

Annual Accounts and
Financial Statements ²⁰**05**
For the year ended 31 July

**HERIOT-WATT UNIVERSITY
REPORT AND FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 JULY 2005**

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OPERATING AND FINANCIAL REVIEW

SCOPE OF THE FINANCIAL STATEMENTS

The financial statements which have been approved by the Court for the year-ended 31 July 2005 consolidate the transactions of the University and its subsidiary undertakings.

FINANCIAL PLANNING

The University's financial planning is designed to enhance revenues and minimise avoidable costs in order to generate net surpluses for investment in the furtherance of the University's educational objectives.

In order to ensure that debt levels do not threaten the achievement of the University's strategic objectives, cash flow is managed closely and the terms of debt instruments are monitored to ensure that financial risk is mitigated.

RESULTS FOR THE YEAR

The consolidated income and expenditure was:

	2005	2004	2003
	£m	£m	£m
Income	94.6	90.9	85.3
Expenditure	(92.9)	(89.6)	(84.5)
Surplus / (Deficit) for the year	<u>1.7</u>	<u>1.3</u>	<u>0.8</u>

The University has continued the trend of recent years with a further improvement in its consolidated operating performance, reflected in a 32% increase in operating surplus to £1.7 million for the year, on revenues up by 4.0%.

Grants from the Scottish Higher Education Funding Council (SHEFC) increased by 2.8% for teaching and 8.3% for research. Tuition fees from UK HE students increased by 9.2% and, due to successful recruiting, tuition fees from non-EU students increased by 16.9%. Although Income from Research Grants and Contracts and other sources only increased by 1.0%, grants from Research Councils increased 11%. Heriot Watt is playing a major role in the research pooling initiatives recently announced by SHEFC. Over £7.4 million has been awarded to the Heriot-Watt University in support of research collaborations with other Scottish Universities over the next four years, further enhancing the University's research led status.

The University's own results, before property transactions, are consistent with the improvement seen in the consolidated figures and its own performance showed a modest increase for the year. The Edinburgh Business School made a good contribution to the consolidated result and it is gratifying to also note the positive contribution made by the Edinburgh Conference Centre.

CASH FLOW MANAGEMENT

The University has continued to focus on cash flow to ensure both that debt levels are controlled and that cash continues to be made available as necessary for educational activities.

This focus had a positive effect as consolidated net debt at the end of the financial year was 14% lower at £17.8 million (2004 - £20.2 million). The University's net debt at the year-end, excluding the Edinburgh Business School, was £26.8 million (2004 - £28.4 million). Cash outflows were reduced primarily due to lower capital expenditure as described below. Current debt levels are regarded as manageable and there are opportunities to further improve cash management.

Unless special terms are agreed, it is the University's policy to pay invoices at the end of the month following the month in which the invoice is dated. At 31 July 2005 there were 21 days (2004 - 23 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

During the year £5.7 million (2004 - £10.8 million) was invested in additions to the fabric and infrastructure of the University capital base.

The principal capital spend was on a new building for the School of Mathematics and Computer Sciences.

Further significant capital spend was also incurred to enhance the University's research capabilities, funded by grants from the SRIF (Scientific Research Investment Fund) scheme.

Unless adequately supported by government or other funding sources no significant new capital spend is anticipated in the foreseeable future. The University has received confirmation of the Funding Council's intent to invest through the Learning & Teaching Infrastructure Fund. This capital will be combined with University funds to continue improvements to the Learning & Teaching infrastructure.

ACTIVITIES DURING THE FINANCIAL YEAR

The University's student numbers, expressed as full-time equivalents, for the current and the previous year are:

Student Numbers – On Campus

<u>Student Numbers</u>		2005 Number	2004 Number
Home/EU	Undergraduate	4,755	4,690
International	Postgraduate	780	837
	Undergraduate	387	400
	Postgraduate	645	595
Total		<u>6,567</u>	<u>6,522</u>

Student Numbers – External Programmes & Distance Learning

<u>Student Numbers</u>		2004 Number
Home/EU	Undergraduate	30
International	Postgraduate	1,920
	Undergraduate	1,570
	Postgraduate	6,260
Total		<u>9,780</u>

The data for 2005 was not available at the date of publication

DUBAI CAMPUS

In April 2005 the University embarked on an innovative project to establish a campus in Dubai. The campus opened in the last week of September with 166 students registered on Msc courses in IT, Strategic Project Planning and a BA Course in Management. There are plans to extend the course availability to include our core disciplines including Construction Management and other Engineering courses.

FUTURE PLANS

The mission of Heriot Watt University is to create and transfer knowledge, to enable students and staff to fulfil their potential and to enrich the communities with which it engages.

The University will continue to implement its strategy of developing learning & teaching delivery, focusing on internationally recognised research, collaboration in research projects and the recruitment of high quality postgraduate students.

EMPLOYEES

In common with other HEIs, the University has been planning the implementation of the new National Framework Agreement which will introduce new terms and conditions for the University's employees. This has included comprehensive and constructive discussion with staff and staff representatives.

Staff are kept up-to-date with strategy implementation and financial and academic performance through a variety of communication channels.

STUDENTS

Students are represented on several Court Committees and on other management groups set up by the University's Planning and Management Executive, where their input is sought on matters affecting development of the University strategy. The University has had a long and successful track record of involving its students in influencing the University's key areas of performance.

DONATION

The University has made no donations in excess of £200 to UK political and charitable organisations.

INSURANCE

The University has insurance policies in place for its officers and for potential claims against them in connection with their role in managing the organisation.

PENSIONS

The University's employees are members of one of four pension schemes, details of which are set out on in note 30, which starts on page 30. All of these schemes provide benefits to members based on final pensionable pay. Total employer contributions for the year charged to the income and expenditure account were £5,640,000, of which 71% related to the Universities Superannuation Scheme (USS) and 28% related to the Lothian Pension Fund (LPF).

In common with other pension funds, USS and LPF are subject to triennial valuations of their scheme's assets and liabilities by professional actuaries. The last valuation, in March 2002, of USS indicated that its assets exceeded its liabilities and the next valuation is due in March 2006. Although the actuary's report will not be published until March 2006, the Chief Executive wrote to Vice Chancellors on 1st December 2005, following an initial report from the actuary to the USS scheme, and concluded his letter by saying that "The management committee considers that the funding objective, the valuation method and the assumptions underlying the valuation calculations together represent a satisfactory basis for the long-term funding of the benefits provided by USS".

However, the last valuation, in March 2002, of LPF indicated that its liabilities exceeded its assets and the FRS 17 accounting disclosures for the year-ended 31st July 2005 disclose a deficit of £13.5m (2004 £11.3m). The next valuation, in March 2005 (the results had not been published at the date of these accounts) is not expected to report that any improvement in this situation should be expected in the foreseeable future and to highlight the risk that the deficit may further increase. University management have commissioned professional advice to assess the options available to resolving this situation.

Details of the other two pension schemes (STSS and SPS) are given on page 34

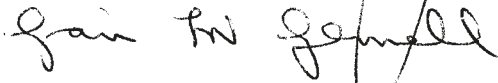
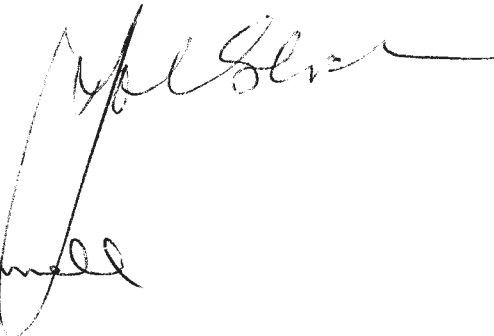
MINORITY INVESTMENTS

The University 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 the University retains a minority investment. As at 31 July 2005 there were twelve investments (2004 – eleven) in a range of different companies. The market value of these investments is not reflected in the University'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 University continues and that appropriate training is arranged. It is the policy of the University that the recruitment, training, career development and promotion of disabled persons should, as far as possible, be identical with that of other employees.

Prof. John S Archer
Principal & Chief Accounting Officer



Gavin J N Gemmell
Chairman of Court

CORPORATE GOVERNANCE STATEMENT

INTRODUCTION

The University 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 University complied substantially with the Governance Code of Practice and General Principles and the provisions of the Code provided by the CUC throughout the year ended 31 July 2005, with the exception of the number of Court members as discussed below. The Court also regularly reviews its governance provisions in line with both any recommendations made by SHEFC and any changes made in the CUC Code.

The University's financial accounting system was replaced during the financial year. During the implementation phases there was disruption to a number of management reports and certain internal control procedures. The new system was implemented and operational by the end of the financial year. Some internal control procedures required to be updated to reflect the requirements of the new system at 31st July 2005 and improvements in financial controls are being put in place. No weaknesses have been identified which have subsequently resulted in material losses, contingencies or uncertainties that require disclosure.

GOVERNING BODY

The Court, which has thirty four members including the Chairman who is always one of the lay members, is the ultimate decision taking body. Nineteen of the Court members are directly elected, eight are co-opted and the others are ex officio. As this is more than the recommended number of members laid down in the SHEFC guidelines, the Court has decided to move towards reducing the membership of Court to twenty five members as existing members of Court come to the end of their existing term of office. The Court has responsibility for the University'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 five times during the year. 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. The University's senior management attend Court meetings along with Deans and Deputy Principals to ensure optimum communication within the University.
- The Court has a Remuneration Committee made up of lay members. The Principal and Secretary are in attendance if required but are not present when their personal remuneration is considered. There is also a Nominating Committee of Court made up of lay members, Principal and Vice-Principal, with the lay members being in the majority. The Remuneration and Nominating Committees meet at least once per year under the convenorship of the Chairman of Court.
- The Court has an Audit Committee made up of lay members which meets at least three times a year with the External and Internal Auditors. It receives and considers reports and recommendations for the improvement of internal controls along with management responses. It also reviews the University's annual financial statements.
- The Court also has Finance, Estate Strategy and Staffing Strategy Committees each of which has a different lay member of Court as convenor.
- The terms of reference of all of the Court Committees are agreed by the Court.
- There is an Emergency Committee consisting of the Chairman of Court, the convenors of the Finance, Estate Strategy and Staffing Strategy Committees, the Principal and Vice-Principal ex officio, and one of the University's elected members of staff on Court. The Committee deals with emergency business which may arise between Court meetings.

- Where the University has commercial interests, the Court through the University's management appoints directors to the boards of companies appropriate to the nature and size of the University's shareholding.
- The University has taken necessary steps to ensure compliance with FR58 on Related Party transactions and any interests which require to be disclosed to members of Court are recorded in the Court minutes. However the Register of Interest had not been kept up to date but has now been completed.
- The Secretary of the University is the Clerk to the Court.

CORPORATE STRATEGY

The University's strategy is documented in its 3 year plan which is reviewed and updated on an annual basis. A copy of the plan is presented annually to the Funding Council.

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 University, 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 SHEFC and other relevant accounting standards. In addition, within the terms and conditions of a Financial Memorandum agreed between the Scottish Higher Education 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 University and of the surplus or deficit and cash flows for that year.

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 University 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 SHEFC 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. This system of internal control is continuously reviewed and developed in line with current best practice.
- safeguard the assets of the University and prevent and detect fraud.
- secure the economical, efficient and effective management of the University's resources and expenditure.
- ensure that the University 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.

RISK MANAGEMENT AND INTERNAL CONTROLS

The University'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 Deputy Principal (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. Due to early problems in implementing the new financial system, this control did not take place each month in the first half of the year. However, subsequent reviews did not reveal any material problems.
- 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. We have identified a number of ways in which these controls may be strengthened and these have all now been implemented.
- Comprehensive Financial Regulations, detailing financial controls and procedures, approved by the Audit Committee and Court. These Regulations are currently under review and an updated set will be presented to the Audit Committee at Court for approval in early 2006.
- An Internal Audit team whose annual programme is approved by the Audit Committee and who report to the Audit Committee. All recommendations from internal audit reports are implemented to agreed time plans.
- Recommendations from the external auditors are also implemented to agreed time plans with priority allocated in accordance with the ranking set out in the audit reports.
- An ongoing process for identifying, evaluating and managing the University's significant risks has been in place throughout the period. This process is regularly reviewed by the Audit Committee.

The Audit Committee on behalf of Court, with the assistance of both external and internal audit, considers the wider aspects of internal control within the University. The Audit Committee, with the assistance of internal audit, also considers the issue of value for money within the University. At the Court meeting on 3rd October 2005, the Audit Committee convenor expressed satisfaction at the University's approach to improving internal controls.

GOING CONCERN

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

CONCLUSION

The University has made good progress in developing its compliance with best practice in Corporate Governance and is improving its system of internal controls.

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

We have audited the financial statements on pages 10 to 36 which have been prepared in accordance with the accounting policies set out on pages 14 to 17.

This report is made solely to the University Court, in accordance with the Charter and Statutes of the University. Our audit work has been undertaken so that we might state to the University Court those matters we are required to state to it in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the University Court, for our work, for this report, or for the opinions we have formed.

RESPECTIVE RESPONSIBILITIES OF THE UNIVERSITY COURT AND AUDITORS

The University Court is responsible for the preparing the financial statements. As described on page 7, this includes responsibility for preparing the financial statements in accordance with the Statement of Recommended Practice: Accounting for Further and Higher Education and applicable United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board, the requirements of the Scottish Higher Education Funding Council's Code of Audit Practice and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Statement of Recommended Practice: Accounting for Further and Higher Education. We also report to you if, in our opinion, the Report of the Convenor of the Finance Committee is not consistent with the financial statements, if the University has not kept proper accounting records, if the accounting records do not agree with the financial statements or if we have not received all the information and explanations we require for our audit.

We also are required to report to you our opinion as to whether:

- Funds from whatever source administered by the University for specific purposes have, in all material respects, been properly applied to those purposes and managed in accordance with any other terms and conditions attached to them; and
- Income has in all material respects, been applied in accordance with relevant legislation and with the University's Financial Memorandum, dated 1 August 1999, with the Scottish Higher Education Funding Council.

We read the other information contained in the financial statements and consider whether it is consistent with the audited accounts. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the accounts.

BASIS OF AUDIT OPINION

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board and the Scottish Higher Education Funding Council's Code of Audit Practice. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the accounts. It also includes an assessment of the significant estimates and judgements made by the University Court in the preparation of the financial statements, and of whether the accounting policies are appropriate to the University's circumstances, consistently applied and adequately disclosed.

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

OPINION

In our opinion:

- the financial statements give a true and fair view of the state of affairs of the University as at 31 July 2005 and of its surplus of income over expenditure and cash flows for the year then ended and have been properly prepared in accordance with the Statement of Recommended Practice: Accounting for Further and Higher Education;
- funds from whatever source administered by the University for specific purposes have, in all material respects, been properly applied to those purposes and managed in accordance with any other terms and conditions attached to them; and
- income has, in all material respects, been applied in accordance with relevant legislation and with the University's Financial Memorandum, dated 1 August 1999, with the Scottish Higher Education Funding Council.



KPMG LLP
Registered Auditor
Chartered Accountants
Saltire Court
20 Castle Terrace
Edinburgh
EH1 2EG

CONSOLIDATED INCOME AND EXPENDITURE ACCOUNT FOR THE YEAR ENDED 31 JULY 2005

	Note	2005 £000	2004 £000
Income			
Funding Council Grants	2	33,926	33,458
Tuition Fees and Education Contracts	3	24,074	20,852
Research Grants and Contracts	4	15,059	14,908
Other Income	5	20,789	21,201
Endowment and Investment Income	6	788	561
Total income		<u>94,636</u>	<u>90,980</u>
Expenditure			
Staff Costs	7	53,821	51,675
Other Operating Expenses	8, 10	33,301	31,591
Depreciation	11	4,118	4,708
Interest Payable	9	1,572	1,669
Total expenditure	10	<u>92,812</u>	<u>89,643</u>
Surplus on continuing operations after depreciation of tangible assets and before taxation		1,824	1,337
Gain / (Loss) on disposal of assets		37	(128)
Surplus on continuing operations after depreciation and disposal of assets but before taxation		<u>1,861</u>	<u>1,209</u>
Taxation		-	-
Surplus on continuing operations after depreciation and disposal of assets and taxation		<u>1,861</u>	<u>1,209</u>
Transfer (to) / from accumulated income within specific endowments		(118)	91
Net surplus for the year retained within general reserves	24	<u>1,743</u>	<u>1,300</u>

All transactions are in respect of continuing operations.

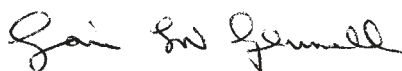
**CONSOLIDATED STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES
FOR THE YEAR ENDING 31 JULY 2005**

	Note	2005 £000	2004 £000
Net Surplus for the year		1,743	1,300
Appreciation of endowment asset investments	14	710	193
New endowments	14	178	69
Total recognised gains relating to the year		<u><u>2,631</u></u>	<u><u>1,562</u></u>
Reconciliation			
Opening reserves and endowments		28,441	26,879
Total recognised gains for the year		2,631	1,562
Closing reserves and endowments		<u><u>31,072</u></u>	<u><u>28,441</u></u>

BALANCE SHEETS AS AT 31 JULY 2005

	Note	Group		University	
		2005 £000	2004 £000	2005 £000	2004 £000
Fixed Assets					
Tangible Assets	11	96,880	95,887	85,543	84,091
Investments	12	87	115	186	220
Total fixed assets		<u>96,967</u>	<u>96,002</u>	<u>85,729</u>	<u>84,311</u>
Endowment Assets	14	<u>6,338</u>	<u>5,450</u>	<u>4,855</u>	<u>4,210</u>
Stock		38	53	-	32
Debtors	15	14,132	9,259	23,212	18,176
Investments and Short Term Deposits	16	307	243	-	-
Cash at Bank and in Hand		<u>10,655</u>	<u>8,865</u>	<u>4,090</u>	<u>5,335</u>
		25,132	18,420	27,302	23,543
Less: Creditors - Amounts falling due within one year	17	<u>(23,811)</u>	<u>(18,425)</u>	<u>(23,132)</u>	<u>(19,070)</u>
Net Current (Liabilities) / Assets		<u>1,321</u>	<u>(5)</u>	<u>4,170</u>	<u>4,473</u>
Total Assets Less Current Liabilities		104,626	101,447	94,754	92,994
Less: Creditors - Amounts falling due after more than one year	18	(30,065)	(30,643)	(29,709)	(31,376)
Less: Provisions for liabilities and charges	19	(806)	(943)	(806)	(943)
NET ASSETS		<u>73,755</u>	<u>69,861</u>	<u>64,239</u>	<u>60,675</u>
Deferred Capital Grants	20	42,463	41,256	40,764	39,759
Specific Endowments	21	6,338	5,450	4,855	4,210
Restricted Funds	22	168	164	-	-
Investment Reserve	23	52	-	-	-
General Reserve	24	24,734	22,991	18,620	16,706
TOTAL FUNDS		<u>73,755</u>	<u>69,861</u>	<u>64,239</u>	<u>60,675</u>

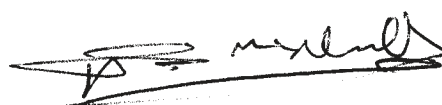
The Financial Statements on pages 10 to 36 were approved by the University Court on Monday 12th December 2005 and were signed its behalf by:-



Gavin J N Gemmell
Chairman of Court



Prof. John S Archer
Principal & Chief Accounting Officer



Phil McNaull
Director of Finance & IS/IT

CONSOLIDATED CASH FLOW STATEMENT FOR THE YEAR ENDING 31 JULY 2005

	Note	2005 £000	2004 £000
Cash inflow from operating activities	25	5,451	7,758
Returns on investment and servicing of finance	26	(944)	(1,338)
Capital expenditure and financial investment	27	(2,048)	(5,950)
Financing	28	(669)	2,321
Increase in cash in the year		<u><u>1,790</u></u>	<u><u>2,791</u></u>

Reconciliation Of Net Cash Flow To Movement In Net Debt

Increase in cash in the year		1,790	2,791
Financing		<u>669</u>	<u>(2,321)</u>
Movement in net debt		2,459	470
Net debt brought forward		<u>(20,240)</u>	<u>(20,874)</u>
Net debt carried forward	29	<u><u>(17,781)</u></u>	<u><u>(20,404)</u></u>

NOTES TO THE ACCOUNTS FOR THE YEAR ENDING 31 JULY 2005

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 2003 and in accordance with applicable accounting standards.

Basis of accounting

The financial statements are prepared in accordance with the historical cost accounting convention as modified by the revaluation of endowment asset investments.

Basis of consolidation

The consolidated financial statements include the University and its subsidiaries, as detailed at note 13. The results of subsidiaries acquired or disposed of during the year are included in the consolidated 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, the activities of the Heriot-Watt University Students Union have not been consolidated as the University does not control these activities.

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 in Note 10.

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.

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 £5,000 which is capitalised in accordance with the University's capitalisation policy.

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

NOTES TO THE ACCOUNTS – continued**Post-retirement benefits**

All new members of staff have the option of joining a pension scheme. The schemes currently open to new members of staff 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) and the Supplementary Pension Scheme (SPS).

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

The subsidiary undertakings do not operate any other pension schemes. Employees of the subsidiary undertakings are members of the University's pension schemes. The amount charged against profits represents the contributions payable to the individual plans in respect of the year.

USS

Heriot-Watt University participates in the USS 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 accounting period.

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.

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 accounting period.

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. The valuation of the scheme indicates a notional deficiency of £676,000, for which a provision is included in note 19. We were unable to obtain an actuarial valuation prior to the approval of the 2004-05 financial statements.

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 University 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.

NOTES TO THE ACCOUNTS – continued

Tangible fixed assets

Land and buildings are included in the balance sheet at historical cost and are depreciated on a straight line basis over their expected useful economic life of 50 years. Freehold land is not depreciated. Where land and buildings are acquired or built with the aid of specific grants they are capitalised and depreciated as above.

Equipment costing less than £5,000 per individual item or group of related items is written off to the income and expenditure account in the year of acquisition. All other equipment is capitalised at cost.

Capitalised equipment is depreciated on a straight line basis over its expected useful economic life as follows:

General equipment	- 5 years
Computers	- 5 years
Furniture & fittings	- 5 years
Motor vehicles	- 4 years

Capitalised equipment for sponsored research is depreciated on a straight line basis over the life of the related research grant or contract.

Assets under construction are included in the balance sheet at cost.

Capital grants

Capital grants received are credited to a deferred capital grant creditor 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 assets are stated at market value. Current asset investments, which may include listed investments, are stated at the lower of their cost and net realisable value.

Stocks

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.

Maintenance of premises

The cost of routine corrective maintenance is charged to the income and expenditure account in the period that it is incurred.

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.

Transactions denominated in foreign currencies are recorded at the rate of exchange ruling at the date of the transaction.

Provisions

Provisions are recognised when the University 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.

NOTES TO THE ACCOUNTS – continued**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, transfer their annual profits to the University by gift aid. In certain circumstances Value Added Tax is recoverable, but where this is not possible the cost is included in the relevant expenditure.

2. FUNDING COUNCIL GRANTS

	Group	
	2005	2004
	£000	£000
Recurrent Grant		
Teaching	22,436	21,826
Research	9,630	8,888
Other	330	505
Specific Grants		
Other grants	223	287
Deferred Capital Grants Released in Year		
Buildings	815	1,524
Equipment	492	428
	<u>33,926</u>	<u>33,458</u>

3. TUITION FEES AND EDUCATION CONTRACTS

	Group	
	2005	2004
	£000	£000
UK Higher education students	7,052	6,456
European Union students (ex. UK)	1,598	1,433
Non European Union students	10,094	8,638
Higher education contracts	956	1,309
Research training support grants	1,698	633
Short course fees	1,354	1,312
Examination and graduation fees	1,322	1,071
	<u>24,074</u>	<u>20,852</u>

NOTES TO THE ACCOUNTS – continued**4. RESEARCH GRANTS AND CONTRACTS**

	Group	
	2005	2004
	£000	£000
Research councils	6,243	5,618
Charities	232	433
UK government	1,797	1,535
UK industry	3,951	3,895
EU Commission	1,481	1,832
Other sources	1,355	1,595
	<u>15,059</u>	<u>14,908</u>

5. OTHER INCOME

	Group	
	2005	2004
	£000	£000
Residences, catering and conferences	11,475	10,229
Other services rendered	2,996	3,051
Royalties	2,293	2,461
Donations	1,213	1,387
Release from deferred capital grants	827	203
Other income	1,985	3,870
	<u>20,789</u>	<u>21,201</u>

6. ENDOWMENT AND INVESTMENT INCOME

	Group	
	2005	2004
	£000	£000
Income from specific endowment assets	213	174
Other investment income	84	67
Other interest receivable	491	320
	<u>788</u>	<u>561</u>

7. STAFF COSTS

	Group	
	2005	2004
	£000	£000
Wages and salaries	44,486	42,852
Social security costs	3,695	3,528
Other pension costs	5,640	5,295
	<u>53,821</u>	<u>51,675</u>

NOTES TO THE ACCOUNTS – continued*Staff Costs (continued)*

Analysed between:

	Group	
	2005	2004
	£000	£000
Academic	20,872	20,336
Academic support	16,180	15,465
Other support	1,135	1,177
Administrative & central services	8,861	8,354
Estates	3,069	2,806
Catering and residences	3,629	3,468
Other	75	69
	<u>53,821</u>	<u>51,675</u>

The average monthly number of persons employed by the University during the year, expressed as full-time equivalents, was:

	Number	Number
Academic	375	380
Academic support	509	506
Other support	38	41
Administrative & central services	246	243
Estates	142	136
Catering and residences	172	173
Other	18	17
	<u>1,500</u>	<u>1,496</u>

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

	2005	2004
	£000	£000
£70,001 - £80,000	7	9
£80,001 - £90,000	11	10
£90,001 - £100,000	5	3
£100,001 - £110,000	2	1
£120,001 - £130,000	-	1
£130,001 - £140,000	1	-
£160,001 - £170,000	-	1
£180,001 - £190,000	1	-
	<u>27</u>	<u>25</u>

NOTES TO THE ACCOUNTS – continued*Staff Costs (continued)*

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

	2005 £000	2004 £000
Salary	172	160
Benefits in kind	9	9
	<u>181</u>	<u>169</u>
Pension contributions	<u>24</u>	<u>22</u>

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

Costs of £12,000 were incurred by the Principal during the year in respect of overseas activities carried out in pursuance of the strategy approved by the governing body.

8. OTHER OPERATING EXPENSES

	Group	
	2005 £000	2004 £000
Other operating expenses include:		
* Auditors' remuneration - external audit	41	45
** Auditors' remuneration - internal audit	51	40
Other services from external audit	20	31
(Profit) / Loss on disposal of tangible fixed assets	(41)	128
Hire of other assets - operating leases - other	502	544
Finance lease charges	3	-
* Inc. £28,500 for Heriot-Watt University		
** Inc. £51,000 for Heriot-Watt University		

9. INTEREST PAYABLE

	Group	
	2005 £000	2004 £000
On bank loans:		
Repayable within 5 years, by instalments	2	2
Repayable wholly or partly in more than 5 years	1,570	1,667
	<u>1,572</u>	<u>1,669</u>

NOTES TO THE ACCOUNTS – continued

10. ANALYSIS OF 2005 EXPENDITURE BY ACTIVITY

	Group				Total £000
	Staff Costs £000	Dep'n. £000	Other Operating Expenses £000	Interest Payable £000	
Academic departments	28,452	786	5,548	-	34,786
Academic services	2,559	45	1,751	-	4,355
General educational	780	-	2,084	-	2,864
Premises	3,420	1,561	4,792	-	9,773
Administration	6,453	259	2,619	-	9,331
Student facilities	1,330	47	1,484	-	2,861
Other expenses	71	3	13	1,572	1,659
Research grants and contracts	6,529	579	7,659	-	14,767
Residences, catering and conference	3,074	817	5,313	-	9,204
Other services rendered	1,153	21	1,337	-	2,511
Equipment	-	-	701	-	701
Total per Income and Expenditure Account	<u>53,821</u>	<u>4,118</u>	<u>33,301</u>	<u>1,572</u>	<u>92,812</u>

Analysis of 2004 Expenditure By Activity

	Group				Total £000
	Staff Costs £000	Dep'n. £000	Other Operating Expenses £000	Interest Payable £000	
Academic departments	28,224	273	2,887	-	31,384
Academic services	2,515	32	1,989	-	4,536
General educational	513	-	3,406	-	3,919
Premises	2,643	2,128	3,960	-	8,731
Administration	5,586	541	2,544	-	8,671
Student facilities	1,147	23	1,142	-	2,312
Other expenses	6	14	208	1,669	1,897
Research grants and contracts	6,218	817	7,457	-	14,492
Residences, catering and conferences	3,491	861	4,088	-	8,440
Other services rendered	1,332	19	1,999	-	3,350
Equipment	-	-	1,911	-	1,911
Total per Income and Expenditure Account	<u>51,675</u>	<u>4,708</u>	<u>31,591</u>	<u>1,669</u>	<u>89,643</u>

NOTES TO THE ACCOUNTS – continued

11. TANGIBLE FIXED ASSETS

		Freehold Land and Buildings	Equipment	Total
		£000	£000	£000
Group				
Cost				
At 1 August 2004		121,547	18,333	139,880
Additions		1,993	3,679	5,672
Disposals		(1,412)	(767)	(2,179)
At 31 July 2005		<u>122,128</u>	<u>21,245</u>	<u>143,373</u>
Depreciation				
At 1 August 2004		29,745	14,248	43,993
Charge for year		2,269	1,849	4,118
Eliminated on disposals		(855)	(763)	(1,618)
At 31 July 2005		<u>31,159</u>	<u>15,334</u>	<u>46,493</u>
Net Book Value	At 31 July 2005	<u>90,969</u>	<u>5,911</u>	<u>96,880</u>
	At 1 August 2004	<u>91,802</u>	<u>4,085</u>	<u>95,887</u>
Analysed between:				
		£000	£000	£000
Funded by capital grants		52,806	3,191	55,997
Own funded		38,163	2,720	40,883
At 31 July 2005		<u>90,969</u>	<u>5,911</u>	<u>96,880</u>
University				
Cost				
At 1 August 2004		109,508	17,570	127,078
Additions		1,741	3,596	5,337
Eliminated on disposals		(894)	(581)	(1,475)
At 31 July 2005		<u>110,355</u>	<u>20,585</u>	<u>130,940</u>
Depreciation				
At 1 August 2004		29,209	13,778	42,987
Charge for year		2,044	1,790	3,834
Eliminated on Disposals		(843)	(581)	(1,424)
At 31 July 2005		<u>30,410</u>	<u>14,987</u>	<u>45,397</u>
Net Book Value	At 31 July 2005	<u>79,945</u>	<u>5,598</u>	<u>85,543</u>
	At 1 August 2004	<u>80,299</u>	<u>3,792</u>	<u>84,091</u>

NOTES TO THE ACCOUNTS – continued*Tangible Fixed Assets (continued)*

Analysed between:

	£000	£000	£000
Funded by capital grants	46,368	3,161	49,529
Own funded	33,577	2,437	36,014
At 31 July 2005	<u>79,945</u>	<u>5,598</u>	<u>85,543</u>

The net book value of the group's tangible fixed assets includes an amount of £55,138 (2004 - £69,046) in respect of assets held under finance leases. The depreciation charge on these assets for the year was £13,908 (2004 - £492).

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.

12. INVESTMENTS

	Group		University	
	2005 £000	2004 £000	2005 £000	2004 £000
Investment in subsidiary companies at cost	-	-	131	105
Minority investments in unquoted companies	87	55	55	55
Works of art	-	60	-	60
	<u>87</u>	<u>115</u>	<u>186</u>	<u>220</u>

Minority investments in unquoted companies include investments made by the University in spin-out companies, which are stated at cost.

13. SUBSIDIARY UNDERTAKINGS

	Number of shares	Percentage owned
The University has major shareholdings in the following companies:		
Edinburgh Business School (Limited by Guarantee)	-	100%
Edinburgh Conference Centre Limited	100,000	100%
* The Scottish Director Centre Limited	2	100%
Heriot-Watt Properties Limited	2	100%
Heriot-Watt Trading Limited	5,000	100%
Heriot-Watt Sports Village Limited	100	100%
Heriot-Watt Services Limited	2	100%
* Interactive University Press Limited	2	100%
* Scottish College of Textiles Limited	6	100%
* SCOT Innovation and Development Limited	80,000	100%
** The Interactive University	-	50%
*** SISTech Limited	250	50%

NOTES TO THE ACCOUNTS – continued*Subsidiary Undertakings (continued)*

The consolidated financial statements of the University include the transactions of the above companies, with the exception of those marked with an asterisk.

* These companies are dormant.

** For The Interactive University the figures are not consolidated as Heriot-Watt University has neither control / influence over the organisation's activities nor a right / obligation to a share of the financial profits / losses.

*** For SISTech Limited the figures are not consolidated as they are deemed to be insignificant.

The group has an investment in EBS Americas for which the figures are not consolidated because they are insignificant.

14. ENDOWMENT ASSETS

	Group		University	
	2005 £000	2004 £000	2005 £000	2004 £000
Balance at 1 August 2004	5,450	5,188	4,210	4,020
Increase in cash balances held	178	69	178	69
Appreciation of endowment asset investments	710	193	467	121
Balance at 31 July 2005	<u>6,338</u>	<u>5,450</u>	<u>4,855</u>	<u>4,210</u>
Represented by:				
Equities (listed)	5,699	4,989	4,216	3,749
Cash balances	639	461	639	461
	<u>6,338</u>	<u>5,450</u>	<u>4,855</u>	<u>4,210</u>

15. DEBTORS

	Group		University	
	2005 £000	2004 £000	2005 £000	2004 £000
Trade debtors	3,476	2,317	2,264	1,464
Research debtors	7,081	5,129	7,081	5,129
Loans by parent undertaking	-	-	8,957	9,078
Amounts owed by group undertakings	-	-	2,524	1,405
Prepayments and accrued income	3,575	1,813	2,386	1,100
	<u>14,132</u>	<u>9,259</u>	<u>23,212</u>	<u>18,176</u>

Included in loans by parent undertaking is £5,000,000 (2004: £5,072,000) due by Heriot-Watt Sports Village Ltd to Heriot-Watt University and £3,931,000 (2004: £3,957,000) due by Edinburgh Conference Centre Ltd to Heriot-Watt University that is due after more than one year.

16. INVESTMENTS AND SHORT-TERM DEPOSITS

	Group		University	
	2005 £000	2004 £000	2005 £000	2004 £000
Listed investments on the London Stock Exchange	307	243	-	-
	<u>307</u>	<u>243</u>	<u>-</u>	<u>-</u>

NOTES TO THE ACCOUNTS – continued

17. CREDITORS AMOUNTS FALLING DUE WITHIN ONE YEAR

	Group		University	
	2005	2004	2005	2004
	£000	£000	£000	£000
Bank loans	667	667	667	667
Loans from subsidiary companies	-	-	1,000	1,750
Obligations under finance leases	19	15	-	-
Grants in advance for research	9,236	4,867	9,236	4,867
Grants in advance from SHEFC	724	510	724	510
Other creditors	51	25	-	-
Trade creditors	1,698	2,473	1,617	2,402
Other taxation and social security	2,708	2,632	2,258	2,213
Accruals and deferred income	8,708	7,236	7,630	6,661
	<u>23,811</u>	<u>18,425</u>	<u>23,132</u>	<u>19,070</u>

18. CREDITORS AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR

	Group		University	
	2005	2004	2005	2004
	£000	£000	£000	£000
Bank loans	27,709	28,376	27,709	28,376
Loans from subsidiary companies	-	-	2,000	3,000
Obligations under finance leases (between 2 to 5 years)	41	47	-	-
Deferred income	2,019	2,108	-	-
Other creditors	296	112	-	-
	<u>30,065</u>	<u>30,643</u>	<u>29,709</u>	<u>31,376</u>
The above loans are repayable as follows:				
In one year or less (note 17)	<u>667</u>	<u>667</u>	<u>1,667</u>	<u>2,417</u>
Between one and two years	670	670	670	670
Between two and five years	3,707	1,349	5,037	4,349
In five years or more	<u>23,332</u>	<u>26,357</u>	<u>24,002</u>	<u>26,357</u>
	<u>27,709</u>	<u>28,376</u>	<u>29,709</u>	<u>31,376</u>
	<u>28,376</u>	<u>29,043</u>	<u>31,376</u>	<u>33,793</u>

Bank loans comprise £18.9 million, repayable by instalments between 2008 and 2016, at rates of between 5.05% and 5.62% and £8.8 million, repayable by instalments between 2004 and 2020, at rates of between 4.87% and 5.60%

Loans from subsidiary companies comprises £3,000,000 (2004: £4,750,000) with £2,000,000 (2004: £3,000,000) due after more than one year, repayable in full by 31 July 2009, at a rate of 1.5% over the bank base rate.

NOTES TO THE ACCOUNTS – continued

19. PROVISIONS FOR LIABILITIES AND CHARGES

	Group and University Pensions £000	Total £000
At 1 August 2004	943	943
Utilised during the year	(137)	(137)
At 31 July 2005	<u>806</u>	<u>806</u>
To be spent before 31 July 2006	<u>109</u>	<u>109</u>

20. DEFERRED CAPITAL GRANTS

	Funding Council £000	Other Grants and Benefactions £000	Total £000
Group			
At 1 August 2004			
Buildings	28,270	10,167	38,437
Equipment	1,985	834	2,819
Total	<u>30,255</u>	<u>11,001</u>	<u>41,256</u>
Cash Received			
Buildings	1,956	239	2,195
Equipment	698	448	1,146
Total	<u>2,654</u>	<u>687</u>	<u>3,341</u>
Transfers			
Buildings	305	(305)	-
Equipment	6	(6)	-
Total	<u>311</u>	<u>(311)</u>	<u>-</u>
Released to Income and Expenditure			
Buildings	(815)	(241)	(1,056)
Equipment	(492)	(586)	(1,078)
Total	<u>(1,307)</u>	<u>(827)</u>	<u>(2,134)</u>
At 31 July 2005			
Buildings	29,716	9,860	39,576
Equipment	2,197	690	2,887
Total	<u>31,913</u>	<u>10,550</u>	<u>42,463</u>

NOTES TO THE ACCOUNTS – continued

*Deferred Capital Grants (continued)***University**

At 1 August 2004

Buildings	28,205	8,739	36,944
Equipment	1,985	830	2,815
Total	<u>30,190</u>	<u>9,569</u>	<u>39,759</u>

Cash Received

Buildings	1,956	-	1,956
Equipment	698	447	1,145
Total	<u>2,654</u>	<u>447</u>	<u>3,101</u>

Transfers

Buildings	305	(305)	-
Equipment	6	(6)	-
Total	<u>311</u>	<u>(311)</u>	<u>-</u>

Released to Income and Expenditure

Buildings	(813)	(206)	(1,019)
Equipment	(492)	(585)	(1,077)
Total	<u>(1,305)</u>	<u>(791)</u>	<u>(2,096)</u>

At 31 July 2005

Buildings	29,653	8,228	37,881
Equipment	2,197	686	2,883
Total	<u>31,850</u>	<u>8,914</u>	<u>40,764</u>

21. ENDOWMENTS

	Group		University	
	Specific 2005 £000	Specific 2004 £000	Specific 2005 £000	Specific 2004 £000
At 1 August 2004	5,450	5,188	4,210	4,020
Additions	60	162	60	162
Appreciation of endowment asset investments	710	193	467	121
Income for year	213	174	213	174
Expenditure for the year	(95)	(267)	(95)	(267)
At 31 July 2005	<u>6,338</u>	<u>5,450</u>	<u>4,855</u>	<u>4,210</u>
Representing:				
Fellowship and scholarship funds	1,789	1,801	1,789	1,801
Prize funds	542	541	542	541
Chairs and lectureship funds	2,421	2,173	938	933
Other funds	1,586	935	1,586	935
	<u>6,338</u>	<u>5,450</u>	<u>4,855</u>	<u>4,210</u>

NOTES TO THE ACCOUNTS – continued

22. RESTRICTED FUNDS

	Group		University	
	2005 £000	2004 £000	2005 £000	2004 £000
Balance at 1 August 2004	164	162	-	-
Income in the year	65	66		
Expenditure in the year	(61)	(64)	-	-
Balance at 31 July 2005	<u>168</u>	<u>164</u>	<u>-</u>	<u>-</u>

23. INVESTMENT RESERVE

	Group		University	
	2005 £000	2004 £000	2005 £000	2004 £000
Balance at 1 August 2004	-	-	-	-
Revaluation for the year	52	-	-	-
Balance at 31 July 2005	<u>52</u>	<u>-</u>	<u>-</u>	<u>-</u>

24. GENERAL RESERVE

	Group		University	
	2005 £000	2004 £000	2005 £000	2004 £000
Balance at 1 August 2004	22,991	21,691	16,706	14,834
Net surplus retained for the year	1,743	1,300	1,914	1,872
Balance at 31 July 2005	<u>24,734</u>	<u>22,991</u>	<u>18,620</u>	<u>16,706</u>

	Group	
	2005 £000	2004 £000
The net surplus retained for the year is analysed as follows:		
University surplus	161	(101)
Gift Aid from subsidiaries	1,410	100
Surplus retained by subsidiaries	172	1,301
	<u>1,743</u>	<u>1,300</u>

NOTES TO THE ACCOUNTS – continued

25. RECONCILIATION OF OPERATING RESULT TO NET CASH INFLOW FROM OPERATING ACTIVITIES

	Group	
	2005	2004
	£000	£000
Surplus on continuing operations after depreciation and disposal of assets and taxation	1,861	1,209
Depreciation	4,118	4,708
(Profit) / loss on disposal of tangible fixed assets	(37)	164
Deferred capital grants released to income	(2,134)	(2,204)
Interest receivable	(575)	(321)
Interest payable	1,572	1,669
Decrease in fixed asset investments	28	-
Decrease in stocks	15	45
(Increase) in debtors	(4,808)	(1,042)
(Increase) / decrease in current asset investments	(64)	11
Increase in creditors	5,471	3,934
(Decrease) in provisions	-	(415)
Increase in restricted funds	4	-
Net Cash Inflow from Operating Activities	<u>5,451</u>	<u>7,758</u>

26. RETURNS ON INVESTMENT AND SERVICING OF FINANCE

	Group	
	2005	2004
	£000	£000
Income received on specific endowments	213	174
Expenditure paid on specific endowments	(95)	(267)
Interest received	491	320
Other investment income received	19	1
Interest paid	(1,572)	(1,566)
Net Cash (Outflow) from Returns on Investment and Servicing of Finance	<u>(944)</u>	<u>(1,338)</u>

27. CAPITAL EXPENDITURE AND FINANCIAL INVESTMENT

	Group	
	2005	2004
	£000	£000
Purchase of tangible fixed assets	(5,362)	(10,854)
Proceeds on disposal of tangible fixed assets	91	-
Fixed asset investments disposed	-	8
Payments to acquire endowment assets	(178)	(69)
Deferred capital grants received	3,341	4,803
Endowments received	60	162
Net Cash (Outflow) from Capital Expenditure and Financial Investment	<u>(2,048)</u>	<u>(5,950)</u>

NOTES TO THE ACCOUNTS – continued

28. FINANCING

	Group	
	2005	2004
	£000	£000
New bank loans received	-	3,000
Repayment of amounts borrowed	(667)	(741)
Capital element of finance lease rentals paid	(2)	62
Net Cash (Inflow)/Outflow from Financing	<u>(669)</u>	<u>2,321</u>

29. ANALYSIS OF CHANGES IN NET DEBT

	At 1 August 2004	Cash Flows	Other Changes	At 31 July 2005
	£000	£000	£000	£000
Cash at bank and in hand	8,865	1,790	-	10,655
	<u>8,865</u>	<u>1,790</u>	<u>-</u>	<u>10,655</u>
Debt due within one year	(667)	667	(667)	(667)
Debt due after one year	(28,376)	-	667	(27,709)
Finance leases	(62)	2	-	(60)
	<u>(20,240)</u>	<u>2,459</u>	<u>-</u>	<u>(17,781)</u>

Had the cash held under endowment asset investments been included above, the net cash inflow would have been £2,637,000 with net debt at 31 July 2005 of £17,142,000 as compared with £19,779,000 as at 31 July 2004. However, to reflect more accurately the restricted nature of the cash held for endowments the University considers the exclusion of this cash from the above figures gives a fairer view of the University's net debt.

The group figures include a re-classification of £168,000 of restricted funds held for the payment of scholarships from endowment assets to cash at bank and in hand and from specific endowments to restricted funds to ensure that the financial statements comply with SORP 2000 'accounting and reporting by charities'.

30. PENSION SCHEMES

The total pension charge in the financial statements reflects the costs incurred by Heriot-Watt University during the year of £5,640,000 (2003 - £5,295,000).

	Group	
	2005	2004
	£000	£000
The total pension charge is analysed as follows:		
Universities Superannuation Scheme	3,992	3,818
Lothian Pension Fund	1,551	1,408
Scottish Teachers Superannuation Scheme	97	69
	<u>5,640</u>	<u>5,295</u>

The pension costs are assessed in accordance with the advice of independent qualified actuaries using the projected unit method. The latest actuarial valuation of the LPF scheme was as at 31st March 2002, and the USS at 31st March 2002.

NOTES TO THE ACCOUNTS – continued

*Pension Schemes (continued)***Universities Superannuation Scheme**

The USS operates on a notionally funded basis. It is a multi-employer scheme and it is not possible to identify each institution's share of the notional assets and liabilities. Therefore, contributions to the scheme are accounted for as if it were a defined contribution scheme. The cost recognised within the results for the year is the contribution payable to the scheme for that year.

The scheme is contracted out of the State Earnings-Related Pension scheme.

The total contribution made for the year ended 31 July 2005 was £5,794,000, of which employer's contributions totalled £3,992,000 (2004: £3,818,000) and employee's contributions totalled £1,803,000 (2004: £1,880,000). The agreed contribution rates for future years are 14% (2004: 14%) for employers and 6.35% (2004: 6.35%) for employees.

Latest actuarial valuation	31 March 2002
Actuarial method	Aggregate
Rate of return on investments	6.0% per annum
Rate of increase in salaries	3.7% per annum
Inflation assumption	2.7% per annum
Market value of the notional fund at the date of last valuation	£19,938 million
Surplus on the fund	101%

Lothian Pension Fund

A full actuarial valuation was carried out at 31 March 2002 by a qualified independent actuary.

The major assumptions used by the actuary were:	2005	2004
Rate of increase in salaries	4.3%	4.4%
Rate of increase in pensions in payment	2.8%	2.9%
Discount rate	5.0%	5.8%
Inflation assumption	2.8%	2.9%

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

	Long term rate of return % p.a.	Assets at 31 July 2005 £000	Long term rate of return % p.a.	Assets at 31 July 2004 £000
Equities	7.3%	32,508	7.9%	23,111
Bonds	4.7%	2,853	5.4%	2,341
Property	5.4%	4,282	6.7%	2,923
Cash	4.5%	812	4.5%	4,069
Total	6.9%	40,455	7.2%	32,444

NOTES TO THE ACCOUNTS – continued*Pension Schemes (continued)*

The following amounts represent Heriot-Watt University's share of the scheme at 31 July 2005 and were measured in accordance with the requirements of FRS 17:

	2005	2004
	£000	£000
Estimated employer assets (A)	40,455	32,444
Present value of liabilities	53,680	43,469
Present value of unfunded liabilities	240	240
Total value of liabilities (B)	53,920	43,709
Net pension liability (A-B)	(13,465)	(11,265)

If the above amounts had been recognised in the financial statements, the University's net assets and general reserve would be as follows:

	2005	2004
	£'000	£'000
Net Assets (excluding pension liability)	73,755	69,861
Pension liability	(13,465)	(11,265)
Net Assets (including pension liability)	60,290	58,596
	2005	2004
	£'000	£'000
General reserve (excluding pension reserve)	24,734	22,991
Pension reserve	(13,465)	(11,265)
General reserve (including pension reserve)	11,269	11,726

Analysis Of Amount To Be Charged To Operating Profit

	Year to 31 July 2005	Year to 31 July 2005
	£000	% of payroll
Amount charged to operating profit		
Service cost	1,526	17.4%
Settlements and curtailments	7	0.1%
Total Operating Charge (A)	1,533	17.5%

Analysis Of Amount Credited To Other Finance Income

	Year to 31 July 2005	Year to 31 July 2005
	£000	% of payroll
Expected return on employer assets	2,360	27.6%
Interest on pension scheme liabilities	(2,558)	(29.9)%
Net Return (B)	(198)	(2.3)%
Estimated net revenue account cost (A) – (B)	1,731	20.2%

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

	Year to 31 July 2005
	£000
Actual return less expected return on pension scheme assets	4,800
Experience (losses) arising on the scheme liabilities	(12)
Changes in assumptions underlying the present value of the scheme liabilities	(6,822)
Actuarial (loss) in pension plan	(2,034)
Actuarial (loss) recognised in STRGL	(2,034)

NOTES TO THE ACCOUNTS – continued*Pension Schemes (continued)*

Movement In Surplus/Deficit During The Year

	Year to 31 July 2005
	£000
(Deficit) at start of the year	(11,265)
Current service cost	(1,526)
Employer contributions	1,551
Contributions in respect of unfunded benefits	14
Impact of settlements and curtailments	(7)
Net return on assets	(198)
Actuarial (losses)	(2,034)
(Deficit) at end of the year	(13,465)

History Of Experience Gains And Losses

	Year to 31 July 2005
	£000
Difference between expected and actual return on assets	4,800
Value of assets	40,455
Percentage of assets	11.9%
Experience (losses) on liabilities	(12)
Present value of liabilities	53,920
Percentage of the present value of liabilities	0.0%
Actuarial (losses) recognised in STRGL	(2,034)
Present value of liabilities	53,157
Percentage of the present value of liabilities	(3.8%)

NOTES TO THE ACCOUNTS – continued*Pension Schemes (continued)***Scottish Teachers Superannuation Scheme**

The STSS operates on a notionally funded basis. It is a multi-employer scheme and it is not possible to identify each institution's share of the notional assets and liabilities. Therefore, contributions to the scheme are accounted for as if it were a defined contribution scheme. The cost recognised within the results for the year is the contribution payable to the scheme for that year.

The scheme is contracted out of the State Earnings-Related Pension scheme.

The total contribution made for the year ended 31 July 2005 was £144,000 (2004: £117,000), of which employer's contributions totalled £97,000 (2004: £69,000) and employee's contributions totalled £47,000 (2004: £48,000). The agreed contribution rates for future years are 12.5% (2004: 12.5%) for employers and 6% (2004: 6%) for employees. (Effective from 1st October 2003 the employer contribution rates were increased from 7.4% to 12.5%).

The last actuarial valuation of the scheme for which information is available was at 31st March 1996. A further valuation of the scheme was carried out at 31st March 2001, and although an interim report has been issued, the final report from the actuary has not been published. The assumptions that have had the most significant effect on the valuations at both 31st March 1996 and 31st March 2001, and other relevant data, are as follows below.

Rate of return on investments in excess of rate of increases in salaries	2.0% per annum
Rate of return on investments in excess of rate of increases in pensions	3.5% per annum
Market value of the assets at 31st March 1996	£2,673 million

At the 1996 actuarial valuation date, which was carried out using the prospective benefit method, the STSS showed a deficiency of £142 million, which requires a supplementary provision by employers of 0.5% per annum for a period of 40 years. This is being effected through an adjustment to employers' contribution rates.

The 2001 valuation 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 2001, 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.

Supplementary Pension Scheme

The SPS operates on a funded basis. The scheme has no active members, with all the members of the scheme during the year being pensioners with pensions in payment.

The valuation of the SPS indicates a notional deficiency for which a provision is included in note 17. We were unable to obtain an actuarial valuation prior to the approval of the 2004-05 financial statements. The size of the scheme is considered insignificant to the financial statements as a whole.

31. POST BALANCE SHEET EVENTS

There are no material post Balance Sheet events.

NOTES TO THE ACCOUNTS – continued

32. CAPITAL COMMITMENTS

	Group	
	2005	2004
	£000	£000
Commitments contracted	1,559	1,406
Authorised but not contracted	-	690
	<u>1,559</u>	<u>2,096</u>

33. FINANCIAL COMMITMENTS

At 31 July 2005 there were annual commitments under non-cancellable operating leases as follows:

	Group	
	2005	2004
	£000	£000
Other:		
Expiring within one year	131	2
Expiring between two to five years inclusive	336	567
Expiring in over five years	3	-
	<u>470</u>	<u>569</u>

34. CONTINGENT LIABILITY

There are no material contingent liabilities.

35. RELATED PARTY TRANSACTIONS

The financial statements of the University include transactions with related parties. In accordance with FRS 8, these are reported where members of the Court disclose an interest in a body with which the University undertakes transactions which are deemed to be material.

The Interactive University is the global publishing and distribution company for the Scottish post compulsory education sector. It provides learning, technology and business services to enable Scottish educational institutions to deliver high quality educational programmes throughout the world.

Total sales to and purchases from Interactive University during the year were £1,176,000 (2004: £1,083,000) and £246,000 (2004: £297,000) respectively. At 31 July 2005 trade debtors included £691,000 (2004: £424,000) due by Interactive University to the Heriot-Watt University.

NOTES TO THE ACCOUNTS – continued**36. ACCESS FUNDS**

	Group		
	Mature Student Bursary	Hardship	Total
	£000	£000	£000
At 1 August 2004	112	550	662
Funding Council grants	55	367	422
Disbursed to students	(38)	(366)	(404)
Repaid to funding body	(103)	(462)	(565)
Balance unspent at 31 July 2005	<u>26</u>	<u>89</u>	<u>115</u>
Repayable to funding body	<u>-</u>	<u>-</u>	<u>-</u>

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

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¹ Lay Member of Court² Member until 31st July 2005³ Member from 1st August 2005⁴ Member until 16th March 2005⁵ Member from 12th December 2005⁶ Member until 30th November 2005

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