,574	3.56	1.05	8,301,003	3.47	1.05
1.0575 – 1.25	13,713,481	2.95	1.23	11,441,370	2.83	1.24
1.325 – 7.738	14,654,733	2.78	2.34	9,664,981	1.69	2.87
Total	75,229,489	3.57	1.11	55,652,780	3.42	1.12

Exercise price (£)	Options outstanding			Options exercisable		
	Number outstanding	Weighted average remaining life (years)	Weighted average exercise price (£)	Number outstanding	Weighted average remaining life (years)	Weighted average exercise price (£)
0.026 – 0.40	15,662,942	4.24	0.25	15,662,942	4.24	0.25
0.405 – 0.50	21,310,841	4.13	0.45	19,649,705	4.01	0.45
0.51 – 0.9475	17,465,042	5.96	0.71	9,678,857	6.48	0.66
1.005 – 1.224	25,943,761	4.37	1.07	9,884,878	4.03	1.09
1.25 – 7.738	31,541,150	3.52	2.18	19,657,354	2.55	2.72
Total	111,923,736	4.31	1.09	74,533,736	4.00	1.12

There were also 13,845,565 RSUs, 7,943,979 LTIP and 894,000 DAB awards outstanding at 31 December 2007 (2006: 7,893,640 RSUs and 7,771,416 LTIP awards) with a weighted average remaining life of 1.43 years (2006: 1.51 years). RSUs, LTIP and DAB awards have no exercise price and all were unvested at 31 December 2007.

13 Commitments and contingencies

The Company leases its office facilities (which expire at various dates through 2018) and certain equipment (including EDA design tools which expire at various dates through 2012) under non-cancelable operating lease agreements.

Future minimum lease commitments at 31 December 2007, are as follows:

Years ending 31 December	Operating leases £000
2008	18,351
2009	16,423
2010	16,062
2011	11,522
2012	4,550
Thereafter	7,115
Total minimum lease payments	74,023

Rental expense under operating leases totalled £15,809,000, £18,800,000 and £17,558,000 for the years ended 31 December 2005, 2006 and 2007 respectively.

Nazomi In May 2002, Nazomi Communications, Inc. (Nazomi) filed suit against ARM alleging willful infringement of US Patent No. 6,332,215. ARM answered the complaint in July 2002 denying infringement. Following an original ruling in ARM's favour, Nazomi appealed and received a supplementary "Markman" hearing in 2005 that resulted in a decision that supported the original ruling. On 13 February 2007, Nazomi again appealed and, on 21 February 2008 the Court of Appeals for the Federal Circuit upheld the District Court's claim construction and affirmed the District Court's grant of summary judgment in favour of ARM. The period for any further appeal by Nazomi has now passed and accordingly this litigation is now concluded with judgment in favour of ARM.

Technology Properties Limited, Inc. In October 2005, Technology Properties Limited, Inc. (TPL) filed suit, in the United States District Court for the Eastern District of Texas (Marshall Division), against certain companies in the Fujitsu, Matsushita, NEC and Toshiba groups of companies alleging infringement of TPL's US Patents Nos. 5,809,336; 5,784,584 and 6,598,148 (the "Litigation"). All of the defendants are licensees of various ARM technologies. It was revealed as part of the preliminary infringement contentions in the Litigation, filed in July 2006, that certain ARM technology is alleged to infringe a single claim in US Patent No 5,784,584 (the "'584 Patent"). In September 2006, ARM filed a motion to intervene in the Litigation and that motion has been granted. ARM is now a defendant party in the Litigation. The claim construction (or "Markman") hearing took place in May 2007. Based on the claim construction delivered by the District Court, TPL filed a motion stipulating that the accused ARM technology does not infringe the '584 Patent with a request that final judgment be entered to that effect. TPL subsequently filed notice to appeal the claim construction to the Court of Appeals for the Federal Circuit. Based on independent legal advice, ARM is confident that the Court of Appeals will uphold the claim construction ruling delivered by the District Court.

ARM does not expect any significant liability in respect of these claims.

Guarantees It is common industry practice for licensors of technology to offer to indemnify their licensees for loss suffered by the licensee in the event that the technology licensed is held to infringe the intellectual property of a third party. Consistent with such practice, the Company provides such indemnification to its licensees but subject, in all cases, to a limitation of liability. The obligation for the Company to indemnify its licensees is subject to certain provisos and is usually contingent upon a third party bringing an action against the licensee alleging that the technology licensed by the Company to the licensee infringes such third party's intellectual property rights. The indemnification obligations typically survive any termination of the license and will continue in perpetuity.

The Company does not provide for any such guarantees unless it has received notification from the other party that they are likely to invoke the guarantee. The provision is made if both of the following conditions are met: (i) information available prior to the issuance of the financial statements indicates that it is probable that a liability had been incurred at the date of the financial statements; and (ii) the amount of the liability can be reasonably estimated. Any such provision is based upon the directors' estimate of the expected costs of any such claim.

There was no provision for such guarantees at either 31 December 2007 or 31 December 2006.

13 Commitments and contingencies continued

At 31 December 2007, ARM had provided in aggregate £nil (2006: £1.1 million) in relation to claims, being the expected future costs to be incurred.

At 31 December 2007, the Company had outstanding capital commitments of £276,000 (2006: £525,000).

14 Geographic and segment information

At 31 December 2007, the Company is organized on a worldwide basis into three business segments, namely the Processor Division (PD), the Physical IP Division (PIPD) and the Systems Design Division (SDD). In 2004, the directors were of the opinion the Company only had one class of business, and then following the acquisition of Artisan in December 2004, the Company had two reportable segments in 2005 (namely PD and PIPD).

This was based upon the Company's internal organisation and management structure and was the primary way in which the Chief Operating Decision Maker (CODM) and the rest of the board were provided with financial information. Whilst revenues were reported into four main revenue streams (namely licensing, royalties, development systems and services), the costs, operating results and balance sheets were only analyzed into the two segments.

In 2006, this structure and system of internal financial reporting to the CODM and board was changed resulting in a third division, namely SDD (called DevSys in 2006, now SDD), becoming a separate reportable segment. In previous years, the results of SDD were reported within PD, but for ease of comparability, have been separated out in the comparatives below. PIPD consists of the business stream previously undertaken by Artisan. PD primarily comprises the legacy ARM products and services. Recent acquisitions have been allocated to the various divisions as follows: KEG and KSI in 2005 to SDD, Falanx in 2006 to PD and Soisic in 2006 to PIPD. Goodwill on each acquisition has also been allocated into these divisions, except for Artisan whereby this has been allocated between PD and PIPD.

The following analysis is of revenues, operating costs, interest income, income before income tax, depreciation and amortization, capital expenditure, total assets and liabilities, net assets and goodwill of each segment and of the Company in total:

Year ended 31 December 2007	Processor Division £000	Physical IP Division £000	Systems Design Division £000	Unallocated £000	Group £000
Segmental income statement					
Revenue	187,829	43,418	27,913	–	259,160
Operating costs	(112,579)	(61,765)	(42,218)	240	(216,322)
Interest, net	–	–	–	5,402	5,402
Income/(loss) before tax	75,250	(18,347)	(14,305)	5,642	48,240
Segmental balance sheet					
Total assets	171,887	278,346	33,517	72,915	556,665
Total liabilities	(33,173)	(13,303)	(10,587)	(5,862)	(62,925)
Net assets	138,714	265,043	22,930	67,053	493,740
Other segmental items					
Depreciation and amortisation	5,411	16,292	4,236	–	25,939
Capital expenditure	3,161	1,336	947	–	5,444
Goodwill	107,478	223,756	13,429	–	344,663
Year ended 31 December 2006					
Segmental income statement					
Revenue	180,426	53,996	28,832	–	263,254
Operating costs	(115,196)	(66,593)	(40,967)	4,522	(218,234)
Interest, net	–	–	–	6,758	6,758
Profit on disposal of available-for-sale investment	–	–	–	5,270	5,270
Income/(loss) before tax	65,230	(12,597)	(12,135)	16,550	57,048
Segmental balance sheet					
Total assets	171,085	300,851	33,614	147,153	652,703
Total liabilities	(37,308)	(19,589)	(10,843)	(10,316)	(78,056)
Net assets	133,777	281,262	22,771	136,837	574,647
Other segmental items					
Cumulative effect of change in accounting policy	(2,028)	(979)	(489)	–	(3,496)
Depreciation and amortisation	4,678	16,352	5,377	–	26,407
Capital expenditure	4,077	2,368	2,114	–	8,559
Goodwill	109,096	227,361	12,786	–	349,243

14 Geographic and segment information continued

Year ended 31 December 2005	Processor Division £000	Physical IP Division £000	Systems Design Division £000	Unallocated £000	Group £000
Segmental income statement					
Revenue	156,641	50,159	25,639	–	232,439
Operating costs	(87,357)	(64,012)	(30,868)	(2,285)	(184,522)
Interest, net	–	–	–	5,317	5,317
Income/(loss) before tax	69,284	(13,853)	(5,229)	3,032	53,234
Segmental balance sheet					
Total assets	161,885	349,769	36,068	168,371	716,093
Total liabilities	(22,226)	(20,115)	(12,168)	(12,534)	(67,043)
Net assets	139,659	329,654	23,900	155,837	649,050
Other segmental items					
Depreciation and amortisation	6,632	18,245	3,518	–	28,395
Capital expenditure	2,737	1,584	1,743	–	6,064
Goodwill	113,358	259,197	13,017	–	385,572

Unallocated operating costs are foreign exchange revaluation on monetary items, including cash and cash equivalents. Unallocated assets and liabilities include cash and cash equivalents, short-term investments and marketable securities, some deferred tax balances, current tax and VAT. There are no inter-segment revenues. The results of each segment have been prepared using consistent accounting policies with those of the Company as a whole.

The following analysis is of revenues by geographic segment and origin and long-lived assets, excluding deferred tax assets, by Group companies in each territory:

	Year ended 31 December		
	2005 £000	2006 £000	2007 £000
Revenues (by market destination):			
Europe	32,971	42,746	42,654
North America	99,727	111,194	109,895
Japan	42,270	40,303	41,868
Asia Pacific excluding Japan	57,471	69,011	64,743
Total revenues	232,439	263,254	259,160

The Company's exports from the UK were £172,592,000, £195,868,000 and £216,976,000 for the years ended 31 December 2005, 2006 and 2007 respectively.

	Year ended 31 December		
	2005 £000	2006 £000	2007 £000
Revenues (by origin):			
Europe	170,505	198,386	215,371
United States	59,183	63,028	42,115
Asia Pacific	2,751	1,840	1,674
Total revenues	232,439	263,254	259,160

	Year ended 31 December	
	2006 £000	2007 £000
Long-lived assets (excluding deferred tax assets):		
Europe	13,045	11,025
United States	3,614	2,827
Asia Pacific	1,166	1,891
Total long-lived assets	17,825	15,743

In 2007, 2006 and 2005, no single customer accounted for more than 10% of total revenues.

15 Fair values of financial instruments

The following methods and assumptions were used to estimate the fair value of each class of financial instrument for which it is practicable to estimate that value:

Cash and cash equivalents, short-term investments and accounts receivable The carrying amount approximates fair value because of the short maturity of those instruments.

Marketable securities The carrying amount approximates fair value because these instruments are marked-to-market.

Foreign currency contracts and embedded derivatives The fair value of foreign currency contracts and embedded derivatives is estimated using the settlement rates prevailing at the period end. The fair value of foreign exchange option contracts is derived using the Black-Scholes valuation model and includes the balance sheet spot rate, currency volatility and respective interest rate curves for the different currencies as inputs to this model.

Short-term debt During the year, the Company entered into a £100 million revolving credit facility providing the Company access to funds for any corporate purpose. Whilst the Company did make various drawdowns totalling £30 million on this facility during the year, these had been fully repaid and the facility was undrawn at the balance sheet date. Any drawn amounts accrue interest at a LIBOR-plus rate whilst there is a nominal charge for the undrawn portion. Furthermore, the facility requires the Company to adhere to various financial covenants relating to EBITDA multiples and interest cover; the Company adhered to all covenants during the year.

The estimated fair values of the Company's financial instruments are as follows:

	At 31 December			
	2006 Carrying amount £000	Fair value £000	2007 Carrying amount £000	Fair value £000
Cash and cash equivalents	90,743	90,743	49,509	49,509
Short-term investments	18,600	18,600	232	232
Marketable securities	19,151	19,151	1,582	1,582
Accounts receivable	69,552	69,552	68,232	68,232
Foreign currency contracts	439	439	(496)	(496)
Embedded derivatives	(1,620)	(1,620)	(220)	(220)
Short-term debt	–	–	–	–

16 Valuation and qualifying accounts

	Balance at 1 January £000	Charged/ (credited) to income statement £000	Acquired with subsidiary undertaking £000	Utilized/ Reclassific- ation £000	Foreign exchange £000	Balance at 31 December £000
2007 – allowance for doubtful debts	2,556	215	–	(1,253)	(14)	1,504
2006 – allowance for doubtful debts	2,173	932	–	(377)	(172)	2,556
2005 – allowance for doubtful debts	1,451	547	27	–	148	2,173
2007 – valuation allowance against deferred tax assets	6,049	4,824	(749)	(533)	(17)	9,574
2006 – valuation allowance against deferred tax assets	366	3,394	2,289	–	–	6,049
2005 – valuation allowance against deferred tax assets	254	112	–	–	–	366

17 Post balance sheet events

At the 2008 Annual General Meeting of the Company, a final dividend of 1.2 pence per share (total cost £15.3 million) will be proposed in respect of the 2007 financial year, and if approved will be paid on 21 May 2008 to shareholders on the register on 2 May 2008.

To the board of directors and members of ARM Holdings plc

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income, consolidated statements of comprehensive income, consolidated statements of cash flows and consolidated statements of changes in shareholders' equity present fairly, in all material respects, the financial position of ARM Holdings plc and its subsidiaries at 31 December 2007 and 2006, and the results of their operations and their cash flows for each of the three years in the period ended 31 December 2007 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in footnote 1 to the consolidated financial statements, the Company changed the manner in which it accounts for uncertain tax positions and the costs related to employees' sabbatical leave in 2007. Also as discussed in footnote 1, in 2006, the Company changed the manner in which it accounts for share-based compensation.

A handwritten signature in blue ink that reads "PricewaterhouseCoopers LLP". The signature is written in a cursive, flowing style.

PricewaterhouseCoopers LLP Chartered Accountants

London, United Kingdom

3 April 2008

Company balance sheet/UK GAAP

As at 31 December

	Notes	2007 £000	2006 £000
Fixed assets			
Investments	4	529,276	512,490
Current assets			
Debtors	5	61	10,039
Cash at bank and in hand		128	123
		189	10,162
Creditors: amounts falling due within one year	6	(66,348)	(96,429)
Net current liabilities		(66,159)	(86,267)
Total assets less current liabilities		463,117	426,223
Net assets		463,117	426,223
Capital and reserves			
Called-up share capital	7	672	695
Share premium account	8	–	97,616
Option reserve	8	61,474	61,474
Other reserve	8	–	267,418
Profit and loss account	8	400,971	(980)
Equity shareholders' funds	9	463,117	426,223

The financial statements on pages 134 to 141 were approved by the board of directors on 3 April 2008 and were signed on its behalf by:



Doug Dunn
Director

1 Principal accounting policies

The financial statements have been prepared in accordance with the Companies Act 1985 and applicable Accounting Standards in the UK. A summary of the more important accounting policies, which have been consistently applied and reviewed by the board of directors in accordance with Financial Reporting Standard (FRS) 18, "Accounting policies", is set out below:

Basis of accounting The financial statements are prepared in accordance with the historical cost convention, as modified for fair value in relation to share-based payments.

Investments in subsidiaries Investments in subsidiaries are initially recorded at cost. Where an acquisition satisfies the provisions of sections 131 to 134 of the Companies Act 1985 for merger relief, the investment is stated at the nominal value of shares issued plus the fair value of any other consideration.

Cash flow statement The Company has taken advantage of the exemption in FRS 1 Revised 1996 "Cash flow statements" which provides that where a company is a member of a group and a consolidated cash flow statement is published, the company does not have to prepare a cash flow statement.

Foreign currency Transactions denominated in foreign currencies have been translated into sterling at actual rates of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies have been translated at rates ruling at the balance sheet date. Exchange differences have been included in operating profit.

Taxation Current tax is provided at amounts expected to be paid using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Financial instruments The Company does not have any financial instruments, other than intercompany payables and receivables and cash. Due to the short-term nature of these balances, the Company considers the fair value of these items to equal the carrying value. Because the Company is included in the consolidated financial statements of the ARM Holdings plc group which are publicly available, and the financial disclosures required by FRS 29 are in those financial statements, no disclosure has been presented in these financial statements.

Share schemes The Group's Employee Share Ownership Plan (ESOP) is a separately administered trust which is funded by loans from the group, and the assets of which comprise shares in the Company. In accordance with UITF 38, "Accounting for ESOP Trusts", the Company recognises the assets and liabilities of the ESOP in its own accounts and shares held by the trust are recorded at cost as a deduction in arriving at shareholders' funds until such time as the shares vest unconditionally to employees.

The Company issues equity-settled share-based payments, including an LTIP, to certain employees of subsidiary undertakings. In accordance with FRS 20, equity-settled share-based payments are measured at fair value at the date of grant. Fair value is measured by use of the Black-Scholes pricing model. The fair value determined at the grant date of the equity-settled share-based payments is expensed in the accounts of the subsidiary companies on a straight-line basis over the vesting period, based on the Company's estimate of the number of shares that will eventually vest.

The Company operates Save As You Earn (SAYE) schemes in the UK and an Employee Share Purchase Plan (ESPP) in the US. Options under the SAYE scheme granted in 2007 was at a 20% discount to market price of the underlying shares on the date of grant, whereas for all prior years was at a 15% discount. The UK SAYE schemes are approved by the Inland Revenue, which stipulates that the saving period must be at least 36 months.

The Company has taken advantage of the exemption available, and has applied the provisions of FRS 20 only to those options granted after 7 November 2002 and which were outstanding at 31 December 2004. The Company does not have any employees and as such, in accordance with UITF 44, all share-based compensation has been recorded as capital contributions to subsidiaries.

Treasury shares The Company has a share buyback programme under which the Company purchases its own shares and holds them as treasury shares. These shares will be used to satisfy employee share option exercises and other share awards. In accordance with UITF 38, the Company recognises these shares at cost as a deduction in arriving at shareholders' funds.

2 Profit for the financial year

As permitted by Section 230 of the Companies Act 1985, the parent company's profit and loss account has not been included in these financial statements. The parent company's profit after taxation, including dividends receivable and before dividends payable was £148,324,000 (2006: £6,741,000). Apart from six directors who have contracts of service with ARM Limited, the Company has no employees. All emoluments of these directors are paid by ARM Limited and are disclosed in the remuneration report within these financial statements.

3 Dividends paid and proposed

	2007 £000	2006 £000
Final dividend paid of 0.6 pence per ordinary share in respect of 2006 (2006: 0.5 pence in respect of 2005)	8,013	6,918
Interim dividend paid of 0.8 pence (2006: 0.4 pence) per ordinary share	10,534	5,449
	18,547	12,367

The ESOP trust has waived its right to receive dividends of over 0.01 pence per share. As such, dividends will not be payable on the 1,201,434 shares currently held within the ESOP. Also, 65,201,176 shares were held as treasury stock by ARM Holdings plc at 31 December 2007 and the Company will waive its right to dividends on these shares.

The directors have recommended the payment of a final dividend of 1.2 pence per share in respect of 2007 (total cost of £15.3 million), bringing the total dividend payable in respect of 2007 (including the interim of 0.8 pence per share) to 2.0 pence per share. This will be paid to shareholders after approval by the shareholders at the 2008 AGM.

4 Fixed asset investments

The cost and net book value of interests in Group undertakings held by the Company was £529,276,000 at 31 December 2007 and £512,490,000 at 31 December 2006. The Company took advantage of merger relief in 2004 and did not record the premium on the issue of shares for the acquisition of Artisan Components Inc. (now ARM Inc.) and thus did not record the premium within the value of the investment in the company balance sheet at that time.

	Investments in subsidiary undertakings £000
Cost and net book value	
At 1 January 2007	512,490
Capital contributions arising from FRS 20 charges	16,786
At 31 December 2007	529,276

Where options over the Company's shares have been issued to the employees of subsidiary undertakings, the fair value of employee services performed (equal to the FRS 20 charge) has been recorded as a capital contribution.

Interests in Group undertakings Details of subsidiary undertakings are as follows:

Name of undertaking	Country of registration	Description of shares held	Proportion of nominal value of issued shares held
ARM Limited	England and Wales	Ordinary £1 shares	less than 0.01%
ARM Finance UK Limited	England and Wales	Ordinary \$1 shares	100%

The principal activity of ARM Limited is the marketing, research and development of RISC-based microprocessors. The remaining shares in ARM Limited were held at the balance sheet date by ARM Finance UK Limited (AFL) and ARM Finance UK Two Limited (AFL2) (with AFL2 itself being a wholly owned subsidiary of AFL). The principal activities of both ARM Finance UK Limited and ARM Finance UK Two Limited are as intermediate holding companies.

Nominees of the Company hold 100% of the ordinary share capital of ARM Employee Benefit Trustee Ltd, a company which acts as trustee to the Group's ESOP.

5 Debtors

	2007 £000	2006 £000
Amounts owed from Group undertakings	–	10,014
Corporation tax	–	25
Prepayments and accrued income	61	–
	61	10,039

6 Creditors: amounts falling due within one year

	2007 £000	2006 £000
Amounts owed to Group undertakings	65,864	96,058
Accruals and deferred income	484	371
	66,348	96,429

7 Called-up share capital

	2007 £000	2006 £000
Authorised		
2,200,000,000 ordinary shares of 0.05 pence each (2006: 2,200,000,000)	1,100	1,100
Allotted, called-up and fully paid		
1,344,055,696 ordinary shares of 0.05 pence each (2006: 1,389,907,834)	672	695

9,866,862 ordinary shares of 0.05 pence each were issued in the year for cash consideration of £5,509,000 as a result of the exercise of employee share options at various times during the year. 55,719,000 ordinary shares were cancelled in the year through Court application and approval at the 2007 AGM.

Share options and awards The Company had the following options and awards outstanding over ordinary shares of 0.05 pence at 31 December 2007:

	Year of grant	Number of options	Range of exercise prices £	Weighted average exercise price £	Latest date of exercise
Executive Scheme	1998	160,000	0.1125	0.1125	6 March 2008
	1999	1,368,817	1.224 – 4.26	1.3704	15 November 2009
	2000	355,329	6.136 – 7.738	6.5486	21 May 2010
	2001	512,670	2.84 – 3.75	3.3914	5 November 2011
	2002	807,835	2.465	2.465	18 April 2012
	2003	551,055	0.4375	0.4375	29 January 2013
	2004	538,915	1.25	1.25	29 January 2014
	2005	584,960	1.055	1.055	3 February 2015
		4,879,581		1.9433	
Unapproved Scheme	2001	2,880,265	2.84 – 4.43	3.4707	5 November 2008
	2002	3,234,340	0.425 – 3.145	2.3984	7 November 2009
	2003	3,430,303	0.4375 – 1.1475	0.4559	4 November 2010
	2004	6,573,342	0.9475 – 1.25	1.2343	21 October 2011
	2005	8,302,183	1.005 – 1.185	1.0609	30 October 2012
	2006	2,551,598	1.16 – 1.36	1.3224	19 November 2013
		26,972,031		1.4687	
Unapproved Performance Scheme	2001	62,909	3.815	3.815	22 May 2008
	2002	630,411	2.1475 – 2.465	2.3524	27 May 2009
	2003	731,428	0.4375	0.4375	30 January 2010
	2004	1,616,000	1.25	1.25	30 January 2011
	2005	2,620,853	1.055	1.055	4 February 2012
	2006	2,445,284	1.325	1.325	1 February 2013
		8,106,885		1.2419	
US ISO Scheme	2003	132,000	0.4375 – 1.1475	0.4579	4 November 2008
	2004	1,466,364	0.9475 – 1.25	1.2207	21 October 2009
	2005	4,392,447	1.005 – 1.185	1.0592	30 October 2010
	2006	833,807	1.1875 – 1.36	1.3257	31 August 2011
		6,824,618		1.1148	
French Scheme	2001	124,500	3.35 – 4.43	3.4962	5 November 2008
	2002	134,250	1.505 – 3.145	2.4799	14 August 2009
	2003	31,250	0.4375 – 1.1475	0.5113	4 November 2010
	2004	344,504	0.9475 – 1.25	1.2407	21 October 2011
	2005	424,386	1.0425 – 1.185	1.0603	30 October 2012
	2006	98,250	1.325 – 1.36	1.3297	3 May 2013
		1,157,140		1.5488	

7 Called-up share capital continued

	Year of grant	Number of options	Range of exercise prices £	Weighted average exercise price £	Latest date of exercise
Belgian Scheme	2003	85,600	1.1475	1.1475	4 November 2010
	2004	353,700	1.25	1.25	29 January 2011
	2005	331,200	1.055	1.055	3 February 2012
	2006	22,500	1.1875 – 1.325	1.2944	31 August 2013
		793,000		1.1588	
1993 Plan	1998	107,894	0.15	0.15	17 December 2008
	1999	293,444	0.16 – 0.28	0.2047	15 November 2009
	2000	900,386	0.25 – 0.58	0.3538	30 October 2010
	2001	2,215,534	0.24 – 0.46	0.2535	30 December 2011
	2002	2,410,826	0.27 – 0.60	0.4141	30 December 2012
	2003	893,433	0.48 – 0.50	0.4980	27 February 2013
		6,821,517		0.3518	
2000 Plan	2001	3,769,368	0.22 – 0.28	0.2231	27 September 2011
	2002	522,374	0.24 – 0.27	0.2574	29 August 2012
		4,291,742		0.2273	
2003 Plan	2003	4,468,407	0.47 – 0.66	0.5091	22 October 2013
	2004	6,228,485	0.55 – 1.01	0.6985	29 November 2014
		10,696,892		0.6193	
Director Plan	2000	89,912	0.57	0.57	16 February 2010
	2001	7,498	0.22	0.22	15 April 2011
	2002	26,236	0.44	0.44	6 February 2012
		123,646		0.5212	
ND00 Plan	2000	98,313	0.19	0.19	19 October 2010
	2001	37,528	0.37	0.37	13 August 2011
	2002	43,282	0.37	0.37	2 July 2012
	2003	263,151	0.51	0.51	18 February 2013
		442,274		0.4133	
SAYE	2003	514,801	0.5865	0.5865	31 December 2008
	2004	107,862	0.9435	0.9435	31 December 2009
	2005	450,409	0.9095	0.9095	31 December 2010
	2006	2,010,443	1.0264	1.0264	31 December 2011
	2007	1,036,648	1.104	1.104	31 December 2012
		4,120,163		0.9760	
Total options		75,229,489			
RSU	2006	5,067,122	–	–	20 November 2010
	2007	8,168,644	–	–	12 November 2011
		13,235,766			
French RSU	2006	350,734	–	–	20 November 2010
	2007	259,065	–	–	12 November 2011
		609,799			
LTIP	2005	2,968,594	–	–	February 2008
	2006	2,246,871	–	–	February 2009
	2007	2,728,514	–	–	February 2010
		7,943,979			
DAB	2007	894,000	–	–	February 2010
Total awards		22,683,544			
Total options and awards		97,913,033			

7 Called-up share capital continued

Under the UK Inland Revenue Executive Approved Share Option Plan (the "Executive Scheme"), the Company may grant options to directors and employees meeting certain eligibility requirements. Options under the Executive Scheme are exercisable between three and ten years after their issue, after which time the options expire.

Under the Company's Unapproved Scheme (the "Unapproved Scheme"), for which it has not sought approval from the UK tax authorities, options are exercisable one to seven years after their issue, after which time the options expire. The Company also operates the US ISO Scheme, which is substantially the same as the Unapproved Scheme, the main difference being that the options are exercisable one to five years after their issue. Under both of these schemes options are exercisable as follows: 25% maximum on first anniversary, 50% maximum on second anniversary, 75% maximum on third anniversary, 100% maximum on fourth anniversary. Various options to directors under the Unapproved Scheme have certain performance criteria attached, which if met are exercisable after three years, otherwise they will become exercisable after seven years.

There are further schemes for our French and Belgian employees (the "French Scheme" and the "Belgian Scheme"). In the French Scheme, options are exercisable between four and seven years after their issue, whilst in the Belgian Scheme, options are exercisable from 1 January following the third anniversary after their issue, up to seven years from issue.

Upon the acquisition of Artisan in 2004, the Company assumed the share schemes of Artisan existing at acquisition. The schemes remained substantially the same as prior to the acquisition, other than the options became options to purchase shares in ARM Holdings plc instead of Artisan Components Inc. The number and value of options were amended in line with the conversion ratio as detailed in the merger agreement. The schemes assumed were the "1993 Plan", the "2000 Plan", the "2003 Plan", the "Director Plan" and the "ND00 Plan".

Under each plan, there are multiple vesting templates and vesting periods. The majority of the options were already vested upon acquisition, and the most common template was 25% vesting after one year, and then 6.25% vesting each quarter thereafter, until 100% vest after four years. Some options vest on a monthly basis, and some vest over five years. All options lapse ten years from the date of grant.

The Company also operates savings-related share option schemes (SAYE) for all employees and executive directors of the Group. The number of options granted is related to the value of savings made by the employee. The period of savings is either three or five years, except for ARM Inc. employees where the period is two years. The option price for grants made in 2007 was set at 80% of the market share price prior to the grant, but in previous years was set at 85%, and the right to exercise normally only arises for a six-month period once the savings have been completed, except for ARM Inc. where the right to exercise only arises for a three-month period. In 2007, the Company commenced a new savings-related option scheme for US employees, namely the Employee Share Purchase Plan (ESPP). The number of options granted is related to the value of savings made by the employee. The period of savings is six months, with the option price being at 85% of the lower of the market share price at the beginning and end of the scheme.

The Company also issues restricted stock units (RSUs) to employees which are actual share awards on vesting rather than options to buy shares at a fixed exercise price. The main RSU awards (to employees in all jurisdictions other than France) vest similarly to the unapproved scheme above, namely 25% on the each anniversary over four years. RSU awards to our French employees vest 50% after two years, and then a further 25% after three and four years. Whilst the Company reserves the right to award options to employees going forward, the majority of awards to employees will be in RSUs.

Additionally, the Company operates a Deferred Annual Bonus plan (DAB). Under the DAB, which is for directors and selected senior management within the Group, participants are required to defer 50% of any related annual bonus into shares on a compulsory basis. These shares will be deferred for three years, and then a further matching award will be made depending on the achievement of an EPS performance condition over that time. The Company also operates the Long Term Incentive Plan (LTIP), also for directors and selected senior management, whereby share awards are made and vest depending on the Company's TSR performance compared to two comparator groups over the three-year performance period.

For disclosures relating to the grants in the year and fair value assumptions, reconciliations of opening to closing option balances and related items, please refer to note 23 in the IFRS accounts within these financial statements.

8 Share premium account and reserves

	Share premium account £000	Option reserve £000	Other reserve £000	Profit and loss account £000
At 1 January 2007	97,616	61,474	267,418	(980)
Premium on exercise of share options	5,504	–	–	–
Purchase of treasury shares	–	–	–	(120,419)
Appropriation for future cancellation of shares	–	–	–	(8,142)
Cancellation of shares	–	–	–	28
Cancellation of share premium account and other reserve	(103,120)	–	(267,418)	370,538
Proceeds on issue of treasury shares on exercise of share options	–	–	–	13,383
Credit in respect of FRS 20 employee share scheme charges	–	–	–	16,786
Profit for the financial year	–	–	–	129,777
At 31 December 2007	–	61,474	–	400,971

The Company has taken advantage of merger relief and not recorded the premium on the issue of shares for the acquisition of Artisan Components Inc. (now ARM Inc.). The option reserve represents the fair value of options granted on the acquisition of Artisan Components Inc. in 2004. The other reserve represents the unrealised profit on the intra-group sale of investments. Following shareholder and Court approval during the year, the other reserve became distributable and has accordingly been transferred to the profit and loss account. In addition, the Company also reduced the share premium account in existence on 30 June 2007 to nil, and thus has similarly been transferred to the profit and loss account.

The Company considers the share premium account, option reserve and other reserve as non-distributable. Within the profit and loss account is £66,815,000 of credits in respect of FRS 20 employee share scheme charges in respect of services performed by employees of subsidiary undertakings and recorded as a capital contribution. The Company also considers these credits as non-distributable. As such, £334,156,000 of the profit and loss account is deemed distributable.

During 2007, to supplement the payment of dividends to shareholders, the Company continued its rolling share buyback programme under the shareholder authority conferred at the 2005 Annual General Meeting. The quantum and frequency of share re-purchases is not predetermined and will take into account prevailing market conditions, the short- to medium-term cash needs of the business and the level of employee share-based remuneration going forward. In 2007, a total of 94.5 million (2006: 63.6 million) shares were re-purchased from the market at a cost of £128,561,000 (2006: £76,519,000). At 31 December 2007, there were 65,201,176 (2006: 49,500,000) shares in the Company still held from these purchases with a market value of £80,849,000 (2006: £62,246,000). Share repurchase transactions in respect of 49,500,000 shares carried out between 19 May 2006 and 31 December 2006 and 6,219,000 shares carried out between 1 January 2007 and 21 February 2007 took place at a time when the Company had no distributable reserves and accordingly such shares have not been properly acquired in accordance with the Companies Act 1985, and are not available for re-issue or cancellation. The Company made an application to the Court during 2007 to cancel these shares pursuant to a special resolution passed at the 2007 AGM.

Offset within the profit and loss account is an amount of £90,000,000 (2006: £58,245,000) representing the cost of own shares held with the ESOP and treasury shares. This comprises £348,000 (2006: £348,000), being the cost of 1,201,434 (2006: 1,201,434) shares held within the ESOP and £89,652,000 (2006: £57,897,000) being the cost of 65,201,176 (2006: 49,500,000) shares held as treasury shares. The nominal value of own shares held is £33,201.

9 Reconciliation of movements in shareholders' funds

	2007 £000	2006 £000
Profit attributable to shareholders	148,324	6,741
Equity dividends	(18,547)	(12,367)
	129,777	(5,626)
New share capital issued	5,509	2,106
Purchase of treasury shares	(120,419)	(18,622)
Appropriation for future cancellation of shares	(8,142)	(57,897)
Proceeds on issue of treasury shares on exercise of share options	13,383	15,754
Credit in respect of FRS 20 employee share scheme charges recorded as capital contributions	16,786	17,437
Net addition to/(reduction in) shareholders' funds	36,894	(46,848)
Opening shareholders' funds	426,223	473,071
Closing shareholders' funds	463,117	426,223

10 Capital commitments

The Company had no capital commitments at 31 December 2007 and 2006.

11 Financial commitments and contingencies

At 31 December 2007 and 2006 the Company had no annual commitments under non-cancellable operating leases.

12 Related party transactions

The Company has taken advantage of the exemption from disclosure available to parent companies under FRS 8, "Related party disclosures", where transactions and balances between Group entities have been eliminated on consolidation.

Independent auditors' report to the members of ARM Holdings plc

We have audited the parent company financial statements of ARM Holdings plc for the year ended 31 December 2007 which comprise the company balance sheet and related notes. These parent company financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the directors' remuneration report that is described as having been audited.

We have reported separately on the Group financial statements of ARM Holdings plc for the year ended 31 December 2007.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report, the directors' remuneration report and the parent company 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 parent company financial statements and the part of the directors' remuneration report to be audited 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 parent company financial statements give a true and fair view and whether the parent company financial statements and the part of the directors' remuneration report to be audited have been 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 parent company financial statements. The information given in the directors' report includes that specific information presented in the Chairman's statement and the Chief Executive Officer's review of operations and the financial review that is cross referred from the review of business section of the directors' report.

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 other information contained in the annual report and consider whether it is consistent with the audited parent company financial statements. The other information comprises only growth strategies, business highlights, the Chairman's statement, the Chief Executive Officer's review of operations, the financial review, board of directors, shareholder information, the corporate governance statement, the corporate social responsibility statement, the directors' report and that part of the remuneration report that is unaudited. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the parent company financial statements. Our responsibilities do not extend to any other information.

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 parent company financial statements and the part of the directors' remuneration report to be audited. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the parent company 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 parent company financial statements and the part of the directors' remuneration report to be audited 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 parent company financial statements and the part of the directors' remuneration report to be audited.

Opinion

In our opinion:

- The parent company 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;
- The parent company financial statements and the part of the directors' remuneration report to be audited have been properly prepared in accordance with the Companies Act 1985; and
- The information given in the directors' report is consistent with the parent company financial statements.



PricewaterhouseCoopers LLP

Chartered Accountants and Registered Auditors
London
3 April 2008

ARM Holdings plc

110 Fulbourn Road
Cambridge CB1 9NJ
United Kingdom
Tel: +44 (0) 1223 400400
Fax: +44 (0) 1223 400410

ARM Limited

Liberty House
Moorbridge Road
Maidenhead
Berkshire SL6 8LT
United Kingdom
Tel: +44 (0) 1628 427700
Fax: +44 (0) 1628 427701

Rockingham Court
Rockingham Street
Sheffield S1 4EB
United Kingdom
Tel: +44 (0) 114 8000
Fax: +44 (0) 114 8001

Blackburn Design Centre
Belthorn House
Walker Road
Blackburn BB1 2QE
United Kingdom
Tel: +44 (0) 1254 893900
Fax: +44 (0) 1254 893901

ARM Belgium NV

Geldenaaksebaan 329
1st fl.
3001 Leuven-Heverlee
Belgium
Tel: +32 16 391 411
Fax: +32 16 406 076

ARM France SAS

12 Avenue des Prés
Montigny le Bretonneux
78059 Saint Quentin en
Yvelines, Cedex
France
Tel: +33 1 30 79 05 10
Fax: +33 1 30 79 05 11

25 Allée Pierre Ziller
Le Paros
BP 70124
06903 Sophia Antipolis
Cedex
France
Tel: +33 4 97 23 51 00
Fax: +33 4 97 23 51 99

Miniparc Polytec
60 Rue des Berges
38000 Grenoble
France
Tel: +33 4 56 38 47 00
Fax: +33 4 56 38 47 01

ARM Germany GmbH

Lehrer-Wirth-Strasse 4
D-81829 Munich
Germany
Tel: +49 89 928 615-0
Fax: +49 89 928 615-19

Kaiser Strasse 100
TPC 111C
D-52134 Herzogenrath
Germany
Tel: +49 24 079 086-0
Fax: +49 24 079 086-11

Keil Elektronik GmbH

Bretonischer Ring 15
D-85630 Grasbrunn
Germany
Tel: +49 89 456 040-0
Fax: +49 89 468 162

ARM Israel

3 Hagavish Street
44424 Kfar Saba
Israel
Tel: +972.9.7644867
Fax: +972.9.7644884

ARM Norway AS

Gryta 2B
7410 Trondheim
Norway
Tel: +47 4000 5757
Fax: +47 7351 3181

ARM Inc.

141 Caspian Court
Sunnyvale, CA 94089-1013
United States
Tel: +1 408 734 5600
Fax: +1 408 734 5050

1250 Capital of Texas
Highway
Building 3, Suite 560
Austin, TX 78746
United States
Tel: +1 512 327 9249
Fax: +1 512 314 1078

8000 Regency Parkway
Suite 660
Cary, NC 27518
United States

5 East Street
Franklin, MA 02038
United States
Tel: +1 508 520 1905
Fax: +1 508 520 1907

1 Jenner Drive, Suite 260
Irvine, CA 92618
United States
Tel: +1 949 341 1900
Fax: +1 949 341 1901

Crystal Glen Center
39555 Orchard Hill Place
Suite 600
Novi, MI 48375
United States
Tel: +1 248 374 5055
Fax: +1 248 374 5056

264B North Broadway
Suite 204A
Salem, NH 03079
United States
Tel: +1 603 896 6322
Fax: +1 603 896 6324

1501 10th Street
Suite 110
Plano, TX 75074
United States
Tel: +1 972 312 1107
Fax: +1 972 312 1159

204 Chandler Court SW
Suite 290
Olympia, WA 98502
United States
Tel: +1 972 312 1107
Fax: +1 972 312 1159

ARM KK

Daini-Ueno Building 8F
3-7-18 Shin-Yokohama
Kohoku-Ku, Yokohama-Shi
Kanagawa 222-0033
Japan
Tel: +81 45 477 5260
Fax: +81 45 477 5261

ARM Korea Limited

Room 1115
Hyundai Building
9-4, Soonae-Dong
Boondang-Ku
Sungnam
Kyunggi-do 463-020
Korea
Tel: +82 31 712 8234
Fax: +82 31 713 8225

ARM Taiwan Limited

10F-3, No. 17, Lane 91
Sec. 1, Nei Hu Rd,
Taipei, 114
Taiwan
Tel: +886 2 2627 1681
Fax: +886 2 2627 1682

ARM Consulting (Shanghai) Co. Ltd

Room 809, Building B
Far East International Plaza
No. 317 XianXia Road
Shanghai 200051
PR China
Tel: +86 21 62351296
Fax: +86 21 62351207

Room 905, Silver
Tech Tower
No. 38 Hai Dian Avenue
Hai Dian District
Beijing 100080
PR China
Tel: +86 10 82603570
Fax: +86 10 82603573

ARM Embedded Technologies Pvt. Limited

Level III, Block B
Salarpuria Hall Mark
Marthahalli-Sarjapur
Outer Ring Road
Bangalore 560 087
India
Tel: +91 80 4138 4000
Fax: +91 80 4112 7403

ARM Physical IP Asia Pacific Pte. Ltd

700 Lorong 1 Toa Payoh
30-07 Trellis Towers
Singapore 319773
Tel: +65 6728 0950
Fax: +65 6728 7901

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ARM Holdings plc
110 Fulbourn Road
Cambridge CB1 9NJ
United Kingdom

Telephone +44 (0)1223 400400
Facsimile +44 (0)1223 400410

www.arm.com

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