

Reports and Financial Statements
Year ended 31 July 2012

HERIOT-WATT UNIVERSITY

Reports and Financial Statements

Year Ended 31st July 2012

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OPERATING AND FINANCIAL REVIEW

HIGHLIGHTS

As the operating and funding environment of universities continues to experience significant change it is pleasing to report that Heriot-Watt has performed well during the financial year to 31 July 2012. Some notable highlights include:

- The accolade of The Sunday Times "Scottish University of the Year" for the second year running in September 2012, the new award of "UK University of the Year for Student Experience", and an overall ranking of 9th in the UK in The Sunday Times' respected university league table
- The top rating in Scotland and 4th among UK universities in the National Student Survey (NSS) 2012, with 91% Heriot-Watt University students expressing overall satisfaction with their experience, and among the highest UK ratings in the great majority of our subjects
- The fastest growth in undergraduate applications 2011-2012 of any mainstream UK university, and a buoyant intake of highly qualified students from across Scotland, the UK and internationally in autumn 2012, at a time of challenge from the introduction of sharply increased tuition fees for students from England, N Ireland and Wales
- The opening in September 2012 of the first phases of a £34 million programme to renew student residential provision at both the Edinburgh and Scottish Borders Campuses
- In addition to these indicators of success and achievement at home, Heriot-Watt's reputation as "Scotland's International University" took another step forward through selection, against international competition, to establish a new purpose-built Heriot-Watt University campus in Putrajaya, Malaysia, to open in 2014
- The completion in November 2011 of a £35 million development of an enlarged Heriot-Watt University Campus in Dubai International Academic City, United Arab Emirates, doubling capacity to provide for up to 5,000 students; investment in the campus is supported through the University's partnership with Eikon International Holding as infrastructure provider.

Other notable headlines specifically in relation to the University's financial performance include:

- 3.5% revenue growth to £155.6 million;
- £6.4 million net surplus, 4.1% of total income (increased from £5.5 million, being 3.7% of total income in 2011)
- Net Assets, excluding pension liability, up from £80.6 million in 2011 to £88.5 million in 2012

VISION, MISSION, STRATEGY

Vision

Heriot-Watt's vision is to be world-leading within its specialist areas of science, engineering, technology and business.

Mission

Our mission is to create and exchange knowledge for the benefit of society. We shall:

- Strengthen research intensity in fields of economic and societal benefit;
- Provide truly global education while maintaining our Scottish roots; and
- Deliver excellent student experience and highly employable graduates.

Strategy

Heriot-Watt University is a research-led university operating in an environment where the focus on performance is critically important. We wish to be recognised as a high performing university achieving excellence in teaching and research, with a strong profile in knowledge transfer and exceptional developments

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in the internationalisation of higher education. During 2012 the University has been revising and refreshing its Strategic Plan for the next five year period. The overall priorities for 2013–18 are identified as

- increased Research Intensification,
- enhanced Learning and Teaching and Student Experience,
- continued Internationalisation, and
- Efficient and Effective Professional Services.

Particular emphasis is given to the expectation that all academic staff should be active at internationally competitive levels in research and/or scholarship, and involved in research-informed teaching, with the University's research base strengthened through continued academic recruitment, strategic collaborations and enhanced strategies to secure research funding.

ECONOMIC IMPACT

An important aspect of the University's activities is impact on the wider economy. During 2012 the University commissioned a study to assess its economic impact. The results of the study indicate that the University makes a significant impact on the local and national economies. The key findings from the study are available from the University on request.

RESOURCES

The University has a combination of tangible and intangible resources that it deploys in pursuit of its strategic objectives. Tangible resources include:

Campus Locations

- Edinburgh;
- Galashiels (Scottish Borders Campus);
- Orkney;
- Dubai.

A new Heriot-Watt campus is currently being developed in Malaysia in the new administrative capital of Putrajaya. The campus is expected to open in 2014.

Research Facilities

- Own specialist laboratories and research equipment
- Access to shared resources through collaborations with other universities
- Access to resources held by industrial partners.

Physical Infrastructure

During the year we continued the implementation of our Estate Strategy, investing in University's physical infrastructure, including major student residential re-developments at the Edinburgh and Scottish Borders Campuses, the new enlarged Dubai Campus, and the commencement of the Heriot-Watt University Malaysia Campus, all as referred to above. In addition, considerable work continues to maintain and upgrade student-facing service facilities; provide up-to-date teaching and research facilities, and to address long term maintenance issues.

Financial

At the year-end the Group had net assets of £70.8 million (2011: £68.7 million), an increase of £2.1 million compared with the prior year. This is mainly due to an increase in the Group's pension liability of £5.9 million and a reduction in balances held in bank and cash, offset by increases in tangible fixed assets. Net assets, excluding the pension liability, increased from £80.6 million to £88.5 million.

This performance is attributable to a strong operating performance and the investment in the Group's asset base.

Further details are set out in the balance sheet on pages 20 to 21.

OPERATING AND FINANCIAL REVIEW

The Group's £40 million revolving credit facility, agreed in 2007, has provided the University with the stability of having secure funding sources in place during a period of extraordinary turmoil in the financial markets. At the year-end drawings totalling £20 million had been made against this facility. The full value of this facility is protected from financial market volatility by long term interest rate swaps. The lending is at very competitive rates and there is no penalty for the unused portion of the facility.

During the year, the Group began to draw down funding from a further facility agreed in May 2011. The total facility available amounts to £25m and was secured to fund the development of new student residences on the Edinburgh and Galashiels campuses. At the year-end a total of £20.5 million had been drawn down, with the balance to be utilised during 2012-13. Discussions are underway with the bank providing this facility regarding its conversion into a term loan and in relation to the balance to be covered by interest rate swaps.

People

At the year-end the University employed 1,644 people, expressed as full time equivalents, of which 663 were academic staff (i.e. roles in teaching and/or research).

New senior appointments made in the year included: Deputy Principal for Learning and Teaching; Director of Governance and Legal Services; Vice-Principal and Chief Executive Officer Heriot-Watt University Malaysia; Chief Operating Officer Heriot-Watt University Malaysia.

We are very positive about the contribution and the progress made through our staff in the past year. We are committed to continuing to develop our staff as well as developing Heriot-Watt as an organisation over the coming years. Our approach is to enable all our staff to be the best that they can be, supported and enabled through the Human Resource Development team, including staff from across the globe. Significant highlights include work to:

Embed Our Values

- Embed the Spirit of Heriot-Watt values across the University, and build on 72% of staff who identified with the University's values in the last staff engagement survey, with a very successful third year of the Spirit of Heriot-Watt awards scheme, including winners from China and Dubai, and the introduction of a Partner Award to recognise the wide outreach and collaborative approach of Heriot-Watt University
- Maintain high levels of staff engagement and commitment, with a new employee engagement strategy "Creating pride and belonging".

Develop Our People

- Recruit high calibre academic staff through the Global Platform initiative, bringing in over 20 new members of academic staff to work alongside our existing academic community.
- Develop individual capability, through the Performance Development Review process, which is now in use widely, with over 90% of staff participating in PDR meetings, to agree annual objectives, and discuss individual performance and development.

Develop Leadership

- Develop Leadership capability with a new Leadership Excellence Framework for all staff, and a Programme to improve the way we manage/lead.
- Develop academic staff, particularly early career researchers, with Academic Enhancement being short-listed for 2 Times Higher awards for 'Outstanding Contribution to Leadership Development' and 'Outstanding Support for Early Career Researchers'.
- Widen Heriot-Watt's approach to early career researchers development to include not only Heriot-Watt, Edinburgh and Scotland but now European 'Crucibles'.

Develop the Organisation

- Support change programmes to enable people to contribute fully to the University's strategic ambitions, with HR and OD acting as advisor, coach and facilitator to those managers leading change in Schools and Services, particularly the School of Textiles and Design which underwent a significant restructuring during 2012

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- Implementing a number of pay, pension and policy changes over the year, putting in place a robust HR framework within which to manage and support all staff, and ensure we remain an excellent employer, with low staff turnover and high levels of engagement.

Equality of Opportunity

The University is committed to equality and to value diversity in our staff and students. Applications for employment by any person with a protected characteristic are always considered fairly. It is the policy of the University that all staff are treated equally, with every effort made to ensure that appropriate training is arranged for all. It is the policy of the University that the recruitment, training, career development and promotion of all those with a protected characteristic should, as far as possible, be identical with that of other employees. The University has successfully retained the 'positive about disability' (two ticks) award.

Reputation

Heriot-Watt's reputation for academic achievement is a core intangible asset on which our strategic ambition rests. The University's standing in the National Student Survey has risen consistently and rapidly in recent years, culminating in this year's position of 4th out of 125 UK universities, and comfortably top in Scotland. In the Sunday Times Good University Guide, the University recorded the greatest rise in the Guide's history, from 31st place last year to 9th this year. Accordingly, Heriot-Watt University has the unprecedented achievement of receiving the Sunday Times title of Scottish University of the Year for the second year running. In the Times Higher Education (THE) rankings of universities worldwide, which is heavily influenced by international research reputation, Heriot-Watt University ranks in the top 3% world-wide (at 360th out of an estimated >12,000 higher education institutions).

In summary, the University provides an inclusive and supportive working environment and complies with all relevant legislation in relation to equality and diversity for staff and students.

RISK MANAGEMENT

The Group has a risk management strategy that identifies, captures and monitors the main risks facing the Group as it seeks to achieve its strategic plan. During 2012 the University undertook a review of the risk management strategy and process which included the delivery of a number of workshops. The review has improved the embedding of risk management across all activities and is firmly aligned to the University's strategic and operational plans. The risk management process is regularly monitored, reviewed and reported to the University's Risk Management Strategy Group, the University Executive and the Audit and Risk Committee.

STAKEHOLDER RELATIONSHIPS

A University is a complex organisation with many stakeholders including:

- Students
- Staff
- Court (governing body)
- Government
- Public funding bodies (Scottish Funding Council, Research Councils and others)
- Private and commercial clients and funders
- Business and industry
- Alumni
- The local and regional and other communities with which we engage in our various locations.

Maintaining strong effective relationships with all of them is critical to achieving success.

CURRENT DEVELOPMENT, PERFORMANCE AND OPERATION OF GROUP BUSINESS

The Group continues to make steady progress in implementing its strategy, which requires a sustained increase in the surplus being generated to provide the necessary funds for future investments, in both major capital projects and new academic staff, which are critical to achieving success.

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Scope of the financial statements

The financial statements which have been approved by the Court for the year-ended 31st July 2012 consolidate the transactions of the University and its subsidiary undertakings.

Results for the year

The Group reported a surplus of £6.4 million for the year; this represents an increase of £0.9 million (16.4%) compared to the prior year.

The table below summarises the consolidated income and expenditure reported for the last five financial years.

	2012	2011	Re-stated ² 2010	2009	2008
	£m	£m	£m	£m	£m
Income	155.6	150.3	142.7	134.5	117.8
<i>Year on year %</i>	<i>+3.5%</i>	<i>+5.3%</i>	<i>+6.1%</i>	<i>+14.2%</i>	<i>+6.4%</i>
Expenditure	(149.2)	(144.8)	(135.6)	(133.9)	(116.4)
<i>Year on year %</i>	<i>+3.0%</i>	<i>+6.8%</i>	<i>+1.3%</i>	<i>+15.0%</i>	<i>+6.9%</i>
Net surplus	6.4	5.5	7.1	0.6	1.4
Underlying surplus ¹	5.7	4.9	2.3	0.2	0.6

¹ excluding FRS 17 pension adjustment

² being the prior year adjustment required to the Group's pension assets and liabilities to implement the UK Government's announcement in June 2010 that, in future, increases in public sector pension schemes will be linked to changes in the Consumer Prices Index (CPI) rather than, as previously, the Retail Price Index (RPI).

In 2011-12 the Group achieved income growth of 3.5% with total income increasing by £5.3 million to £155.6 million. Growth was seen across most of the Group's main income categories, except for Funding Body Grants, where there has been a reduction due to the decline in the recurring teaching grant and the capital grant provision.

The Group's sources of funding continue to be diversified, as set out in Notes 2 to 6 on pages 30 and 31. The Group utilises the public funds made available from the Scottish Funding Council (SFC) highly efficiently, with its total income being more than four times greater than its core base funding. In 2011-12 the recurrent grants received from the SFC for teaching decreased by 9.3% (2011: decrease 1.5%) and for research decreased by 2.1% (2011: 4.2% decrease). The net decrease, for teaching and research combined, being £2.5 million.

The strong performance of Tuition Fees and Education Contracts (Note 3) achieved during 2012 was due to income growth across all categories of students, which reflected both higher student numbers and fee levels.

Geographical Analysis of Student Income Growth

	2012	Change	2011	2010	2009	2008
	£m	%	£m	£m	£m	£m
UK and European Union students	13.6	+7.1%	12.7	13.2	11.6	10.5
Non-European Union students	38.6	+19.1%	32.4	26.6	21.5	14.8

Considerable effort continues to be committed to developing new research proposals. During the year the Group successfully sustained research grant income in an increasingly competitive environment. Total external research income for the year was £22.7 million (2011: £21.2 million).

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In relation to the Group's active subsidiaries Edinburgh Business School and Heriot-Watt Trading Ltd reported positive results. Heriot-Watt Sports Village Ltd reported a loss. Heriot Watt University Malaysia was incorporated during the year.

Edinburgh Business School reported a surplus of £1.4m (2011: £3.1m).

Heriot-Watt Trading Ltd reported a profit of £159,000 (2011: £160,000).

Heriot-Watt Sports Village Ltd reported a loss of £22,000 (2011: profit £9,000). The directors are continuing to review the business' trading position in order to strengthen the underlying financial performance.

The overall Group financial performance can be summarised as follows:

	2012	Change	Restated			
			2011	2010	2009	2008
	£m	%	£m	£m	£m	£m
Income	155.6	+3.5%	150.3	142.7	134.5	117.8
Staff Costs	77.1	+2.5%	75.2	66.4	73.4	66.3
Other Operating Expenses	64.8	+3.8%	62.4	61.4	50.3	43.0
Depreciation	7.4	+15.6%	6.4	7.1	7.5	5.2
Interest Payable	1.0	-28.5%	1.4	1.9	1.8	1.9
Total Expenditure ¹	150.3	+3.3%	145.4	136.8	133.0	116.4

¹ prior to profits/losses on disposals, taxation and transfers to/from endowments & restricted funds

Staff costs have increased by 2.5% compared to the prior year. This increase is attributable to an increase in staff numbers, up year on year by the equivalent of 33 full-time persons, and automatic increments in grade. Further disclosures are shown in Note 7 to the financial statements. Interest payable decreased due to a diminution of the negative charge on the return on pension assets, based on FRS 17 actuarial estimates. Overall interest payable on the group's bank facilities fell by £0.4m reflecting a reduction in the interest costs of the interest swap arrangements referred to in Note 37, outweighing the interest costs arising from the additional resources drawn during the year to fund the development of the new student residencies.

Cash flow management

The Group's focus on cash flow aims to ensure that cash is available as necessary for normal business and for implementation of the strategic plan.

Net debt increased by £23.7 million (2011: decrease £4.5 million) during the year to £26.4 million (2011: £2.7 million). In May 2011 the Group arranged a £25m development and term loan facility with the Clydesdale Bank to provide long term funding (27 years) for construction of replacement student residences. The drawdown of these funds commenced in 2011-12 which is reflected in the increase in net debt.

Further detail as to the individual elements comprising the Group's cash flow statement can be found in Notes 25 to 28 of the Notes to the Accounts on pages 42 to 44.

Unless special terms are agreed, it is group policy to pay invoices at the end of the month following the month in which the invoice is dated. At 31st July 2012 there were 15 days (2011 - 31 days) of purchases in trade creditors. No interest was payable under the terms of the Late Payment of Commercial Debts (Interest) Act 1998.

Capital projects

The gross capital investment of £31.2 million (2011: £7.5 million) was partially supported by new deferred capital grant receipts of £5.5 million (2011: £5.9 million). The focus of spend of capital investment during the year continued to be on enhancing the physical and IT infrastructure for the Group's students, both on and off

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campus. The main investment related to the construction of new halls of residence on both the Edinburgh and the Scottish Borders Campuses.

Student Numbers

The University's student numbers over the last two academic years are summarised below on a headcount basis:

	2012	<i>Change</i>	2011
Scottish Campuses			
Undergraduates	6,180	+6%	5,825
Taught Postgraduates	1,600	-4%	1,660
Research Postgraduates	<u>840</u>	<u>+7%</u>	<u>785</u>
	8,620	+4%	8,270
Dubai Campus			
Undergraduates	1,815	+59%	1,145
Taught Postgraduates	<u>935</u>	<u>+18%</u>	<u>790</u>
	2,750	+42%	1,935
Independent Distance Learners and Students at Approved Learning Partners (mainly transnational)			
Undergraduates	4,170	+17%	3,550
Taught Postgraduates	9,445	+7%	8,790
Research Postgraduates	<u>250</u>	<u>+25%</u>	<u>200</u>
	13,865	+11%	12,540
	<u>25,235</u>	<u>+11%</u>	<u>22,745</u>

YEAR END POSITION OF THE GROUP

Net assets excluding the pension liability exceeded £88m at the year end. The pension liability continues to fluctuate by material amounts with a significant increase of £5.8m since the previous year end. Full details are provided in Note 30.

During the year the Group's net current liabilities increased by £1.2 million (2011: decreased £10.1m million). This increase is attributable to a number of changes in both the trading element of the Group's working capital and movements in short term cash and debtor balances.

The Group operates a net current liability position to optimise its working capital and uses its revolving credit facility to provide liquidity when required. The University continues to experience growth and careful management of flexible credit facilities are an important element to fund this growth. Based on submissions made to the Group's banks, the Group continues to comply with all of its bank covenants at the year end. In addition projections in October confirmed that this will also be the case for the foreseeable future.

TRENDS AND FACTORS INFLUENCING FUTURE PERFORMANCE

Recent years have seen dramatic changes in the environment in which universities operate. From 2010, the UK Government embarked on a cost reduction programme, with public funding for teaching in universities in England being sharply reduced and replaced by sharply increased tuition fees to be paid by students. The Scottish Government announced cuts in the block grant to the Scottish Funding Council (SFC) for 2011-12 and Scottish universities experienced a period of considerable uncertainty over the Scottish Government's intentions towards student fees. Following the elections to the Scottish Parliament in May 2011, the Scottish Government confirmed that it would fund the tuition costs of Scottish undergraduate students studying in Scotland from the public purse but that universities in Scotland would be allowed to charge tuition fees to students from the 'Rest of UK' from 2012-13. The Scottish Government's spending review was announced in September 2011 and underpinned its manifesto commitment to support higher education with a 14% increase in grants to the SFC over the three years to 2014-15. Other trends and factors which are likely to affect the university's future development, performance and position include:

Academic Profile

- Ability to increase research activity and research funding
- Ability to attract and retain high calibre academic staff

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- Ability to attract well-qualified students, including fee-paying students from “Rest-of-UK” and internationally
- Ability to develop appropriately balanced global presence in the form of international campuses, alliances with learning partners and research collaborations
- Ability to deliver a high-quality educational experience for students, providing high levels of student satisfaction and ensuring a high proportion of graduates are able to move rapidly into graduate-level employment
- Ability to demonstrate delivery of commitments to major funders (Scottish Government and Funding Council, Research Councils UK) and other key stakeholders

External Factors

- Relative certainty on Scottish Government funding
- A new competitive market in Rest of UK student fees
- The impact of the credit crunch and rising longevity on USS and LGPS pension scheme funding
- Exchange rates (the competitiveness of Heriot-Watt’s sterling denominated fees in other countries)
- Continuing uncertainty in the economic and financial environment - e.g. uncertainty on recovery prospects, employment, interest rate, energy and commodity price indicators
- The adverse impact on staff and student recruitment of the UK Border Agency (UKBA) visa requirements
- The Research Excellence Framework
- The University’s research income has been growing steadily in recent years, with a substantial amount of the growth coming from recently recruited academic staff. However, it remains short of our targets and benchmarks, and so research growth is a central theme of the new University strategic plan, including new academic appointments. While overall academic staff numbers have not grown over the last five years, within the last two years academic recruitment has accelerated considerably, with over 50 new appointments made.

The University continues to achieve the challenging targets that it sets itself in recruitment of students in competitive overseas markets. 2012–2013 is the first year in which Scottish universities have been permitted to charge differential fees for students from parts of the UK other than Scotland (‘RUK’ students), and it is pleasing to report that the University has exceeded its already ambitious RUK intake targets.

There have been signs in recent years’ student recruitment of increasing constraints on demand due to the UKBA’s onerous visa requirements. The effect of UK government immigration policy on the ability of universities to recruit overseas students is a matter of debate and engagement with government. Meanwhile, the University is assiduous in ensuring that the UKBA’s requirements are observed.

October 2013 will be the census date for the ‘Research Excellence Framework’ (the successor to the Research Assessment Exercise). The outcome from REF will be known by the end of 2014, and will determine the ‘research excellence grant’ (currently around £10m per annum for the University) for around the next five years. RAE/REF gradings are also a critical element in the perception of a university’s research standing and thus the outcomes of REF will be of major strategic importance to the University.

Corporate Activity to improve financial sustainability

- Implementation of the Strategic Plan
- Continued development of a consistent set of Key Performance Indicators in line with the Strategic Plan
- Better alignment of debtor and creditor cash cycles to ensure cash to fund future expansion
- Development of new Estate strategy and IT strategy
- Continuing to implement process reviews to identify opportunities to improve our effectiveness and efficiency
- Delivering the efficiency and effectiveness improvements identified by academic performance reviews via the implementation of agreed recovery plans
- Significant contingency provision in the University’s operating plan to mitigate potential for income shortfalls
- Continued focus on strong governance

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These features are emphasised in the new University strategic plan. The plan is explicit in terms of quantitative performance indicators in all key areas of activity.

EMPLOYEES

Staff have been kept up-to-date during the year with strategy development, implementation and financial and academic performance through a variety of communication channels.

STUDENT REPRESENTATION

The University has had a long and successful track record of involving its students in decision-making with positive influence on key areas of performance. Students are represented on the Court and several Committees of Court.

DONATIONS

No donations were made during 2011-12 to UK political organisations.

INSURANCE

The Group has insurance policies in place for its officers and for potential claims against them in connection with their role in managing the organisation. In addition, insurance policies are in place to cover all relevant areas of risk in relation to the University's activities and assets.

PENSIONS

The Group's employees are members of one of four pension schemes, the Universities Superannuation Scheme (USS), the Lothian Pension Fund (LPF), Supplementary Pension Scheme (SPS) and the Scottish Teachers Superannuation Scheme (STSS). Of these the first three are still active, with members still employed by the Group.

Details of the accounting policies are set out in Note 1, on pages 23 to 29 and further disclosures are set out in Note 30 on pages 44 to 52. All four schemes provide benefits to members based on final pensionable pay. For the Lothian Pension Fund the underlying assets and liabilities of the University's share of the fund are identifiable and the disclosures required by Financial Reporting Standard 17 'Retirement Benefits' have been fully adopted.

During the year the Group paid total employer contributions of £12.3 million (2011: £11.6 million), details of which are shown in the table below.

<u>Employer Contributions</u>	2011-12	Change	2010-11	Change	2009-10
	£000	%	£000	%	£000
Universities Superannuation Scheme	9,180	+6.8%	8,592	+6.0%	8,107
Lothian Pension Fund	2,996	+4.7%	2,861	+1.9%	2,809
Scottish Teachers Superannuation Scheme	86	-10.4%	96	-1.1%	97
Supplementary Pension Scheme	-	-	-	-	369
Total	<u>12,262</u>	+6.2%	<u>11,549</u>	+1.5%	<u>11,382</u>

The Group continues to operate its Pension+Plus arrangement for employees who are members of USS. Those participating in this arrangement no longer pay employee pension contributions in the usual way. They have instead agreed to a reduction in their salaries equal to their pension contributions and the Group has, in turn, agreed to increase its own pension contributions to cover both the employee and the employer elements.

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Both sides have benefited from this arrangement, with reductions in employee and employer National Insurance contributions. The Group has reinvested the savings it has made in new initiatives and the employees involved have benefited from an increase in take home pay.

Both USS and LPF published their latest triennial valuation reports, for which the reference date is 31st March 2011, in December 2011 and January 2012 respectively.

On the 10th May 2011 the Joint Negotiating Committee of USS agreed changes to the Scheme and the University, as a participating employer, implemented these changes with effect from 1st October 2011. Some of these changes affected current members, but others only impact employees who join the scheme from the implementation date. None of these changes affect those already receiving a pension before the implementation date.

Changes for existing members include an increase to the contribution rate to 7.5%, a higher normal pension age of 65 for future service and a cap to pension increases for service after the implementation date.

For new entrants and re-joiners (unless entitled to re-join the final salary section) to USS a new section of the scheme where benefits are calculated on service and salary at the end of each year rather than final salary on retirement / leaving and re-valued annually in line with official pensions (subject to a cap). The contribution rate for the new section will be 6.5% of salary.

In addition, flexible retirement is to be introduced, cost sharing between members and employers and changes to the early retirement terms from 2013 for those retiring due to redundancy.

In 2013 the Group will be required to adopt arrangements to facilitate pension 'auto enrolment'. Planning is underway to ensure that these arrangements are in place by July 2013, which is the University's staging date under the relevant legislation.

MINORITY INVESTMENTS

The Group has had, for a number of years, a policy for the commercialisation of its research base, in some cases through the creation of 'spin-out' companies, in which it retains a minority investment. As at 31st July 2012 there were fifteen investments (2011 - sixteen) in a range of different companies. The market value of these investments is not reflected in the group's financial statements.

EMPLOYMENT OF DISABLED PERSONS

Applications for employment by disabled persons are always fully considered, bearing in mind the aptitudes of the applicant concerned. In the event of existing employees becoming disabled every effort is made to ensure that their employment with the group continues and that appropriate training is arranged. It is the policy of the Group that the recruitment, training, career development and promotion of disabled persons should, as far as possible, be identical with that of other employees.



*Professor Stephen K Chapman
Principal & Chief Accounting Officer*



*Lord George Penrose
Chairman of Court*

CORPORATE GOVERNANCE STATEMENT

INTRODUCTION

The Group is committed to exhibiting best practice in all aspects of corporate governance and this statement describes the principal governance provisions which presently apply. The Court of the University keeps these provisions under review to take account of best practice from time to time including the principles set out in the Guide for Members of Higher Education Governing Bodies in the UK prepared by the Committee of University Chairmen (CUC). This incorporates internal control guidance for directors on the Combined Code as amended by the British Universities Finance Directors Group.

In the opinion of the Court, the Group complied with the Governance Code of Practice and General Principles and the provisions of the Code provided by the CUC throughout the year ended 31st July 2012. The Court also regularly reviews its governance provisions in line with both recommendations made by SFC and any changes made in the CUC Code.

GOVERNING BODY

The Court, which has twenty five members including the Chairman, who is always one of the lay members, is the ultimate decision taking body. Eleven of the Court members are directly elected, eleven are co-opted and three are ex officio. The Court has responsibility for the Group's strategic direction, reputation, financial well-being, the well-being of staff and students and, in association with the Senate, establishing and maintaining high standards of academic conduct and probity.

To discharge these responsibilities:

- The Court met six times during the year including at an annual strategy review 'away day'. The principal business of the Court is the consideration and approval of strategic plans and annual budgets, the monitoring of staffing, student, estates and finance issues, the setting and review of appropriate performance measures and ensuring that there is a clear definition of delegated powers and lines of accountability. At each meeting the Court receives a management report from the Principal as well as reports from its Committees. Members of the University Executive attend Court meetings along with Deans to support engagement and communication with the University Community.
- The terms of reference of all of the Committees of Court are approved by the Court.
- The Court has a Remuneration Committee which is made up of lay members. The Principal and Secretary are in attendance but are not present when their personal remuneration is considered. There is also a Governance & Nominations Committee of Court made up of lay members, the Principal and the Vice-Principal, with the lay members being in the majority. The Remuneration and the Governance & Nominations Committees meet at least once per year under the convenership of the Chairman of Court.
- The Court has an Audit & Risk Committee. Made up of lay members it met six times during the year, all of these with the External Auditors and all except one with the Internal Auditors. It commissions, receives and considers reports and recommendations for the improvement of internal controls along with management responses. It also reviews the University's annual reports and financial statements.
- The Court also has Finance and Staff Committees- Four committees report to the Finance Committee: the University Collections Committee; the Endowments Committee; the Campus Committee; and the Fees Working Group.
- There is an Emergency Committee of Court consisting of the Chairman of Court as Chair of the Committee and the chairs of the key committees of the Court as well as the Principal and Vice Principal ex officio. The Committee deals with emergency business which may arise between Court meetings.
- Where the Group has commercial interests, the Court, through the Group's management, appoints directors to the boards of companies appropriate to the nature and size of the University's shareholding.
- The Group has taken necessary steps to ensure compliance with FRS8 on Related Party transactions and any interests which require to be disclosed to members of Court are recorded in the Court minutes. The Register of Interest for members of Court is maintained and updated annually.
- The Secretary of the University is the Clerk to the Court.

CORPORATE GOVERNANCE STATEMENT

CORPORATE STRATEGY

The Strategic Plan 'Focus on the Future', in place in 2011-12, was approved by the Court in June 2008 and submitted to the SFC and publicly launched in November 2008. Throughout 2011-12 a new University Strategic Plan (2013-18) has been under development with the direct involvement of members of the Court through a range of strategy workshop events; through discussions at the May Court Away Day; and through an additional Court strategy discussion event which took place in February 2012. The Court approved an outline of the Strategic Plan, with underpinning Key Performance Indicators, at its meeting in June 2012, and approved the final Plan at its meeting in October 2012, for publication, launch and submission to the SFC.

The University's supporting Five-Year (Financial) Plan is reviewed and updated on an annual basis and is approved by the Court each year at its June meeting prior to submission to the SFC. Throughout its annual schedule of meetings the Court receives regular update reports on the development of the Five-Year Plan and issues arising which are presented by the Vice-Principal.

Statement of responsibilities of the University Court

The Court is responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Group, and enable it to ensure that the financial statements are prepared in accordance with the University's Charter, the Statement of Recommended Practice (SORP): Accounting for Further and Higher Education, Accounts Directions from SFC and other relevant accounting standards. In addition, within the terms and conditions of a Financial Memorandum agreed between the Scottish Funding Council and the Court of the University, the Court, through its designated office holder, is required to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Group and of the surplus or deficit and cash flows for that year.

The Group acknowledges that the Court assumed new responsibilities in April 2006 when the Office of the Scottish Charity Regulator (OSCR) assumed its new statutory responsibilities and powers as a statutory non Ministerial Department. The Group believes that the delivery of its mission by its charitable activities provides continuing public benefit. It aims to comply with OSCR's regulatory requirements as they are developed, including the requirement to maintain independent control by its trustees.

In causing the Accounts to be prepared the Court has ensured that:

- They are prepared on the going concern basis in that the Court is satisfied that the Group has adequate resources to continue in operation for the foreseeable future.
- Suitable accounting policies are selected and applied consistently.
- Judgements and estimates are made that are reasonable and prudent.
- Applicable accounting standards are followed, subject to any material departures disclosed and explained in the Accounts.

The Court has taken reasonable steps to:

- Ensure that funds from SFC are used only for the purposes for which they have been given and in accordance with the Financial Memorandum and any other conditions which the Funding Council may from time to time prescribe. Under the terms of the Financial Memorandum the designated officer, who is required to ensure such compliance, is the Principal and Vice-Chancellor.
- Ensure that there are appropriate financial and other internal controls in place to safeguard public funds and funds from other sources, and ensure value for money is achieved in the application of those funds. This system of internal control is continuously reviewed and developed in line with current best practice.
- Safeguard the assets of the Group and prevent and detect fraud.
- Secure the economical, efficient and effective management of the Group's resources and expenditure.

CORPORATE GOVERNANCE STATEMENT

- Ensure that the Group's management has an adequate system of internal control, and regularly monitors and reviews its effectiveness. Such a system is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement or loss.
- Maintain a safe and secure environment for the staff and students.

RISK MANAGEMENT AND INTERNAL CONTROLS

The Group's system of internal financial control includes the following:

- Definition of the responsibilities of, and the authority delegated to, heads of academic and administrative operating groups.
- A comprehensive planning process for each operating group, together with detailed annual income, expenditure, capital and cash flow budgets, overseen by the Vice-Principal (Strategy & Resources) together with the Director of Finance and the Director of Planning.
- Monthly reviews of financial results involving variance reporting and updates of forecast outturns and regular reviews of academic performance
- Clearly defined requirements for approval of expenditure, with investment decisions involving capital or revenue expenditure being subject to formal detailed appraisal and review according to approval levels set by the Court.
- Financial Regulations, detailing financial controls and procedures, approved by the Audit & Risk Committee and Court.
- An Internal Audit function, which during 2011-12 was contracted out to Ernst & Young. Their annual audit programme is approved by the Audit & Risk Committee to whom they report
- During the year 11 internal audit recommendations were made which related to the highest category of which 45% are complete. Recommendations from the external auditor are also implemented, where possible, to the agreed time plans, with priority allocated in accordance with the ranking set out in the audit reports. In relation to the 2011-12 audit, 3 recommendations were made which related to the highest category.
- The strategic risk management group, comprising senior members of the management team, with lay members of Court in attendance, which identifies, evaluates and manages the Group's significant risks.
- The Audit & Risk Committee on behalf of Court, and with the assistance of both external and internal audit, considers the wider aspects of internal control within the University. It also, with the assistance of internal audit, considers the issue of value for money within the Group.

Over the last five years the Group has successfully used its approach to risk management to focus its available audit resource to the best effect. Progress continued to be made during the last year towards the objective of actioning all recommendations on a prioritised and timely basis and the Audit & Risk Committee continues to encourage the Group's management to build on this progress. This is shown in the table below¹.

Year	No. of external audit recommendations	Completed	No. of internal audit recommendations	Completed
2007-08	14	100%	117	100%
2008-09	12	100%	63	94%
2009-10	9	100%	66 ¹	71%
2010-11	5	100%	65 ¹	75%
2011-12	3 ²	0%	74 ¹	31%

¹ excludes minor recommendations

² recommendations arose from the 2011-12 audit and will be addressed during 2012/13

CORPORATE GOVERNANCE STATEMENT

GOING CONCERN

The Court is satisfied that the Group continues to operate as a going concern.



*Professor Stephen K Chapman
Principal and Chief Accounting Officer*

17th December 2012

INDEPENDENT AUDITOR'S REPORT TO THE UNIVERSITY COURT OF HERIOT-
WATT UNIVERSITY

We have audited the Group and University financial statements of Heriot-Watt University for the year ended 31 July 2012 set out on pages 18 to 56. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

This report is made solely to the University Court of Heriot-Watt University, as a body, in accordance with the Charter and Statutes of the University and, in the University Court's role as charity trustees, in accordance with section 44 (1) (c) of the Charities and Trustee Investment (Scotland) Act 2005 and regulation 10 of the Charities Accounts (Scotland) Regulations 2006 (as amended). Our audit work has been undertaken so that we might state to the University Court of Heriot-Watt University those matters we are required to state to it in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the University Court of Heriot-Watt University, as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of the University Court of Heriot-Watt University and auditor

As explained more fully in the statement of responsibilities of the University Court set out on page 13, the University Court of Heriot-Watt University are responsible for the preparation of the financial statements which give a true and fair view. We have been appointed as auditor under section 44 (1)(c) of the Charities and Trustee Investment (Scotland) Act 2005 and report to you in accordance with the regulations made under that Act. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's and University's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the University Court of Heriot-Watt University; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Operating and Financial Review to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the Group's and University's affairs as at 31 July 2012 and of the Group's income and expenditure, recognised gains and losses and cash flows for the year then ended;
- have been properly prepared in accordance with UK Generally Accepted Accounting Practice and the Statement of Recommended Practice: accounting for further and higher education; and
- have been prepared in accordance with the Charities and Trustee Investment (Scotland) Act 2005, and regulation 14 of the Charities Accounts (Scotland) Regulations 2006 (as amended).

Opinion on other matters prescribed by the terms of our engagement

In our opinion, in all material respects:

- funds from whatever source administered by the institution for specific purposes have been properly applied to those purposes and, if relevant, managed in accordance with relevant legislation, and any other terms and conditions attached to them; and
- funds provided by the Scottish Funding Council have been applied in accordance with the Financial Memorandum.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF THE UNIVERSITY
COURT OF HERIOT-WATT

Matters on which, under the terms of our engagement, we are required to report by exception

We have nothing to report in respect of the following matters where the Charities Accounts (Scotland) Regulations 2006 (as amended) and the terms of our engagement require us to report to you if, in our opinion:

- the information given in the Operating and Financial Review is inconsistent in any material respect with the financial statements; or
- adequate and proper accounting records have not been kept; or
- the financial statements are not in agreement with the accounting records and returns; or
- we have not received all the information and explanations we require for our audit.



DJ Watt

for and on behalf of KPMG LLP, Statutory Auditor

Chartered Accountants

KPMG LLP is eligible to act as an auditor in terms of section 1212 of the Companies Act 2006

Saltire Court

20 Castle Terrace

EH1 2EG

20 December 2012

CONSOLIDATED INCOME AND EXPENDITURE ACCOUNT
FOR THE YEAR ENDED 31st JULY 2012

	<i>Note</i>	<i>2012</i> £000	<i>2011</i> £000
Income			
Funding body grants	2	38,574	43,464
Tuition fees and education contracts	3	73,034	64,074
Research grants and contracts	4	22,748	21,217
Other income	5	20,779	19,767
Endowment and investment income	6	512	1,837
Total Income		<u>155,647</u>	<u>150,359</u>
Expenditure			
Staff costs	7	77,136	75,213
Other operating costs	8	64,811	62,379
Depreciation	11	7,425	6,366
Interest and other finance costs	9	957	1,416
Total Expenditure		<u>150,329</u>	<u>145,374</u>
Surplus on continuing operations after depreciation of tangible assets and before taxation		5,318	4,985
Gain on disposal of assets		25	15
Surplus on continuing operations after depreciation and disposal of assets but before taxation		<u>5,343</u>	<u>5,000</u>
Taxation	10	(229)	4
Surplus on continuing operations after depreciation and disposal of assets and taxation		<u>5,114</u>	<u>5,004</u>
Transfer from net accumulated income in endowment and restricted funds		1,275	513
Net surplus for the year retained within general reserves	24	<u>6,389</u>	<u>5,517</u>

All transactions are in respect of continuing operations.

CONSOLIDATED STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES
FOR THE YEAR ENDING 31ST JULY 2012

	<i>Note</i>	<i>2012</i> £000	<i>2011</i> £000
Surplus on continuing operations after depreciation of assets at valuation and disposal of assets and tax		6,389	5,517
Appreciation of endowment asset investments	<i>15</i>	1,248	373
(Decrease)/increase in endowment asset cash balances held	<i>15</i>	(819)	1,554
Actuarial (loss)/gain in respect of pension schemes		(6,457)	2,571
Total recognised gains relating to the year		<u>361</u>	<u>10,015</u>
 Reconciliation			
Opening reserves and endowments		27,606	17,591
Total recognised gains relating to the year		361	10,015
Closing reserves and endowments		<u>27,967</u>	<u>27,606</u>

BALANCE SHEETS
AS AT 31st JULY 2012

	Note	Group		University	
		2012 £000	2011 £000	2012 £000	2011 £000
Fixed Assets					
Tangible assets	11	128,260	104,441	121,793	98,106
Intangible assets	12	71	121	-	-
Investments	13	5,045	45	9,208	5,050
Total Fixed Assets		<u>133,376</u>	<u>104,607</u>	<u>131,001</u>	<u>103,156</u>
Endowment Assets	15	<u>9,093</u>	<u>8,664</u>	<u>7,789</u>	<u>7,351</u>
Current Assets					
Stock		7	84	-	84
Debtors	16	30,518	26,345	35,286	23,969
Short term investments	13	2,000	-	-	-
Cash at bank and in hand		14,138	23,256	3,383	7,755
		<u>46,663</u>	<u>49,685</u>	<u>38,669</u>	<u>31,808</u>
Less: Creditors - amounts falling due within one year	17	(54,477)	(56,303)	(56,841)	(53,850)
Net Current Liabilities		<u>(7,814)</u>	<u>(6,618)</u>	<u>(18,172)</u>	<u>(22,042)</u>
Total Assets less current liabilities		134,655	106,653	120,618	88,465
Less: Creditors - amounts falling due after more than one year	18	(45,622)	(25,468)	(49,165)	(23,929)
Less: Provisions for liabilities	19	(581)	(599)	(581)	(599)
Net Assets excluding pension liability		<u>88,452</u>	<u>80,586</u>	<u>70,872</u>	<u>63,937</u>
Pension liability	30	(17,685)	(11,849)	(17,560)	(11,770)
Net Assets including pension liability		<u>70,767</u>	<u>68,737</u>	<u>53,312</u>	<u>52,167</u>

BALANCE SHEETS
AS AT 31st JULY 2012

	Note	Group		University	
		2012 £000	2011 £000	2012 £000	2011 £000
Deferred capital grants	20	42,798	41,131	41,257	39,519
Endowment Funds					
Expendable	21	2,560	2,389	2,560	2,389
Permanent	21	6,533	6,275	5,229	4,962
		<u>9,093</u>	<u>8,664</u>	<u>7,789</u>	<u>7,351</u>
Reserves					
Income & expenditure account excl. pension reserve	24	36,559	30,791	21,826	17,067
Pension reserve	24	(17,685)	(11,849)	(17,560)	(11,770)
		<u>18,874</u>	<u>18,942</u>	<u>4,266</u>	<u>5,297</u>
Income & expenditure account incl. pension reserve					
Restricted funds	22	2	-	-	-
Investment reserve	23	-	-	-	-
		<u>70,767</u>	<u>68,737</u>	<u>53,312</u>	<u>52,167</u>
Total Funds					

The Financial Statements on pages 18 to 56 were approved by the University Court on 17th December 2012 and were signed on its behalf by:-



Lord George Penrose
Chairman of Court



Prof. Stephen K Chapman
Principal & Chief Accounting Officer



Ann Marie Dalton
Acting Director of Finance

CONSOLIDATED CASH FLOW STATEMENT
FOR THE YEAR ENDING 31st July 2012

	<i>Note</i>	<i>2012</i> <i>£000</i>	<i>2011</i> <i>£000</i>
Net cash inflow from operating activities	25	2,980	7,392
Returns on investment and servicing of finance	26	(2,191)	(1,659)
Capital expenditure and financial investment	27	(24,407)	(1,210)
Financing	28	14,500	6,000
		<u>(9,118)</u>	<u>10,523</u>
(Decrease)/increase in cash in the year			

Reconciliation Of Net Cash Flow To Movement In Net Debt

	<i>2012</i> <i>£000</i>	<i>2011</i> <i>£000</i>
Net debt at 1 August	(2,744)	(7,267)
Increase in cash in the year	(9,118)	10,523
Financing	(14,500)	(6,000)
Change in net funds	<u>(23,618)</u>	<u>4,523</u>
Net debt at 31 July	29 <u>(26,362)</u>	<u>(2,744)</u>

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

1. Principal Accounting Policies

Fundamental accounting concept

The financial statements have been prepared on the going concern basis, with the parent undertaking having agreed to provide adequate funds, if required, so that all the undertakings within the group may meet their liabilities as they fall due.

Basis of preparation

These financial statements have been prepared in accordance with the Statement of Recommended Practice (SORP): Accounting for Further and Higher Education 2007 and in accordance with applicable accounting standards.

Basis of accounting

The financial statements are prepared in accordance with the historical cost accounting convention with the exception of certain items which are measured at fair value as disclosed in the accounting policies below, and as modified by the revaluation of endowment asset investments.

Basis of consolidation

These financial statements, and associated notes, reflect the group income and expenditure account, statement of total recognised gains and losses and cash flow statement for the year ended 31st July. Balance sheets, and their associated notes, as at 31st July are prepared for the parent (Heriot-Watt University) and the group.

The group financial statements include the University and its subsidiaries, as detailed in notes 13 and 14, in compliance with FRS 2 'accounting for subsidiary undertakings' and FRS 9 'associates and joint ventures'. The results of subsidiaries acquired or disposed of during the year are included in the group income and expenditure account from the day of acquisition or up to the date of disposal.

All intra-group sales and profits are eliminated fully on consolidation.

In accordance with FRS 2 'accounting for subsidiary undertakings', the activities of the Heriot-Watt University Students' Union have not been consolidated, both on grounds of materiality and the fact that it is a separate legal entity in which the University has no financial interest and no control or significant influence over policy decisions.

Recognition of income

Income from tuition fees is recognised in the year for which it is received and includes all fees chargeable to students or their sponsors. The costs of any fees waived by the University and any scholarships given to students are included as expenditure.

Income from grants, contracts and other services rendered is included to the extent of the completion of the contract or service concerned.

Income from donations is credited to the income and expenditure account in the year in which it is earned, unless specific restrictions apply.

All income from short-term deposits and endowments is credited to the income and expenditure account in the year in which it is earned.

Income from specific endowments not expended in accordance with the restrictions of the endowment is transferred from the income and expenditure account to specific endowments.

NOTES TO THE ACCOUNTS

For the year ending 31st July 2012

Leased assets

Costs in respect of operating leases are charged on a straight-line basis over the lease term. Leasing agreements, which transfer to the group substantially all the benefits and risks of ownership of an asset, are treated as if the asset has been purchased outright. The assets are included in fixed assets and the capital elements of the leasing commitments are shown as obligations under finance leases. The lease rentals are treated as consisting of capital and interest elements.

The capital element is applied in order to reduce outstanding obligations and the interest element is charged to the income and expenditure account in proportion to the reducing capital element outstanding. Assets held under finance leases are depreciated over the shorter of the lease term or the useful economic lives of equivalent owned assets.

Repairs and maintenance

Expenditure to ensure that a tangible fixed asset maintains its previously recognised standard of performance is recognised in the income and expenditure account in the period it is incurred. The group has a planned maintenance programme, which is reviewed on an annual basis.

Taxation

The University is an exempt charity within the meaning of schedule 2 of the Charities Act 1993 and as such is a charity within the meaning of section 506(1) of the Income and Corporation Taxes Act (ICTA 1988).

Accordingly, the University is potentially exempt from taxation in respect of income or capital gains received within categories covered by section 505 of the ICTA 1988 or section 256 of the Taxation of Chargeable Gains Act 1992, to the extent that such income or gains are applied to exclusively charitable purposes. The subsidiaries, excluding the Edinburgh Business School, pay to the University, under the Gift Aid scheme, amounts as agreed by the directors of each subsidiary company. In certain circumstances Value Added Tax is recoverable, but where this is not possible the cost is included in the relevant expenditure.

Retirement benefits

All new members of staff have the option of joining a pension scheme.

The schemes currently available to new members of staff on Heriot-Watt contracts of employment are the Universities Superannuation Scheme (USS) and the Lothian Pension Fund (LPF).

Existing employees are entitled to maintain their membership of the Scottish Teachers Superannuation Scheme (STSS), whereas the Supplementary Pension Scheme (SPS) is closed and contains only pensioner members.

Full provision has been made for those pension costs which do not arise from externally funded defined benefit schemes.

The scheme currently available to new members of staff on Edinburgh Business School contracts of employment is the Universities Superannuation Scheme (USS). Existing employees are entitled to maintain their membership of the Lothian Pension Fund (LPF).

None of the group's other subsidiary undertakings operate any other pension schemes.

The amount charged against profits represents either the contributions payable to the individual plans in respect of the year or the service cost expected to arise from employee service in the current year.

USS

Heriot-Watt participates in the Universities Superannuation Scheme (USS), a defined benefit scheme which is contracted out of the State Second Pension (S2P). The assets of the scheme are held in a separate trustee administered fund. Because of the mutual nature of the scheme, the scheme's assets are not hypothecated to individual institutions and a scheme wide contribution rate is set. Heriot-Watt is therefore exposed to actuarial risks associated with other institutions' employees and is unable to identify its share of the underlying assets and liabilities of the scheme on a consistent and reasonable basis and therefore, as required by FRS17 'Retirement Benefits', accounts for the scheme as if it were a defined contribution scheme. As a result, the amount charged to the income and expenditure account represents the contributions payable to the scheme in respect of the year.

NOTES TO THE ACCOUNTS

For the year ending 31st July 2012

LPF

The LPF is a pension scheme providing benefits based on final pensionable pay. The assets and liabilities of the scheme are held separately from those of Heriot-Watt University. Pension scheme assets are measured using market values. Pension scheme liabilities are measured using a projected unit method and discounted at the current rate of return on a high quality corporate bond of equivalent term and currency to the liability. Contributions to the Scheme are calculated so as to spread the cost of pensions over employees' working lives with the University. The Contributions are determined by an actuary on the basis of triennial valuations using the Age Attained Method. Variations from regular cost are spread over the expected average remaining working lifetime of members of the schemes, after making allowances for future withdrawals. The amount charged to the statement of financial activities represents the service cost expected to arise from employee service in the current year.

STSS

Heriot-Watt University participates in the STSS pension scheme providing benefits based on final pensionable pay. The assets of the scheme are held separately from those of Heriot-Watt University. Heriot-Watt University is unable to identify its share of the underlying assets and liabilities of the scheme on a consistent and reasonable basis and therefore, as required by FRS17 'Retirement Benefits', accounts for the scheme as if it were a defined contribution scheme. As a result, the amount charged to the income and expenditure account represents the contributions payable to the scheme in respect of the year.

SPS

The SPS is a pension scheme providing benefits based on final pensionable pay. The assets and liabilities of the scheme are held separately from those of Heriot-Watt University. Pension scheme assets are measured using market values.

In May 2010 the trustees purchased a bulk annuity with Aviva in respect of the benefits for all remaining members of this Scheme. Following this transaction Aviva now hold the assets of the Scheme and are responsible for the payment of the pensions for all members of the Scheme, although the policy is still in the name of the Trustees. The assets and liabilities of this Scheme are therefore deemed to be equal to each other, with expected return on assets and interest cost also assumed to be equal in the future as a result of this transaction. The intention is to wind-up this Scheme, so that responsibility can be officially transferred to Aviva, rather than being in the name of the Trustees. The Trustees believe that this will be completed by 31st January 2013.

Intangible fixed assets

The purchase by Edinburgh Business School of Author Royalty Rights have been capitalised and are being written down over a period of 4 years, the expected economic life of the courses.

Tangible fixed assets

Land & Buildings

Freehold land is not depreciated.

Buildings are included in the balance sheet at historical cost and are depreciated on a straight line basis over their expected useful economic life as follows:

External fabric	50 years
Internal fabric	35 years
Mechanical & engineering	20 years

Where land and buildings are acquired or built with the aid of specific grants they are capitalised and depreciated as above.

Costs incurred after the initial purchase are capitalised to the extent that they increase the expected future benefits to the group from the existing asset beyond its previously assessed standard of performance; the cost of such enhancements being added to the gross carrying amount of the asset concerned.

NOTES TO THE ACCOUNTS

For the year ending 31st July 2012

Acquisition with the aid of specific grants

Where tangible fixed assets are acquired with the aid of specific grants, they are capitalised and depreciated as above. The related grants are credited to a deferred capital grant account and are released to the income and expenditure account over the expected useful economic life of the related asset on a basis consistent with the depreciation policy.

Investments

Listed investments held as fixed assets or endowment funds are shown at market value. Investments in subsidiary undertakings are shown at the lower of cost or net realisable value and investments in associates are shown in the consolidated balance sheet at attributable share of net assets.

Current asset investments, which may include listed investments, are shown at the lower of cost and net realisable value.

Stock

Stocks are stated at the lower of their cost and net realisable value. Where necessary, provision is made for obsolete, slow-moving and defective stocks.

Cash flows and liquid resources

Cash flows comprise increases or decreases in cash. Cash includes cash in hand, cash at bank and money market deposits. No other investment, however liquid, is included as cash.

Foreign currency translation

Assets and liabilities denominated in foreign currencies are translated at the rate of exchange ruling at the end of the financial year, with all resulting exchange differences being taken to the income and expenditure account in the period in which they arise.

Research grants and contracts

Income from grants for sponsored research is included only to the extent of direct and indirect expenditure incurred on each project during the year.

Expenditure is written off in the year in which it is incurred except for equipment costing more than £20,000 which is capitalised in accordance with the group's capitalisation policy.

Other income received in advance is included in the balance sheet within creditors: amounts falling due within one year.

Charitable donations

Endowment funds

All charitable donations received are accounted for as follows:

- Restricted expendable: both the capital and the income elements are retained on the balance sheet until they are expended for the purpose specified by the donor.
- Restricted permanent: both the capital and the income elements are retained on the balance sheet, the capital element on a permanent basis and the income element until it is expended for the purpose specified by the donor
- Unrestricted expendable: recognised as a donation in the income and expenditure account in the year received.

Donations for fixed assets

Donations received to be applied to the cost of a tangible fixed asset are shown on the balance sheet as a deferred capital grant. The deferred capital grant is released to the income and expenditure account over the same estimated useful life that is used to determine the depreciation charge associated with the tangible fixed asset.

NOTES TO THE ACCOUNTS

For the year ending 31st July 2012

Provisions

Provisions are recognised when the group has a present legal or constructive obligation as a result of a past event, it is probable that a transfer of economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

Gift Aid

Gift Aid payments and receipts are recognised in the income and expenditure account in the year in which they are made.

Financial instruments

Financial assets

Classification

The University classifies its financial assets in the following categories: at fair value, 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 the income and expenditure account

Financial assets at fair value through the income and expenditure account comprise derivatives. Assets in this category are classified as current assets. The University does not trade in derivatives and does not apply hedge accounting.

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, which are classified as non-current assets. Loans and receivables comprise trade and other receivables and cash at bank and in hand in the balance sheet.

c) Available-for-sale financial assets

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.

Recognition and measurement

Financial assets are recognised when the University becomes party to the contractual provisions of the financial instrument. Financial assets are derecognised when the rights to receive cash flows from the asset have expired or have been transferred and the University has transferred substantially all risks and rewards of ownership.

a) Financial assets at fair value through surplus or deficit

Financial assets carried at fair value are initially recognised at fair value, and transaction costs are expensed in the income and expenditure account. Financial assets carried at fair value are subsequently measured at fair value. Gains or losses arising from changes in the fair value are presented in the income and expenditure account.

b) Loans and receivables

Loans and receivables 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 loans and receivables is established when there is objective evidence that the University will not be able to collect all amounts due according to the original terms of the receivables. 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 loan and receivable is impaired.

NOTES TO THE ACCOUNTS

For the year ending 31st July 2012

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. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in the income and expenditure account. When a loan or receivable is uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited in the income and expenditure account.

c) Available-for-sale financial assets

Available-for-sale financial assets are initially recognised and subsequently carried at fair value. Changes in the fair value of financial assets classified as available for sale are recognised in reserves. When financial assets classified as available for sale are sold or impaired, the accumulated fair value adjustments recognised in reserves are included in the income and expenditure account.

Investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are measured at cost less impairment.

The University assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. 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 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 impairment loss on that financial asset previously recognised in the income and expenditure account – is removed from reserves and recognised in the income and expenditure account. Impairment losses recognised in the income and expenditure account on equity instruments are not reversed through the income and expenditure account.

Financial Liabilities

Classification

The University classifies its financial liabilities in the following categories: at fair value through surplus or deficit, and other financial liabilities. The classification depends on the purpose for which the financial liabilities were issued. Management determines the classification of its financial liabilities at initial recognition.

a) Financial liabilities at fair value

Financial liabilities at fair value comprise derivatives. Liabilities in this category are classified as current liabilities. The University does not trade in derivatives and does not apply hedge accounting.

b) Other financial liabilities

Other financial liabilities are included in current liabilities, except for maturities greater than 12 months after the balance sheet date. These are classified as non-current liabilities. The University's other financial liabilities comprise trade and other payables in the balance sheet.

NOTES TO THE ACCOUNTS

For the year ending 31st July 2012

Recognition and measurement

Financial liabilities are recognised when the University becomes party to the contractual provisions of the financial instrument. A financial liability is removed from the balance sheet when it is extinguished, that is when the obligation is discharged, cancelled or expired.

a) Financial liabilities at fair value

Financial liabilities carried at fair value are initially recognised at fair value, and transaction costs are expensed in the income and expenditure account. Financial liabilities carried at fair value are subsequently measured at fair value. Gains or losses arising from changes in the fair value are presented in the income and expenditure account.

b) Other financial liabilities

Other financial liabilities are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

2. Funding Body Grants

	<i>Group</i>	
	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>
Recurrent teaching grant	22,063	24,321
Recurrent research grant	13,484	13,771
LTIF grants	759	54
CIF grants	572	2,765
Release of deferred capital grants	1,303	2,039
Other grants	393	514
	<u>38,574</u>	<u>43,464</u>

3. Tuition Fees and Education Contracts

	<i>Group</i>	
	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>
UK Higher education students	10,379	9,967
European Union students (ex. UK)	3,224	2,721
Non-European Union students	38,623	32,420
Higher education contracts	10,837	10,091
Research training support grants	6,159	5,112
Short course fees	608	713
Examination and graduation fees	3,204	3,050
	<u>73,034</u>	<u>64,074</u>

4. Research Grants and Contracts

	<i>Group</i>	
	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>
Research councils	11,055	11,447
Charities	849	737
UK government	841	1,454
UK industry	3,243	3,046
EU Commission	2,626	2,061
Other sources	4,134	2,472
	<u>22,748</u>	<u>21,217</u>

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

5. Other Income

	<i>Group</i>	
	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>
Residences, catering and conferences	13,584	13,635
Income from governments and other funding bodies	4,852	4,232
Donations	541	610
Release of deferred capital grants	398	473
Other income, including foreign currency gains	1,404	817
	<u>20,779</u>	<u>19,767</u>

6. Endowment and Investment Income

	<i>Group</i>	
	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>
Income from specific endowment assets	241	284
Other investment income	-	1,296
Other interest receivable	271	257
	<u>512</u>	<u>1,837</u>

7. Staff Costs

	<i>Group</i>	
	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>
Wages and salaries	60,122	58,592
Voluntary severance	485	1,152
Social security costs	4,796	4,588
Other pension costs	11,733	10,881
	<u>77,136</u>	<u>75,213</u>

Analysed between:

	<i>Group</i>	
	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>
Academic	38,842	37,480
Academic teaching support services	18,143	18,088
Administrative & central services	11,613	10,913
Premises	4,941	4,874
Catering and residences	3,597	3,858
	<u>77,136</u>	<u>75,213</u>

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

At the year-end the number of persons employed by the group, expressed as full-time equivalents, was:

	<i>2012</i>	<i>2011</i>
	<i>Number</i>	<i>Number</i>
Academic	663	642
Academic teaching support services	439	438
Administrative & central services	278	254
Premises	148	141
Catering and residences	116	136
	<u>1,644</u>	<u>1,611</u>

The number of staff who received emoluments in the following ranges was:

	<i>2012</i>	<i>2011</i>
	<i>Number</i>	<i>Number</i>
£70,001 - £80,000	34	34
£80,001 - £90,000	22	14
£90,001 - £100,000	8	10
£100,001 - £110,000	6	6
£110,001 - £120,000	5	5
£120,001 - £130,000	3	4
£130,001 - £140,000	2	1
£140,001 - £150,000	2	2
£150,001 - £160,000	-	-
£160,001 - £170,000	1	1
	<u>83</u>	<u>77</u>

The above emoluments include amounts payable to the Principal by Heriot-Watt University of:

	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>
Salary	162	162
Benefits in kind	7	13
	<u>169</u>	<u>175</u>
Pension contributions	<u>38</u>	<u>36</u>

The pension contributions are in respect of the Universities Superannuation Scheme (USS) and are paid at the same rate as for other employees.

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

8. Other Operating Expenses

	<i>Group</i>	
	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>
Other operating expenses include:		
* External auditor's remuneration - audit	58	43
External auditor's remuneration – non-audit services	151	51
** Internal auditors' remuneration	62	62
Hire of other assets - operating leases - other	270	293

* Inc. £40,000 (2011: £32,000) for Heriot-Watt University

** Inc. £62,000 (2011: £62,000) for Heriot-Watt University

9. Interest and Other Finance Costs

	<i>Group</i>	
	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>
Net return on pension assets	(122)	83
On bank loans: repayable within 5 years, by instalments	-	-
On bank loans: repayable wholly or partly in more than 5 years	1,079	1,333
	<u>957</u>	<u>1,416</u>

10. Taxation

The taxation charge for the year relates to Singapore Withholding Tax charged on work carried out by an Accredited Learning Partner on behalf of the Group and a tax charge on bank interest received by Heriot Watt Malaysia.

11. Tangible Fixed Assets

	<i>Land & Buildings</i>	<i>Equipment</i>	<i>Work In Progress</i>	<i>Total</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
Group				
Cost				
At 1 August 2011	141,178	33,606	14,254	189,038
Additions	-	-	31,244	31,244
Transfers	3,555	8,845	(12,400)	-
Disposals	-	(260)	-	(260)
At 31 July 2012	<u>144,733</u>	<u>42,191</u>	<u>33,098</u>	<u>220,022</u>
Depreciation				
At 1 August 2011	59,222	25,375	-	84,597
Charge for year	3,681	3,744	-	7,425
Transfers	-	-	-	-
Disposals	-	(260)	-	(260)
At 31 July 2012	<u>62,903</u>	<u>28,859</u>	<u>-</u>	<u>91,762</u>

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

Net Book Value

At 31 July 2012	81,830	13,332	33,098	128,260
At 1 August 2011	81,956	8,231	14,254	104,441

Analysed between:

	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
Funded by capital grants	43,607	5,101	-	48,708
Own funded	38,223	8,231	33,098	79,552
At 31 July 2012	81,830	13,332	33,098	128,260

The land and buildings of Heriot-Watt Sports Village Ltd are subject to a first standard security in respect of the grants received from **sportscotland**.

Included in cost for the group is £33,098,000 (2011: £14,254,000) relating to assets in the course of construction, of which £26,653,000 (2011: £8,117,000) relates to freehold land and buildings and £6,445,000 (2011: £6,137,000) relates to equipment.

	<i>Land & Buildings £000</i>	<i>Equipment £000</i>	<i>Work In Progress £000</i>	<i>Total £000</i>
University				
Cost				
At 1 August 2011	135,054	32,763	13,150	180,967
Additions	-	-	30,823	30,823
Transfers	3,234	8,768	(12,002)	-
Disposals	-	(260)	-	(260)
At 31 July 2012	138,288	41,271	31,971	211,530
Depreciation				
At 1 August 2011	58,015	24,846	-	82,861
Charge for year	3,488	3,648	-	7,136
Transfers	-	-	-	-
Disposals	-	(260)	-	(260)
At 31 July 2012	61,503	28,234	-	89,737
Net Book Value				
At 31 July 2012	76,785	13,037	31,971	121,793
At 1 August 2011	77,039	7,917	13,150	98,106

Analysed between:

	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
Funded by capital grants	42,103	5,065	-	47,168
Own funded	34,682	7,972	31,971	74,625
At 31 July 2012	76,785	13,037	31,971	121,793

The net book value of the University's tangible fixed assets funded by capital grants includes £5,911,000 (2011: £7,132,000) in cash received for assets either under construction or in the course of being purchased as at the year-end date.

NOTES TO THE ACCOUNTS

For the year ending 31st July 2012

Included in cost for the University is £31,971,000 (2011: £13,150,000) relating to assets in the course of construction, of which £25,526,000 (2011: £7,030,000) relates to freehold land and buildings and £6,445,000 (2011: £6,120,000) relates to equipment.

12. Intangible Fixed Assets

	<i>Group</i>	
	<i>Royalties</i> £000	<i>Total</i> £000
Cost		
At 1 August 2011	200	200
Additions	-	-
Disposals	-	-
At 31 July 2012	<u>200</u>	<u>200</u>
Amortisation		
At 1 August 2011	79	79
Charge for year	50	50
At 31 July 2012	<u>129</u>	<u>129</u>
Net Book Value		
At 31 July 2012	<u>71</u>	<u>71</u>
At 1 August 2011	<u>121</u>	<u>121</u>

13. Investments

	<i>Group</i>		<i>University</i>	
	<i>2012</i> £000	<i>2011</i> £000	<i>2012</i> £000	<i>2011</i> £000
Term deposit account (3yrs)	5,000	-	-	-
Term deposit account (1yr)	2,000	-	-	-
Investment in subsidiary companies at cost	-	-	9,163	5,005
Minority investments in unquoted companies	45	45	45	45
	<u>7,045</u>	<u>45</u>	<u>9,208</u>	<u>5,050</u>

Minority investments in unquoted companies include investments made by the group in spin-out companies, which are stated at cost. Term deposit account investments are held with Royal Bank of Scotland and Bank of Scotland. The 2012 University investment in subsidiary companies amount includes the cost of the investment in Heriot-Watt University Malaysia Sdn Bhd

14. Subsidiary Undertakings

	Number of shares	Percentage owned
The group has major shareholdings in ordinary shares in the following companies incorporated in Scotland:		
Edinburgh Business School (Limited by Guarantee)	-	100%
¹ Edinburgh Conference Centre Limited	100	100%
¹ Heriot-Watt Services Limited	100	100%

NOTES TO THE ACCOUNTS

For the year ending 31st July 2012

Heriot-Watt Sports Village Limited	5,000,100	100%
Heriot-Watt Trading Limited	5,000	100%
¹ Scottish College of Textiles Limited	6	100%
² SISTech Limited	1000	50%

The group also has a majority shareholding in the following overseas business:

	Number of shares	Percentage owned
Heriot-Watt University Malaysia Sdn Bhd	20,000,000	100%

The consolidated financial statements of the group include the transactions of the above companies, with the exception of those marked below.

- ¹ These companies are dormant.
² For SISTech Limited the figures are not consolidated as they are deemed to be insignificant.

15. Endowment Assets

	<i>Group</i>		<i>University</i>	
	<i>2012</i>	<i>2011</i>	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
Balance at 1 August	8,664	6,737	7,351	5,531
(Decrease)/ increase/ in cash balances held	(819)	1,554	(819)	1,554
Appreciation of endowment asset investments	1,248	373	1,257	266
Balance at 31 July	<u>9,093</u>	<u>8,664</u>	<u>7,789</u>	<u>7,351</u>
Represented by:				
Equities (listed)	6,926	5,679	5,622	4,366
Cash balances	2,167	2,985	2,167	2,985
	<u>9,093</u>	<u>8,664</u>	<u>7,789</u>	<u>7,351</u>

16. Debtors

	<i>Group</i>		<i>University</i>	
	<i>2012</i>	<i>2011</i>	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
Amounts falling due within one year:				
Trade debtors	10,576	6,897	7,635	4,704
Research debtors	9,356	9,031	9,356	9,031
Other debtors	47	328	47	-
Loans by parent undertakings	-	-	3,239	-
Amounts owed by group undertakings	-	-	5,822	653
Prepayments and accrued income	7,010	6,289	5,658	5,781
	<u>26,989</u>	<u>22,545</u>	<u>31,757</u>	<u>20,169</u>

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

Amounts falling due after more than one year:

Prepayments and accrued income	3,529	3,800	3,529	3,800
	<u>30,518</u>	<u>26,345</u>	<u>35,286</u>	<u>23,969</u>

Included in prepayments and accrued income is £3,529,000 (2011: £3,800,000) due after more than one year which constitutes deemed consideration received by Heriot-Watt University from Borders College for the sale of its Galashiels site to the College in return for 17.5 years rent-free occupation of part of the site, commencing from the 1st February 2008, the practical completion date for the redevelopment of the site.

	<i>Group</i>		<i>University</i>	
	<i>2012</i>	<i>2011</i>	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
Trade debt provision				
At 1 August	1,780	1,261	1,726	1,261
Provided for during the year	479	1,422	452	1,302
Utilised during the year	(391)	(903)	(377)	(837)
At 31 July	<u>1,868</u>	<u>1,780</u>	<u>1,801</u>	<u>1,726</u>

At 31st July 2012 debtors with a carrying value of £5,780,000 (2011: £3,149,000) were impaired and provided for. The basis used to assess underlying trade debt balances was enhanced during 2012, and credit balances relating to advanced payments were fully identified and reclassified as income in advance. This has resulted in an increase in trade debtors carrying value. There has been no significant change in the underlying value of trade debt, its profile or default risk on the previous year. The amount of the provision was £1,868,000 (2011: £1,780,000). The ageing of these debtors is as follows:

	<i>Group</i>		<i>University</i>	
	<i>2012</i>	<i>2011</i>	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
Less than 3 months past due	-	39	-	39
Between 3 to 6 months past due	-	29	-	29
Over 6 months past due	5,780	3,081	5,552	2,942
	<u>5,780</u>	<u>3,149</u>	<u>5,552</u>	<u>3,010</u>

The debtors assessed as individually impaired comprises student and commercial customers of £4,576,000 (2011: £2,343,000) and research customers of £1,204,000 (2011: £806,000) with whom it is judged there is an increased risk of default due to the age of the individual debts concerned.

Debtors that are less than three months past their due date, except those specifically provided for, are not considered impaired. As at 31st July 2012 debtors with a carrying value of £1,204,000 (2011: £2,554,000) were past their due date but not impaired. The ageing of debtors which are past their due date but not impaired is as follows:

	<i>Group</i>		<i>University</i>	
	<i>2012</i>	<i>2011</i>	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
Less than 3 months past due	1,274	2,554	735	2,165
Between 3 to 6 months past due	-	-	-	-
Over 6 months past due	-	-	-	-
	<u>1,274</u>	<u>2,554</u>	<u>735</u>	<u>2,165</u>

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

The debtors assessed as past due but not impaired primarily relate to balances due from student and commercial customers of £1,174,000 (2011: £1,775,000) and research customers of £100,000 (2011: £779,000) with which there is no history of default recently.

All debtors are denominated in GB pounds. The carrying amount of short term receivables approximates their fair value. The effective interest rate on non-current debtors is nil.

17. Creditors: Amounts Falling Due Within One Year

	<i>Group</i>		<i>University</i>	
	<i>2012</i>	<i>2011</i>	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
Bank loans	-	6,000	-	6,000
Amounts owed to subsidiary undertakings	-	-	6,636	67
Grants in advance for research	19,859	15,792	19,859	15,792
Grants in advance from SFC	6,670	8,108	6,670	8,108
Other creditors	606	48	420	22
Trade creditors	2,599	2,936	2,223	2,845
Other taxation and social security	463	3,431	2,080	3,214
Accruals and deferred income	24,280	19,988	18,953	17,802
	<u>54,477</u>	<u>56,303</u>	<u>56,841</u>	<u>53,850</u>

All creditors are denominated in GB pounds. The carrying amount of short term payables approximates their fair value. The effective interest rate on non-current creditors, except bank loans, is nil.

18. Creditors: Amounts Falling Due After More Than One Year

	<i>Group</i>		<i>University</i>	
	<i>2012</i>	<i>2011</i>	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
Bank loans	40,500	20,000	40,500	20,000
Deferred income	4,941	5,287	3,536	3,800
Amounts owed to subsidiary undertakings	-	-	5,000	-
Other creditors	181	181	129	129
	<u>45,622</u>	<u>25,468</u>	<u>49,165</u>	<u>23,929</u>

The above loans are repayable as follows:

In one year or less (note 16)		6,000		6,000
		6,000		6,000
Between one and two years		-		-
Between two and five years		-		-
In five years or more	40,500	20,000	40,500	20,000
	<u>40,500</u>	<u>20,000</u>	<u>40,500</u>	<u>20,000</u>
	<u>40,500</u>	<u>26,000</u>	<u>40,500</u>	<u>26,000</u>

NOTES TO THE ACCOUNTS

For the year ending 31st July 2012

The University has in place a committed revolving credit facility against which drawings of £20 million (2011: £26 million) had been made. Of this, £20 million is regarded as representing a balance falling due after more than one year and is matched by long-term fixed rate interest swaps which mature between 2016 and 2037 at rates of between 5.05% and 5.62%. The University also has a £25m loan facility with Clydesdale Bank of which £20.5m was drawn down at 31 July 2012.

19. Provisions For Liabilities And Charges

	<i>Group and University</i>	
	<i>Pensions</i>	<i>Total</i>
	<i>£000</i>	<i>£000</i>
At 1 August 2011	599	599
Provided for during the year	17	17
Utilised during the year	(35)	(35)
At 31 July 2012	<u>581</u>	<u>581</u>
To be spent before 31 July 2013	<u>36</u>	<u>36</u>

20. Deferred Capital Grants

	<i>Funding</i>	<i>Other</i>	<i>Total</i>
	<i>Council</i>	<i>Grants</i>	<i>Total</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>
Group			
At 1 August 2011			
Buildings	25,243	11,224	36,467
Equipment	2,700	1,964	4,664
Total	<u>27,943</u>	<u>13,188</u>	<u>41,131</u>
Cash Received			
Buildings	3,226	-	3,226
Equipment	-	2,310	2,310
Total	<u>3,226</u>	<u>2,310</u>	<u>5,536</u>
Released to Income and Expenditure			
Buildings	(1,303)	(693)	(1,996)
Equipment	(406)	(1,467)	(1,873)
Total	<u>(1,709)</u>	<u>(2,160)</u>	<u>(3,869)</u>
At 31 July 2012			
Buildings	27,166	10,531	37,697
Equipment	2,295	2,806	5,101
Total	<u>29,461</u>	<u>13,337</u>	<u>42,798</u>

Cash received of £5,911,000 (2011: £7,132,000) is excluded from deferred capital grants and disclosed in creditors falling due within one year as it relates to grants received for which the matching tangible fixed asset was either still being constructed and/or was in the course of being purchased as at the yearend date and so had not been capitalised.

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

Deferred Capital Grants (continued)

University	<i>Funding Council £000</i>	<i>Other Grants £000</i>	<i>Total £000</i>
At 1 August 2011			
Buildings	25,190	9,724	34,914
Equipment	2,700	1,905	4,605
Total	27,890	11,629	39,519
Cash Received			
Buildings	3,226	-	3,226
Equipment	-	2,310	2,310
Total	3,226	2,310	5,536
Released to Income and Expenditure			
Buildings	(1,301)	(645)	(1,946)
Equipment	(406)	(1,446)	(1,852)
Total	(1,707)	(2,091)	(3,798)
At 31 July 2012			
Buildings	27,115	9,079	36,194
Equipment	2,294	2,769	5,063
Total	29,409	11,848	41,257

21. Endowments

	<i>Group</i>			<i>University</i>		
	<i>Restricted Expendable £000</i>	<i>Restricted Permanent £000</i>	<i>Total £000</i>	<i>Restricted Expendable £000</i>	<i>Restricted Permanent £000</i>	<i>Total £000</i>
At 1 August 2011	2,389	6,275	8,664	2,389	4,962	7,351
Additions	435	22	457	435	22	457
Appreciation	(31)	1,279	1,248	(31)	1,288	1,257
Income for year	39	202	241	39	135	174
Expenditure for the year	(272)	(1,245)	(1,517)	(272)	(1,178)	(1,450)
At 31 July 2012	2,560	6,533	9,093	2,560	5,229	7,789
	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
At 1 August 2010	2,200	4,537	6,737	2,200	3,331	5,531
Additions	558	1,408	1,966	558	1,408	1,966
Appreciation	67	306	373	68	197	265
Income for year	40	179	219	40	114	154
Expenditure for the year	(476)	(155)	(631)	(477)	(88)	(565)
At 31 July 2011	2,389	6,275	8,664	2,389	4,962	7,351

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

22. Restricted Funds

	<i>Group</i>		<i>University</i>	
	<i>2012</i>	<i>2011</i>	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
Balance at 1 August	-	87	-	-
Additions	2	12	-	-
Expenditure in the year	-	(99)	-	-
Balance at 31 July	<u>2</u>	<u>-</u>	<u>-</u>	<u>-</u>

23. Investment Reserve

	<i>Group</i>		<i>University</i>	
	<i>2012</i>	<i>2011</i>	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
Balance at 1 August	-	959	-	-
Revaluation for the year	-	(959)	-	-
Balance at 31 July	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>

24. Income and Expenditure Account including Pension Reserve

	<i>Group</i>		<i>University</i>	
	<i>2012</i>	<i>2011</i>	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
Balance at 1 August	18,942	10,854	5,297	611
Net surplus retained for the year	6,389	5,517	5,345	2,157
Transfer (to)/from reserves	(6,457)	2,571	(6,376)	2,529
Balance at 31 July	<u>18,874</u>	<u>18,942</u>	<u>4,266</u>	<u>5,297</u>

	<i>Group</i>	
	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>
The net surplus retained for the year is analysed as follows:		
University surplus	3,853	707
Gift Aid from subsidiaries	1,489	1,450
Surplus retained by subsidiaries	1,047	3,360
	<u>6,389</u>	<u>5,517</u>

Reconciliation:

	<i>Group</i>		<i>University</i>	
	<i>2012</i>	<i>2011</i>	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
Income and expenditure reserve	36,559	30,791	21,826	17,067
Pension reserve	(17,685)	(11,849)	(17,560)	(11,770)
Balance at 31 July	<u>18,874</u>	<u>18,942</u>	<u>4,266</u>	<u>5,297</u>

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

Income and Expenditure Account including Pension Reserve (continued)

Represented by:

	<i>Group</i>		<i>University</i>	
	<i>2012</i> <i>£000</i>	<i>2011</i> <i>£000</i>	<i>2012</i> <i>£000</i>	<i>2011</i> <i>£000</i>
Income and expenditure account				
At 1 August	30,791	25,848	17,067	15,458
Surplus for the year	6,389	5,517	5,345	2,157
Transfer to pension reserve	(621)	(574)	(586)	(548)
At 31 July	<u>36,559</u>	<u>30,791</u>	<u>21,826</u>	<u>17,067</u>
	<i>Group</i>		<i>University</i>	
	<i>2012</i> <i>£000</i>	<i>2011</i> <i>£000</i>	<i>2012</i> <i>£000</i>	<i>2011</i> <i>£000</i>
Pension Reserve				
Deficit at 1 August	(11,849)	(14,994)	(11,770)	(14,847)
Current service cost	(2,277)	(2,232)	(2,225)	(2,181)
Employer contributions	2,869	2,883	2,794	2,813
Contributions in respect of unfunded benefits	14	16	14	16
Curtailments and settlements	(82)	-	(82)	-
Past service cost	(37)	(17)	(37)	(17)
Net return on assets	134	(76)	122	(83)
Actuarial (losses)/gains	(6,457)	2,571	(6,376)	2,529
Deficit at 31 July	<u>(17,685)</u>	<u>(11,849)</u>	<u>(17,560)</u>	<u>(11,770)</u>

25. Reconciliation Of Surplus Before Tax To Net Cash Inflow From Operating Activities

	<i>Group</i>	
	<i>2012</i> <i>£000</i>	<i>2011</i> <i>£000</i>
<u>Income & expenditure</u>		
Surplus on continuing operations after depreciation & disposal of assets and taxation	5,114	5,004
Restricted funds	(2)	87
Interest receivable	(271)	(257)
Interest payable	957	1,416
Taxation	229	(4)
	<u>6,027</u>	<u>6,246</u>
<u>Fixed assets & deferred capital grants</u>		
Depreciation of tangible fixed assets	7,425	6,366
Profit on disposal of tangible fixed assets	(25)	(15)
Amortisation of intangible fixed assets	50	50
Deferred capital grants released to income	(3,869)	(3,593)
Transfer from deferred capital grants to creditors	(1,221)	(4,736)
	<u>2,360</u>	<u>(1,928)</u>

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

Endowments & pensions

Transfer from accumulated income to specific endowments	1,277	426
Transfer from accumulated income to restricted funds	(2)	87
Pension income	(621)	(574)
	<u>654</u>	<u>(61)</u>

Working capital

(Increase)/decrease in fixed asset investments	(5,000)	5,433
(Increase) in short term investments	(2,000)	-
Increase in stocks	77	(54)
Increase in debtors	(4,173)	(3,645)
Increase in creditors	5,051	2,427
(Decrease) /Increase in provisions	(18)	20
	<u>(6,063)</u>	<u>4,181</u>

Reserves

Increase/(Decrease) in restricted funds	2	(87)
(Decrease) in investment reserve	-	(959)
	<u>2</u>	<u>(1,046)</u>

Net Cash Inflow from Operating Activities	<u>2,980</u>	<u>7,392</u>
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26. Returns On Investment And Servicing Of Finance

	<i>Group</i>	
	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>
Income received on specific endowments	241	219
Expenditure paid on specific endowments	(1,517)	(632)
Interest received	271	257
Income received on restricted funds	-	12
Expenditure paid on restricted funds	-	(99)
Interest paid	(957)	(1,416)
Taxation paid	(229)	-
Net Cash Outflow from Returns on Investment and Servicing of Finance	<u>(2,191)</u>	<u>(1,659)</u>

27. Capital Expenditure And Financial Investment

	<i>Group</i>	
	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>
Purchase of tangible fixed assets	(31,244)	(7,534)
Proceeds on disposal of tangible fixed assets	25	25
Increase/(decrease) in endowment cash balances	819	(1,554)
Deferred capital grants received	5,536	5,887
Endowments received	457	1,966
Net Cash Outflow from Capital Expenditure and Financial Investment	<u>(24,407)</u>	<u>(1,210)</u>

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

28. Financing

	<i>Group</i>	
	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>
New amounts drawn down	20,500	6,000
Repayment of amounts borrowed	(6,000)	-
Net Cash Inflow from Financing	<u>14,500</u>	<u>6,000</u>

29. Analysis Of Changes In Net (Debt) / Funds

	<i>At</i>			<i>At</i>
	<i>1 August</i>	<i>Cash</i>	<i>Non-cash</i>	<i>31 July</i>
	<i>2011</i>	<i>Flows</i>	<i>Changes</i>	<i>2012</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
Cash at bank and in hand	23,256	(9,118)	-	14,138
	<u>23,256</u>	<u>(9,118)</u>	<u>-</u>	<u>14,138</u>
Debts due within one year	(6,000)	-	6,000	-
Debts due after one year	(20,000)	(14,500)	(6,000)	(40,500)
	<u>(2,744)</u>	<u>(23,618)</u>	<u>-</u>	<u>(26,362)</u>

Had the cash held under endowment asset investments been included above, the net debt movement would have been £24,436,000 (2011: cash inflow £6,077,000) with net debt at 31 July 2012 of £24,195,000 (2011: net cash £241,000). However, to reflect more accurately the restricted nature of the cash held for endowments the group considers the exclusion of this cash from the above figures gives a fairer view of the group's net debt.

30. Pension Schemes

The total pension charge in the financial statements reflects the costs incurred by the group during the year of £11,733,000 (2011 - £10,881,000).

	<i>Group</i>	
	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>
The total pension charge is analysed as follows:		
Universities Superannuation Scheme	9,180	8,591
Lothian Pension Fund	2,467	2,194
Scottish Teachers Superannuation Scheme	86	96
Supplementary Pension Scheme	-	-
	<u>11,733</u>	<u>10,881</u>

The pension costs are assessed in accordance with the advice of independent qualified actuaries using the projected unit method. The latest actuarial valuations of the USS and Lothian Pension Fund (LPF) schemes were on 31st March 2012, of the Scottish Teachers Superannuation Scheme on 31st March 2005 and of the Supplementary Pension Scheme (SPS) on 31st July 2004.

In accordance with FRS17 'Retirement Benefits' the total pension charges disclosed for both LPF and the SPS are the current service cost which represents the increase in the present value of the schemes' liabilities expected to arise from employee service in the current year.

NOTES TO THE ACCOUNTS

For the year ending 31st July 2012

Universities Superannuation Scheme

Heriot-Watt participates in the Universities Superannuation Scheme (USS), a defined benefit scheme which is contracted out of the State Second Pension (S2P). The assets of the scheme are held in a separate fund administered by the trustee, Universities Superannuation Scheme Limited.

The appointment of directors to the board of the trustee is determined by the company's Articles of Association. Four of the directors are appointed by Universities UK; three are appointed by the University and College Union, of whom at least one must be a USS pensioner member; one is appointed by the Higher Education Funding Councils; and a minimum of two and a maximum of four are co-opted directors appointed by the board. Under the scheme trustee deed and rules, the employer contribution rate is determined by the trustee, acting on actuarial advice.

The latest triennial actuarial valuation of the scheme was at 31st March 2011 and was carried out using the projected unit method.

This was the second valuation for USS under the new scheme-specific funding regime introduced by the Pensions Act 2004, which requires schemes to adopt 'a statutory funding objective', which is to have sufficient and appropriate assets to pay its benefits as they fall due (the technical provisions).

The actuary also carries out a review of the funding level each year between triennial valuations and details of his estimate of the funding level at 31st March 2012 are also included in this note.

The assumptions which have the most significant effect on the result of the valuation are those relating to the rate of return on investments, the rates of increase in salary and pensions and the assumed rates of mortality.

The financial assumptions used were derived from market yields prevailing at the valuation date. An "inflation risk premium" adjustment was also included by deducting 0.3% from the market-implied inflation on account of the historically high level of inflation implied by government bonds (particularly when compared to the Bank of England's target of 2% for CPI, which corresponds broadly to 2.75% for RPI per annum).

To calculate the technical provisions, it was assumed that the valuation rate of interest would be 6.1% per annum, salary increases would be 4.4% per annum (with short-term general pay growth at 3.65 per annum and an additional allowance for increases in salaries due to age and promotion reflecting historic scheme experience, with further cautionary reserve on top for past service liabilities) and pensions would increase by 3.4% per annum for 3 years following the valuation, then 2.6% per annum thereafter.

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

The standard mortality tables were used as follows:

Male members' mortality	SINA ("light") year of birth tables
Female members' mortality	SINA ("light") year of birth tables adjusted down for one year

The use of these mortality tables reasonably reflects the actual USS experience, but also provides an element of conservatism to allow for further improvements in mortality rates. The CMI 2009 projections with a 1.25% pa long term rate were also adopted. The assumed life expectations on retirement at age 65 are:

Males currently aged 65	23.7 years	Females currently aged 65	25.6 years
Males currently aged 45	25.5 years	Females currently aged 45	27.6 years

At the valuation date, the value of the assets of the scheme was £32,433 million and the value of the scheme's technical provisions was £35,343 million, indicating a shortfall of £2,910 million. The assets therefore were sufficient to cover 92% of the benefits which had accrued to members after allowing for expected future increases in earnings.

The actuary also valued the scheme on a number of other bases as the valuation date.

- On the scheme's historic gilts basis, using a valuation rate of interest in respect of past service liabilities of 4.4% per annum (the expected return on gilts), the funding level was approximately 68%.
- Under the Pension Protection Fund regulations, introduced by the Pensions Act 2004, the Scheme was 93% funded.
- On a buy-out basis (i.e. assuming the Scheme had discontinued on the valuation date) the assets would have been approximately 57% of the amount necessary to secure all the USS benefits with an insurance company.
- Using FRS 17, as if USS was a single employer scheme, and using an AA bond discount rate of 5.5% per annum, based on spot yields, the actuary estimated that the funding level was 82%.

As part of this valuation, the trustees have determined, after consultation with the employers, a recovery plan to pay off the shortfall by 31 March 2021. The next formal triennial actuarial valuation is at 31 March 2014. If experience up to that date is in line with the assumptions made for this current actuarial valuation and contributions are paid at the determined rates or amounts, the shortfall at 31 March 2014 is estimated to be £2.2 billion, equivalent to a funding level of 95%. The contribution rate will be reviewed as part of each valuation and may be reviewed more frequently.

NOTES TO THE ACCOUNTS

For the year ending 31st July 2012

The technical provisions relate, essentially, to the past service liabilities and funding levels, but it is also necessary to assess the on-going cost of newly accruing benefits.

The cost of future accrual was calculated using the same assumptions as those used to calculate the technical provisions but the allowance for promotional salary increases was not as high. Analysis has shown very variable levels of growth over and above general pay increases in recent years, and the salary growth assumption built into the cost of future accrual is based on more stable, historic, salary experience. However, when calculating the past service liabilities of the scheme, a cautionary reserve has also been included, on account of the variability mentioned above.

As at the valuation date the Scheme was still a Final Salary Scheme for future accruals and the prevailing employer contribution rate was 16% of Salaries.

Following UK government legislation, from 2011 statutory pension increases or revaluations are based on the Consumer price index measure of inflation. Historically, these increases had been based on the Retail Price Index.

Since the previous valuation (at 31 March 2008) there have been a number of changes to the benefits provided by the scheme although these became effective from October 2011. These include:

New Entrants

Other than in specific, limited circumstances, new entrants are now provided on a Career Revalued Benefits (CRB) basis rather than a Final salary (FS) basis

Normal pension age

The normal pension age was increased for future service and new entrants, to age 65.

Flexible Retirement

Flexible retirement options were introduced.

Member contributions increased

Contributions were uplifted to 7.5% p.a. and 6.5% p.a. for FS Section members and CRB Section members respectively.

Cost sharing

If the total contribution level exceeds 23.5% of Salaries per annum, the employers will pay 65% of the excess over 23.5% and members would pay the remaining 35% to the fund as additional contributions.

Pension increase cap

For service derived after 30 September 2011, USS will match increases in official pensions for the first 5%. If official pensions increase by more than 5% then USS will pay half of the difference up to a maximum increase of 10%.

Since 31 March 2011 global investment markets have continued to fluctuate and following its peak in September 2011 inflation has declined rapidly towards the year end, although the market's assessment of inflation has remained reasonably constant. The actuary has estimated that the funding level as at 31 March 2012 under the scheme specific funding regime had fallen from 92% to 77%. This estimate is based on the results from the valuation at 31 March 2011 allowing primarily for investment returns and changes to market conditions. These are sighted as the two most significant factors affecting the funding positions which have been taken into account for the 31 March 2012 estimation.

On the FRS17 basis, using an AA bond discount rate of 4.9% per annum based on spot yields, the actuary estimated that the funding level at 31 March 2011 was 74%. An estimate of the funding level measured on a buy-out basis at that date was approximately 56%

Surpluses or deficits which arise at future valuations may impact on the institution's future contribution commitment. A deficit may require additional funding in the form of higher contribution requirements, where a surplus could, perhaps, be used to similarly reduce contribution requirements. The sensitivities regarding

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

the principal assumptions used to measure the scheme liabilities on a technical provisions basis as at the last triennial valuation are set out below:

<i>Assumption</i>	<i>Change in assumption</i>	<i>Impact on shortfall</i>
Investment return	Decrease by 0.25%	Increase by £1.6 billion
The gap between RPI and CPI	Decrease by 0.25%	Increase by £1 billion
Rate of salary growth	Increase by 0.25%	Increase by £0.6 billion
Members live longer than assumed	1 year longer	Increase by £0.8 billion
Equity markets in isolation	Fall by 25%	Increase by £4.6 billion

USS is a “last man standing” scheme so that in the event of the insolvency of any of the participating employers in USS, the amount of any pension funding shortfall (which cannot otherwise be recovered) in respect of that employer will be spread across the remaining participant employers and reflected in the next actuarial valuation of the scheme.

The trustee believes that over the long-term equity investment and investment in selected alternative asset classes will provide superior returns to other investment classes. The management structure and targets set are designed to give the fund a major exposure to equities through portfolios that are diversified both geographically and by sector. The trustee recognises that it would be theoretically possible to select investments producing income flows broadly similar to the estimated liability cash flows. However, in order to meet the long-term funding objective within a level of contributions that it considers the employers would be willing to make, the trustee needs to take on a degree of investment risk relative to the liabilities. This taking of investment risk seeks to target a greater return than the matching assets would provide whilst maintaining a prudent approach to meeting the fund’s liabilities. Before deciding what degree of investment risk to take relative to the liabilities, the trustee receives advice from its internal investment team, its investment consultant and the scheme actuary, and considers the views of the employers. The positive cash flow of the scheme means that it is not necessary to realise investments to meet liabilities. The trustee believes that this, together with the on-going flow of new entrants into the scheme and the strength of the covenant of the employers enables it to take a long-term view of its investments. Short-term volatility of returns can be tolerated and need not feed through directly to the contribution rate although the trustee is mindful of the desirability of keeping the funding level on the scheme’s technical provisions close to or above 100% thereby minimizing the risk of the introduction of deficit contributions. The actuary has confirmed that the scheme’s cash flow is likely to remain positive for the next ten years or more.

The next formal triennial valuation is due as at 31st March 2014. The contribution rate will be reviewed as part of each valuation and may be reviewed more frequently.

The total contribution made for the year ended 31st July 2012 was £9,402,000 (2011: £8,793,000), of which employer’s contributions totalled £6,461,000 (2011: £6,295,000) and employee’s contributions totalled £2,941,000 (2011: £2,498,000).

The employer’s contributions include £89,839 (2011: £83,000) of outstanding contributions at the balance sheet date.

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

Lothian Pension Fund

A full actuarial valuation was carried out at 31st March 2011 by a qualified independent actuary.

The major assumptions used by the actuary were:

	<i>2012</i>	<i>2011</i>
Price increases	2.1%	2.7%
Salary increases	4.5%	5.0%
Pension increases	2.1%	2.7%
Discount rate	4.3%	5.3%

The assets in the scheme and the expected rate of return at the last actuarial review date were:

	<i>Long term rate of return % p.a.</i>	<i>Assets at 31 July 2012 £000</i>	<i>Long term rate of return % p.a.</i>	<i>Assets at 31 July 2011 £000</i>
Equities	5.5%	47,308	7.0%	48,988
Bonds	2.9%	5,529	4.6%	5,581
Property	3.7%	6,758	5.1%	6,201
Cash	2.8%	1,843	4.2%	1,240
Total		<u>61,438</u>		<u>62,010</u>

The following amounts represent Heriot-Watt University's share of the scheme at 31st July 2012 and were measured in accordance with the requirements of FRS 17:

Reconciliation of employer assets

	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>
At 1 August	62,010	54,502
Expected return on assets	4,063	3,695
Contributions by members	682	695
Contributions by employer	2,883	2,899
Benefits paid	(2,531)	(2,249)
Actuarial (losses)/gains	<u>(5,669)</u>	<u>2,468</u>
At 31 July	<u>61,438</u>	<u>62,010</u>

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

Pension Schemes (continued)

Reconciliation of present value of liabilities

	2012 £000	2011 £000
At 1 August	(73,859)	(69,496)
Current service cost	(2,277)	(2,232)
Interest cost	(3,929)	(3,771)
Contributions by members	(682)	(695)
Curtailements and settlements	(82)	-
Past service losses	(37)	(17)
Benefits paid	2,531	2,249
Actuarial (losses)/gains	(788)	103
At 31 July	<u>(79,123)</u>	<u>(73,859)</u>
Net pension liability	<u>(17,685)</u>	<u>(11,849)</u>

Analysis Of Amount Charged To Operating Profit

	2012 £000	2012 % of payroll	2011 £000	2011 % of payroll
Amount charged to operating profit				
Service cost	2,277	20.6%	2,232	19.45%
Past service (losses)	(37)	(0.3%)	(17)	(0.2)%
Total Operating Charge	<u>2,240</u>	20.3%	<u>2,215</u>	19.3%

Analysis Of Amount Credited To Other Finance Income

	2012 £000	2012 % of payroll	2011 £000	2011 % of payroll
Expected return on employer assets	4,063	32.2%	3,695	32.2%
Interest on pension scheme liabilities	(3,929)	(32.9)%	(3,771)	(32.9)%
Net Return	134	(0.6)%	(76)	(0.6)%

Analysis Of Amount Recognised In The Statement Of Total Recognised Gains And Losses (STRGL)

	2012 £000	2011 £000
Actual return less expected return on pension scheme assets	(5,669)	2,468
Experience (losses)/gains arising on the scheme liabilities	(788)	103
Actuarial gain in pension plan	<u>(6,457)</u>	<u>2,571</u>
Actuarial gain recognised in STRGL	<u>(6,457)</u>	<u>2,571</u>

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

Pension Schemes (continued)
Movement In Deficit During The Year

	2012 £000	2011 £000
Deficit at start of the year	(11,849)	(14,994)
Current service cost	(2,277)	(2,232)
Employer contributions	2,869	2,883
Contributions in respect of unfunded benefits	14	16
Curtailments and settlements	(82)	-
Past service losses	(37)	(17)
Net return on pension assets	134	(76)
Actuarial (losses)/gains	(6,457)	2,571
Deficit at end of the year	<u>(17,685)</u>	<u>(11,849)</u>

History Of Experience Gains And Losses

	2012 £000	2011 £000
Difference between expected and actual return on assets	(5,669)	2,468
Value of assets	61,438	62,010
<i>Percentage of assets</i>	(9.2%)	4.0%
Experience (losses) / gains on liabilities	(788)	103
Total present value of liabilities	79,123	73,859
<i>Percentage of the total present value of liabilities</i>	(1.0%)	-%
Actuarial (loss) / gain recognised in STRGL	(6,457)	2,571
Total present value of liabilities	79,123	73,859
<i>Percentage of the total present value of liabilities</i>	(8.2%)	3.5%

The total contribution made for the year ended 31st July 2012 was £3,719,000 (2011: £3,543,000), of which employer's contributions totalled £2,996,000 (2011: £2,861,000) and employee's contributions totalled £723,000 (2011: £682,000). The agreed contribution rates for future years are 25.9% (2011: 25.9%) for employers and 6.4% (2010: 6.4%) for employees. The employer's contributions include £287,000 (2011: £295,000) of outstanding contributions at the balance sheet date.

NOTES TO THE ACCOUNTS

For the year ending 31st July 2012

Scottish Teachers Superannuation Scheme

Heriot-Watt participates in the Scottish Teachers Superannuation Scheme (STSS), a defined benefit scheme which is contracted out of the State Second Pension (S2P). STSS operates on a notionally funded basis. The latest actuarial valuation of the scheme was at 31st March 2005 and was carried out using the prospective benefit method.

The 2005 actuarial valuation date was carried out using an approach known as 'superannuation contributions adjusted for past experience' (SCAPE). Using SCAPE, with effect from 1st April 2001, the notional investments will earn a real rate of return (in excess of price increases) specified by the Government Actuary. In addition, the Teachers Superannuation (Scotland) Amendment Act 2003 states that, for the purposes of the actuarial review as at 31st March 2005, the balance in the account at that date shall be such that the value of the scheme's assets equals the value of the scheme's liabilities.

The results of this valuation were rolled forward to give a liability of £24.37 million at 31st March 2010.

The assumptions used (to which the valuation results were particularly sensitive) are shown in the table below.

	<i>Valuation</i>
Real rate of return (discount rate)	4.6%
Real rate of return in excess of prices	1.8%
Real rate of return in excess of earnings	0.3%
Mortality for new members	PA92 tables rated down 2 years for males and 1 years for females
Mortality for existing & deferred members	PA92 tables rated down 1.5 years for males and 0.5 years for females
Mortality for existing pensioners	PMA 92 tables rated down 1 year for males

Surpluses or deficits which arise at future valuations may impact on Heriot-Watt's future contribution commitment. A deficit may require additional funding in the form of higher contributions, whereas a surplus could be used to reduce contribution requirements.

The total contribution made for the year ended 31st July 2012 was £126,000 (2011: £137,000), of which employer's contributions totalled £86,000 (2011: £96,000) and employee's contributions totalled £40,000 (2011: £41,000). The agreed contribution rates for future years are 14.9% (2011: 14.9%) for employers and 6.4% (2011: 6.4%) for employees. The employer's contributions include £10,000 (2011: £12,000) of outstanding contributions at the balance sheet date.

HWU Supplementary Pension Scheme

In May 2010, members were informed of the impending purchase of 'buy-in' annuities by an insurance company, with a date confirmed in June and the insurance company taking over pension payments in August 2010.

However, change in Government legislation, linking pension increases to CPI, during the 'buy-in' phase caused a delay in completing the 'buy-in' process. This was resolved in January 2012, and the scheme actuaries confirmed that the insurance company were now in a position to produce a revised final premium which could reflect CPI increases. The actuaries confirmed arrangements with the Scheme Trustees in February 2012. The Trustees confirmed their agreement to the 'buy in' at that time

At the date of these Accounts, the actuaries are in the process of informing the Regulator that we are now in a position to complete the 'buy-in' and then proceed to the 'buy-out' phase. The Regulators have confirmed that a valuation of the scheme is no longer required given the stage that the scheme is at in the 'buy-in/buy-out' process.

The 'buy- in' phase should be complete by December 2012 and 'buy out' phase should be complete with the notification of the Pensions Regulator and HMRC by January 2013.

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

31. Post Balance Sheet Events

There are no material post Balance Sheet events.

32. Capital Commitments

Provision has not been made for the following capital commitments at 31st July 2012:

	<i>Group</i>	
	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>
Commitments contracted	3,308	27,539
Authorised but not contracted	4,742	8,365
	<u>8,050</u>	<u>35,904</u>

33. Financial commitments

At 31st July 2012 there were annual commitments under non-cancellable operating leases as follows:

	<i>Group</i>	
	<i>2012</i>	<i>2011</i>
	<i>£000</i>	<i>£000</i>
Other:		
Expiring within one year	313	354
Expiring between two to five years inclusive	315	501
Expiring in over five years	-	-
	<u>628</u>	<u>855</u>

34. Contingent Liability

There are no material contingent liabilities.

35. Related Party Transactions

There are no material related party transactions.

36. Access Funds

	<i>Group</i>		
	<i>Childcare</i>	<i>Hardship</i>	<i>Total</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>
At 1 August 2011	7	67	74
Funding Council grants	96	387	483
Disbursed to students	(52)	(359)	(411)
Vired between funds	(45)	45	0
	<u>6</u>	<u>140</u>	<u>146</u>
Balance unspent at 31 July 2012	<u>6</u>	<u>140</u>	<u>146</u>
Repayable to funding body	<u>6</u>	<u>140</u>	<u>146</u>

Funding council grants are available solely for students; the group acts only as a paying agent. The grants and related disbursements are therefore excluded from the Income and Expenditure Account.

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

37. Financial Instruments

The University group has exposure to the following risks from the use of financial instruments:-

- Liquidity risk
- Credit risk
- Market risk

Liquidity risk

Liquidity risk is the risk that the group will not be able to meet its financial obligations as they fall due. The University's approach to managing liquidity is to ensure that it will have sufficient liquid funds to meet its liabilities as they fall due.

The group's key income sources are set out in notes 2 to 6 above. These income streams are considered by the University to be reliable and stress tests against the bank covenants in place show these income streams to be more than sufficient to satisfactorily service the existing level of debt.

Liquidity is managed by the use of the annual operating plan process and the monitoring of actual performance against budgets and forecasts.

The table below details the contractual maturities of financial liabilities.

	<i>Carrying amount</i>	<i>Contractual cash flows</i>	<i>Within one year</i>	<i>After more than one year</i>
	£000	£000	£000	£000
Financial liabilities				
Trade creditors and other payables <small>(less accruals)</small>	30,378	-	30,197	181
Other financial liabilities	40,500	-	-	40,500
	<u>70,878</u>	<u>-</u>	<u>30,197</u>	<u>40,681</u>

Credit risk

Credit risk is the risk of financial loss to the University group if a customer or counter party fails to meet its contractual obligations and arises from the trade receivables.

The maximum exposure to credit risk is represented by the carrying value of each financial asset in the balance sheet.

The University operates a debt management process including monitoring, escalation procedures and recourse to court action to recover monies outstanding. Provision is made for doubtful receivables upon the age of the debt and experience of collecting overdue debts. Cash and cash equivalents are held with banks which are not expected to fail.

The maximum exposure to credit risk at the reporting date was:-

	Carrying Amount	
	2012	2011
	£000	£000
Financial assets		
Trade debtors and other receivables	19,978	16,256
Cash and cash equivalents	14,138	23,256
	<u>34,116</u>	<u>39,512</u>

The movement in the impairment provision in respect of financial assets is set out in Note 16 above.

NOTES TO THE ACCOUNTS
For the year ending 31st July 2012

Financial Instruments (continued)

Market risk

Market risk is the risk that market prices such as interest rates, foreign exchange rates and equity prices will affect income or the value of holdings in financial instruments.

Interest rate risk

The University holds the following fixed rate interest rate swap arrangements:

- A swap was entered into on 28th June 2002 for £10 million at 5.05%, expiring on 30th September 2016 and amortising on a straight line basis from 31st December 2008.
- A swap was entered into on 28th June 2002 for £5 million at 5.62%, expiring on 30th September 2016 and amortising on a straight line basis from 31st December 2008.
- A swap was entered into on 5th October 2007 for £5 million at 5.03%, rising to £18 million on 30th September 2016, expiring on 31st March 2037 and amortising on a straight line basis from 30th September 2014.

	Carrying Amount	
	2012	2011
	£000	£000
Fixed rate instruments		
Financial assets	-	-
Financial liabilities	40,500	26,000
	<u>40,500</u>	<u>26,000</u>

	Carrying Amount	
	2012	2011
	£000	£000
Variable rate instruments		
Financial assets	-	-
Financial liabilities	-	-
	<u>-</u>	<u>-</u>

Currency risk

The University group is exposed to currency risk on transactions and balances that are denominated in currencies other than sterling. Whenever practical, the University enters into agreements in its functional currency in order to minimise currency risks. The University group is exposed to currency risks from its activities conducted overseas but does not enter into any hedge arrangements and does not consider currency risk to be material.

Fair values

The fair values, together with the carrying amounts of financial assets and liabilities in the balance sheet are as follows:-

	Carrying amount	Fair value	Carrying amount	Fair value
	2012	2012	2011	2011
	£000	£000	£000	£000
Financial assets held for sale	-	-	-	-
Trade debtors and other receivables	19,978	19,978	16,256	16,256
Cash and cash equivalents	14,138	14,138	23,256	23,256
Trade creditors and other payables	(30,378)	(30,378)	(36,496)	(36,496)
	<u>3,738</u>	<u>3,738</u>	<u>3,016</u>	<u>3,016</u>

NOTES TO THE ACCOUNTS

For the year ending 31st July 2012

Estimation of fair values

The following methods and assumptions were used to estimate fair values:-

Financial assets held for sale	Based on an assessment of recoverable amounts
Trade debtors and other receivables	Fair value deemed to be the same as book value
Cash and cash equivalents	Fair value deemed to be the same as book value
Trade creditors and other payables	Fair value deemed to be the same as book value

MEMBERS OF COURT

At 30 November 2012

Chairman of Court	The Rt Hon Lord George Penrose ¹	P.C., Q.C., M.A., LLB., C.A., LLD (Hon), D.Univ (Hon), FRSE
Principal & Vice-Chancellor	Professor Steve Chapman	FRSE, FRSC, C.Chem
Vice-Principal	Professor Julian D C Jones	OBE, FRSE, FOSA, FInstP, BSc, PhD
City of Edinburgh	Councillor Ricky Henderson ^{1,7} Councillor Tim McKay ⁶	
Senate	<i>Dr Alexander Bell</i> ² Professor Andrew Cairns ⁵ <i>Dr Jennie Hansen</i> ² Dr Stephen Houston ⁵ Professor James Ritchie Professor Peter Woodward	<i>BSc, PhD, DipEd, FHEA, MInstP, CPhys</i> MA, PhD, FFA <i>BA, MSc, PhD</i> BEng, PhD BSc, MSc, CEng, MIMechE, MIET, FHEA BEng, PhD
Staff	Mr Allan Gray Professor David Lane Ms Gill McDonald	BSc, PhD, FEng, FRSE, FRGS, FIET, FSUT MA, MBA, MCLIP, FHEA
Graduates	Dr Jock Clear ^{1,5} <i>Mr Gregor Colville</i> ² Mr Keith Wallace ¹	BSc, DEng <i>MEng, MSc, DIC, CEng, FIES, MEI,</i> <i>AMIChemE</i> Bsc (Hons), CEng, CDir, FICE, FIHT, FCILT, FRSA
Students Association	Mr Michael Ross ³ Ms Laura Gregson ⁴	BSc BSc
Co-opted	Professor Nicholas Beadle ¹ Professor Ken Gill ¹ Ms Shonaig Macpherson ¹ Mr Strone Macpherson ¹ Dr Judith McClure ¹ Mr Iain McLaren ¹ Mr Andrew Milligan ¹ Mr David Robinson ¹ Mr Tony Strachan ¹ Professor Ian Wall ¹	CMG, MBA, LLB BA, PgCE, MBA, FRSA, CPFA, MCIPD, MAAT CBE, DUniv, FRSE, FRSA, CCIPM, LIB MA, MBA CBE, MA, DPhil, FSAScot BA, CA BSc MA, FFA, FRSA MBA, FCIS, MIOd DSc, FRICS, Hon FRIAS

¹ Lay Member of Court

² Member until 31st July 2012

³ Member from 1st June 2011

⁴ Member from 1st June 2012

⁵ Member from 1st August 2012

⁶ Member until May 2012

⁷ Member from May 2012

MEMBERSHIP OF COMMITTEES OF COURT

At 30 November 2012

AUDIT & RISK COMMITTEE

Mr D G Robinson (Chair)

Mr W Dick
Professor K Gill
Mr B Kay
*Mr A Milligan*²
Mr T Strachan
Mr K Wallace⁵

EMERGENCY COMMITTEE

Lord G Penrose (Chair)

Professor S Chapman
Professor J Jones
Dr J McClure
Mr I McLaren
Mr D G Robinson

FINANCE COMMITTEE

Mr I McLaren (Chair)

Professor S Chapman
Professor J Jones
Professor David Lane
Mr A Milligan³
Dr J McClure
Lord G Penrose
*Mr R Perman*¹
Professor Ian Wall

GOVERNANCE AND NOMINATIONS COMMITTEE

Lord G Penrose (Chair)

Professor S Chapman
Professor J Jones
Dr Judith McClure
Mr I McLaren
Mr D Robinson

REMUNERATION COMMITTEE

Lord G Penrose (Chair)

Dr J McClure
Mr I McLaren

STAFF COMMITTEE

Dr J McClure (Chair)

Mr R Bailey
*Dr A Bell*¹
Professor S Chapman
Mr A Gray
Professor J Jones
Ms S Macpherson⁴
Lord G Penrose
Professor A C Walker

¹ Member until 31st July 2012

² Member until December 2011

³ Member from December 2011

⁴ Member from January 2012

⁵ Member from October 2012

COMMITTEE ATTENDANCE RECORD
At 30th November 2012

Name	Dates to/from	Court 8 meetings	Audit & Risk Committee (ARC) 10 meetings	Finance Committee (FC) 6 meetings	Governance & Nominations Committee 3 meetings	Staff Committee (SC) 7 meetings
Professor Nicholas Beadle		7/8				
Dr Alex Bell	Court & SC member until 31 July 2012*	6/6*				5/6*
Professor Andrew Cairns	Court member from Aug 2012*	1/2*				
Prof Steve Chapman		7/8		5/6	3/3	6/7
Dr Jock Clear	Court member from Aug 2012*	0/2*				
Mr Gregor Colville		5/6				
Professor Ken Gill		6/8	6/10			
Mr Allan Gray		7/8				6/7
Prof Julian Jones		8/8		6/6	2/3	3/7
Dr Jennie Hansen	Court member until 31 July 2012*	6/6*				
Dr Stephen Houston	Court member from Aug 2012*	2/2*				
Professor David Lane		6/8		4/6		
Ms Shonaig Macpherson	SC member from Jan 2012*	8/8				2/5*
Mr Strone Macpherson		8/8				
Dr Judith McClure		6/8		3/6	3/3	6/7
Ms Gill McDonald		7/8				
Councillor Tim Mckay	Court member until May 2012*	4/6*				
Councillor Ricky Henderson	Court member from May 2012*	1/2*				
Mr Iain McLaren		3/8		6/6	2/3	
Mr Andrew Milligan		7/8	8/10	4/6		
Rt Hon Lord George Penrose		8/8		4/6	3/3	3/7
Prof James Ritchie		7/8				
Mr David G Robinson		8/8	10/10		3/3	
Mr Michael Ross		8/8				
Mr Tony Strachan		8/8	8/10			
Professor Ian Wall		8/8		4/6		
Mr Keith Wallace	ARC member from 1 Oct 2012*	8/8	2/3*			
Professor Peter Woodward		7/8				
Mr Will Dick			10/10			
Mr Bob Kay			10/10			
Mr Richard Bailey						7/7
Mr Ray Perman	FC member until 31 July 2012			2/4*		
Professor A C Walker						7/7
Ms Laura Gregson	Court member from Aug 2012*	1/2*				
*Indicates total number of meetings held during period of membership						

