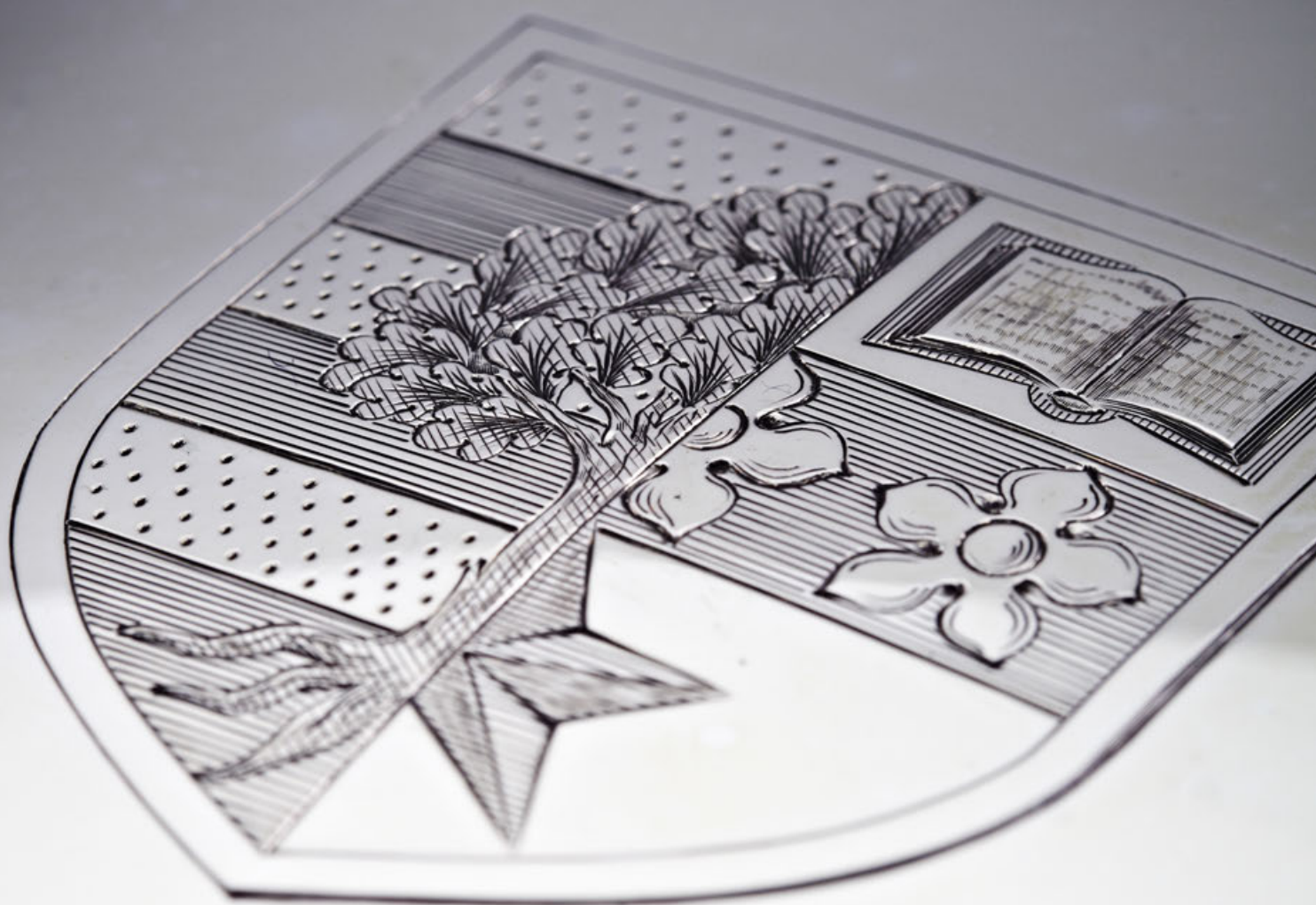


Reports and Financial Statements

*For the year ended
31 July 2017*





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Introduction by Principal and Vice-Chancellor

I am pleased to report that the University has further honed its distinctive strengths in developing highly employable students and impactful research outcomes across its global community during the last year.

Despite the significant uncertainties caused by the challenging external fiscal and political environment we have focused on ensuring a personalised experience for our students, growing partnerships with industry and employers, ensuring widening accessibility and multiple entry routes for undergraduate students, attracting high calibre academic and professional staff and delivering strategic infrastructure projects.

This year has seen the graduation of our first complete cohort of undergraduates studying in Malaysia and establishment of new funded research and research leadership there. Our mission as a highly distinctive and global university has been recognised through the accolade of being The Times and Sunday Times International University of the Year 2018. Our global standing in research has been recognised through our entry, for the first time, into the most eminent global research ranking, the Shanghai Academic Ranking of World Universities that marks out the top 500 universities in the world. In the UK, we won major recognition for our pioneering work and societal impact in British Sign Language in the Social and Community Impact Guardian Award 2017. Our Academics also had success at the Times Higher Education Awards 2017, where our scientists were recognized for the part they played in the "Research Project of the year: STEM", with ground-breaking work to develop highly sophisticated camera detectors for microscopes allowing diseases, such as cancer, dementia and diabetes, to be examined like never before; and where the work of Institute for Social Policy, Housing, Equalities Research, working on the impact of economics and policy changes on homelessness, was highly commended in the Arts, Humanities & Social Science Research Project category.

While we have many successes to report, as flagged last year, the expected cooling of some areas of the international economy and the highly competitive nature of some educational products affected the rate of our overall growth. As a result, during the year we embarked on and made significant progress in reducing our predicted 2018/19 forward expenditure base by 6%. This has included making reductions in costs base efficiency enhancements, through staff leaving under voluntary redundancy and in staff restructuring in Edinburgh Business School. Taken together, the slowing of our income growth and the recognition of costs associated with voluntary redundancy resulted

in a loss for the year of £1.4m. While the necessary completion of our savings plans are likely to depress financial performance in the coming year, our near-term forecasts are to return to surpluses that underpin the University's financial sustainability. We continue, also, to construct our financial plans to contain appropriate contingency to provide resilience and to afford the capacity for future strategic investment and development.

Our reputation as a distinctive university that operates an increasingly integrated global university has advanced significantly. This provides a platform for clear differentiation in our mission and for development of new educational opportunities. During the last year we have been strengthening the international nature of programmes and research. For example, with a significant expansion of student mobility between campus locations and intra-campus teaching which together offers greater flexibility in subject choice, location and mode of study. Under new leadership and a new Board, the Edinburgh Business School has introduced a new full time MBA with travelling student cohorts making use of our global footprint. In special partnerships we have undertaken new activities in gaining a leading provision in Scotland, for example, in offering a wide range of graduate level apprenticeships (working with Skills Development Scotland and with employers). We have expanded our collaborations with British Geological Survey through our joint Lyell Centre and furthermore with sportscotland through our joint National Performance Sport Centre, Oriam. In Dubai we have seen development in architectural engineering and in Malaysia further development of our prestigious programmes in actuarial science.

We continue to invest in its strategic future to develop student experience, enterprise culture and research. We were successful in raising a capital bond of £112M on debt capital markets with two US and one UK investor, repayable over 15-30 years at a competitive fixed interest rate. In recent months we have completed the first phase of major refurbishment of student learning spaces to meet the changed working environments needed and this will continue in the next year in the UK and for scheduled Dubai campus improvements. In the area of research and enterprise we will be embarking on development of a discovery and innovation building with concomitant

digital facilities – this will put design capabilities at the heart of our provision to ensure a modern, accessible learning and research environment. In particular we are also planning major multi-disciplinary research provision in artificial intelligence and robotics, bringing together social, technical and engineering sciences with a wide industrial partnership. The recruitment of leading researchers will continue with the launch of a Bi-Centennial Research Leaders Initiative. Looking ahead, we shall also complete the restoration of Panmure House, the home of Adam Smith, and its development as a place of debate, policy and public engagement through the Edinburgh Business School.

We are supported in our endeavours by many funding partners and value these partnerships, especially the Scottish Funding Council and Skills Development Scotland. In Scotland the Scottish Funding Council Outcome Agreement process remains an important tool to support our plans to deliver education, inclusivity and widening access. In Malaysia and Dubai we are pleased to work with, and gain the active support of, the Malaysia Qualifications Authority and the Knowledge and Human Development Authority, respectively. Our institutional commitment to diversity is underpinned through our values, through our leadership ethos and recognised through our Athena SWAN awards.

The Strategy Review in the Annual Report herein, describes our detailed achievements during the past year. I am pleased to acknowledge the valued support and guidance of the Court and the expertise, hard work and dedication of staff in the University that make Heriot-Watt such a special place for higher education and partnership working. During 2017/18 we shall be developing our refreshed longer term Strategy Plan for 2018 and beyond. I look forward to working with students, staff, alumni, funders and many partners across the world during this important process.

Our recognition this year of being the UK's leading integrated international university has meant we are now looking ahead to new opportunities. Our focus is both on continued refining of our operations to better serve students and academic staff across our global university and upon seeking and winning new income. Like Scotland itself, we are passionate about partnership and to drive our role as an enabler of excellence in education and impactful research in the wider communities where we are based, in Edinburgh, Orkney, Galashiels, Dubai and Putrajaya.

Professor Richard A. Williams
Principal and Vice-Chancellor
15 December 2017

Strategic Report



Background

HERITAGE

In 1821, when the School of Arts of Edinburgh was established, it was the world's first Mechanics Institute, the start of a worldwide movement that would revolutionise access to education in science and technology for ordinary people, with the purpose of addressing societal needs by incorporating fundamental scientific thinking and research into engineering solutions. As the institution developed into the Watt Institution & School of Arts (1852) and Heriot-Watt College (1855), its focus on “the practical application of knowledge and learning for the betterment of society” remained a defining characteristic. In 1966 the College became Heriot-Watt University, established by Royal Charter. Since then, it has continued to focus on innovating and responding to the needs of business and industry.

The University's Orkney campus opened in 1989, as part of the International Centre for Island Technology. By 1992 the last of Heriot-Watt's Edinburgh departments had located to its current purpose-built Edinburgh campus, amid 380 acres of parkland.

The Scottish Borders campus and the University's School of Textiles and Design, based in Galashiels, was born of the merger with the Scottish College of Textiles in 1998. In 2005, Heriot-Watt was the first UK university to create an overseas campus in Dubai's International Academic City. In 2014, Heriot-Watt opened its state-of-the-art campus in Putrajaya, Malaysia; serving the South East Asia region and beyond.

The University remains true to its heritage of creating and exchanging knowledge for the benefit of society, delivering teaching that is professionally relevant and careers-focused, and developing world-leading, innovative research that provides practical solutions to contemporary issues. It provides a distinctive education and a high quality student experience and now stands as a leading institution with an established reputation for high quality across both its teaching and research, continuing to grow as a university characterised by a commitment to excellence.

STUDENT NUMBERS, LOCATION, DOMICILE AND LEVEL OF STUDY

Heriot-Watt Group has 28,825 students. Their location, the domicile of those on Scottish campuses and the level of study are portrayed in the graphs below:

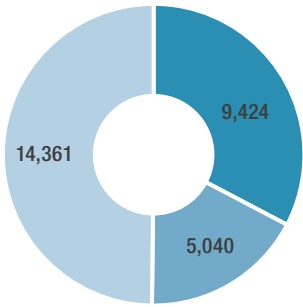
Beyond its campuses, Heriot-Watt University has an unsurpassed international in-country presence delivering degree programmes to more than 8,000 independent distance learning students and through an innovative Approved Learning Partner network where almost 6,000 students study in a network of 55 institutions in 39 countries.

INSTITUTIONAL STRUCTURE

The University has structured its teaching and research into five academic schools and one postgraduate institute:

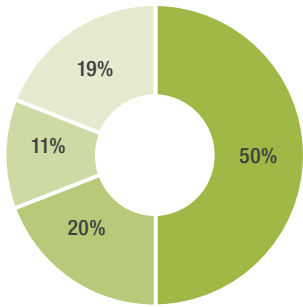
- > *School of Engineering and Physical Sciences*
- > *School of Energy, Geoscience, Infrastructure and Society*
- > *School of Social Sciences**
- > *School of Mathematical and Computer Sciences*
- > *School of Textiles and Design*
- > *Edinburgh Business School*

Study location



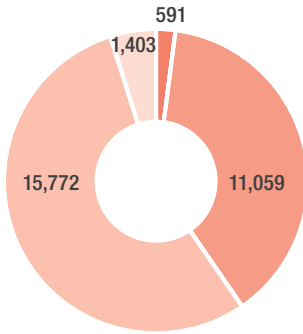
- Scottish campuses
- Overseas campuses
- International programmes

Domicile



- Scotland
- Elsewhere in the UK
- European Union
- Overseas

Level of study



- Foundation students
- Undergraduate students
- Postgraduate taught students
- Postgraduate research students

* In October 2016, the School of Management and Languages was renamed the School of Social Sciences.



VISION AND MISSION

Heriot-Watt's vision is to be: "world-leading within all its specialist areas of science, engineering, technology and business". This vision requires the University to be at the forefront of research and research-intensive education in the UK and internationally, and to deliver world-class innovative research and high quality teaching and learning, relevant to economic growth and development across business and industry.

To achieve this vision, Heriot-Watt's mission focuses on strengthening research intensity in the fields of economic and societal benefit, providing truly global education, delivering an excellent student experience and highly employable graduates. Although its ambitions are far reaching and its approach is globally focused, Heriot-Watt is committed to its Scottish roots and to playing an essential role locally and nationally.

STRATEGIC DIRECTION

The characteristics of global recognition and professional relevance are defining distinctions of the University and are the bedrock of its strategic direction. Maintaining this distinctiveness will require the University and its academic staff to:

- > exploit the synergy between excellent teaching and research in a global and professional context, and
- > perform at internationally competitive levels of creativity in research, scholarship and teaching as synergistic activities.

Underpinning this strategic direction is the University's operational focus on continuing to be a high performing, rapidly growing and financially sustainable institution.

STRATEGIC PLAN

The Strategic Plan 2013-2018 presents the University's direction and priorities for the five year period. The plan defines the University's ambitions, aims and objectives, and the pattern and scale of activities that will underpin its achievement. There are three key areas of focus in the strategic plan:

- > Learning, teaching and student experience;
- > Research intensification; and
- > Internationalisation.

Each one of these has clearly articulated aims and a number of key performance indicators which are discussed in the following sections.

During 2017/18 the University will be developing a refreshed longer term Strategy Plan for 2018 and beyond.

Learning, Teaching and the Student Experience



Heriot-Watt University has a longstanding reputation for providing highly employable graduates who have a distinctive professional orientation. It is also establishing an excellent reputation for the quality of student experience that it offers. This achievement has undoubtedly been influential in generating demand from students to study at Heriot-Watt. A distinctive feature of Heriot-Watt's provision is the diversity of locations and modes of study, underlining the importance of a key principle of the University's provision as one of "Identical academic standards; diversity of learning experiences".

At the core of the University's Learning and Teaching strategy is the vision to deliver world-leading, research-informed education and to be recognised globally for the high quality of our graduates. That vision will be fulfilled through four strategic objectives of enhancing student learning, reshaping the learning environment, developing staff and growing and diversifying the student population; each with a key aim and a set of priority areas for development.

The strategy is delivered through a partnership approach between students and staff in all locations and with external stakeholders such as employers and professional bodies.

The University perceives that a major risk to its learning and teaching strategy is the impact on the student experience that might arise from the failure of its student facilities to keep pace with the growth in student numbers. In response, informed both by our Learning and Teaching strategy and by our review of estate efficiency and utilisation, the University

has set out an ambitious portfolio of capital programmes. While the portfolio of capital investment addresses a range of estate needs, the earliest is related to the enhancement and expansion of teaching, learning and study space on our Edinburgh Campus.

The 2016/17 academic year brought progress in the form of:

- > enhancement and expansion of learning and study space, primarily through the major development of "Learning Commons" space that, in a convenient, central, accessible location, complements and supplements the Cameron Smail Library by providing over 200 seats offering a variety and choice of learning and study settings; with state-of-the-art digital learning and study facilities; and a focus on collaborative learning facilities with advanced collaboration and communication technologies;
- > the opening of Oriam, Scotland's National Performance Centre for Sport, on our Edinburgh Campus, where Scotland's top sportsmen and women will access facilities and support services pivotal for successful performance on the international stage; alongside the provision of extensive access for both students and the local community to the £33m world-class facilities, inspiring participation in sport or the enjoyment of a more active lifestyle; and
- > the opening of new residences on our Edinburgh Campus, providing 450 beds in a mix of five person flats and studio apartments, all with en-suite rooms.

The University's recent success in raising finance by way of a private placement bond in December 2016 has generated funds to enable it to commit to its immediate capital plans, including providing for increased quality and quantity of teaching and learning space to meet the needs of growing student numbers and of higher student expectations, reflecting the University's commitment to ensure that the learning and teaching environment we offer has the most up to date technologies and facilities. Projects underway or planned, include:

- > The alteration and refurbishment of the James Watt Centre, following significant stakeholder engagement, into a modern state of the art learning and teaching facility with complementary hospitality and conference facilities along with 130 new study spaces.
- > The construction, at a cost of c.£19m, of a Discovery and Innovation Centre: a pioneering innovation building, integrating twenty-first century learning and teaching spaces, research laboratories and workspaces, innovation and enterprise space, all developed around the latest models for "open space collaboration" and utilising the latest digital technology to accelerate innovation and foster the co-creation of ideas.

- > The modernisation of the Student Services Centre, to become the main point of contact for all international students, bringing together the 'Go Global' office ; Scholarships office; International Student Advisors office and existing Centre staff in one location; the creation, nearby, of a Student Wellbeing Office, where student counselling, student disability and support teams will be based; and the provision of a designated training room for Assistive Technology and a resource area adjacent to the very popular Learning Commons.
- > A £6m refurbishment project for the Library to transform it into a modern, flexible and comfortable learning environment, with over 1,000 study spaces, a variety of collaborative study spaces, double the number of accessible study rooms and improved layout of library stock.
- > Work across the University to upgrade a variety of Learning and Teaching spaces, including, the creation of a new 'mini' Learning Commons in the Postgraduate Centre; a rolling programme of refurbishment of existing student residences; and the enhancement of Student Union facilities.

The coming year will also see improvements to the Edinburgh Business School building; the refurbishment of the historic Panmure House, the last home of Adam Smith; and Edinburgh Business School's investment in the preparation of new learning materials.

Beyond the physical environment, during 2016/17, the University learning and teaching activities continued to place emphasis on the areas of:

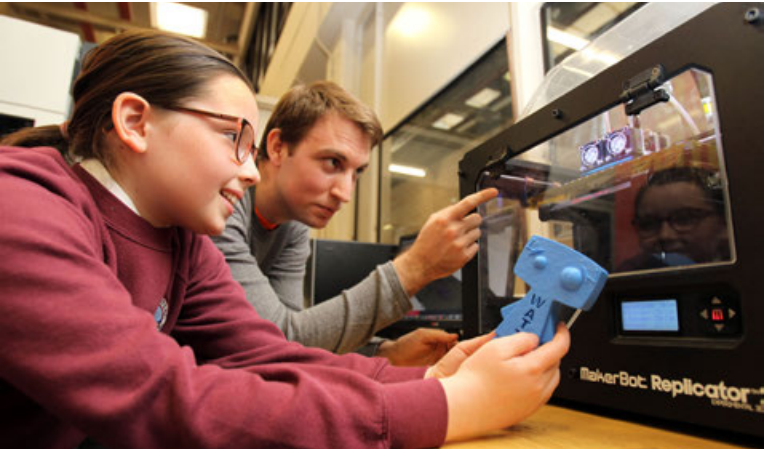
- > **A University wide retention strategy**, building on the recent overhaul of personal tutoring by: developing processes for identifying and supporting "at risk" students; the acceptance across the University that there shall be no unnecessary impediment to students seeking to change programmes; and improvements in our approach to student transition and induction.
- > **Increasing the number of students participating in the University's 'Go-Global' programme**, transferring to another campus location for a semester, a year or longer.
- > **Graduate attributes:** through a focus on an awareness-raising and engagement campaign for students as well as embedding those attributes in the curriculum.

The implementation of our Learning and Teaching strategy is monitored and evaluated annually through the University's Key Academic Performance Indicators:

Key Performance Indicator		Status, activity and progress towards target
Entry scores (undergraduate students)	an indication of demand for places from well qualified candidates, measured by the UCAS tariff of UK university entrants	Heriot-Watt displayed a steep upward trend, rising ahead of the general escalation of entry scores, until 2013, before mirroring the sectoral trend of stabilisation of students' entry scores. Our target to move from the second quartile of UK universities to the first quartile was achieved in 2012. Although we saw that eroded marginally in 2015/16, in the last year we recovered that position; and at 24th place among UK universities find ourselves, once again, sitting on the tail of the Russell Group and congruent with both the average entry scores for pre-1992 universities and for Scottish universities, and well ahead of the UK average.
Widening access – SIMD 1-40 student recruitment	an indication of the social diversity of the student population, generally measured in Scotland as the fraction of entrants from the 40% most deprived areas as measured by the Scottish Index of Multiple Deprivation (SIMD 1-40)	The University set itself the target of achieving at least 25% of Scottish entrants from SIMD 1-40 areas. That target was exceeded in 2014/15 with a step change in entrants that year, an achievement that has been broadly sustained since then. The concentration of SIMD 1-40 population in the conurbations of the West of Scotland and in Dundee creates an underlying regional catchment variation that marks Heriot-Watt's relative performance as particularly creditable.
Retention/ progression (undergraduate students)	an indication of the institution's effectiveness in engaging and supporting new students and meeting their expectation, measured by the fraction of university entrants continuing or progressing in the same university in the year after their entry	There has been a trend of very gradual long-run improvement in retention across the sector, with some marginal decline in more recent years. Although Heriot-Watt struggled to track that long term improvement, the performance of the 2013/14 entry cohort bucked the reversing sectoral trend and exceeded our own 93% target, set to move our performance from the third quartile to the second quartile of UK universities. The upturn to greater than 93% retention achieved by the 2013/14 entry cohort was not sustained in the following year, although there is evidence of another slight improvement in the most recent data, for the 2015/16 entry cohort. Retention and progression thus remain a focus of attention across the University.
Student satisfaction – overall satisfaction and average NSS score	reflections on students' learning experience by monitoring both overall satisfaction, as measured by the proportion of positive responses to the question on overall satisfaction in the National Student Survey (NSS); and by averaging students' analytical reflections on over all 22 NSS questions	Against a long-term trend of improvement in overall satisfaction, and results generally above or at the target level of 89%, 2017 has seen a significant fall in Heriot-Watt's performance to 83% satisfaction, likely related to a number of structural changes at the University. The University is committed to recovering to the target levels and has developed an action plan that, using the granularity of the response data, will be targeted at certain subject areas and certain aspects of learning, teaching and the student experience.
Graduate employment – employment or further study	an indication of the institution's effectiveness in preparing graduates for a successful future, measured by the fraction of UK university first degree graduates in employment or further study/ training six months after graduation	Somewhat indiscriminate in terms of the quality of employment or training and with most universities being bunched within a few percentage points of each other, this metric, nevertheless, still has wide currency in the sector. Heriot-Watt's improvement to above the UK and Scottish averages for the 2015 graduating cohort, consistent with meeting our target to achieve a position within the upper quartile of UK universities, is pleasing.
Graduate employment – graduate-level employment	an indication of the institution's effectiveness in preparing graduates for 'graduate level' employment	Heriot-Watt places an emphasis on benchmarking its performance where the employment of its graduates, six months after graduation, is classified as 'graduate level'. Over the planning period, performance has been at or around our 82% target, set so as to achieve a position around the upper decile of UK universities. Most recently, the swing was downward to 76.3%. With the benefit of a reconfiguration of our Careers Advice Services, the aim is to recover, once again, to the target level as soon as possible, a performance judged to be achievable and sustainable.



Research intensification



The underpinning principles of our research strategy are:

- > **to be world leading, within all our specialist areas of science, engineering, technology and business**
- > **to create and exchange knowledge for the benefit of society, and,**
- > **to strengthen research intensity in fields of economic and societal benefit.**

Establishing our fundamental strategic target as being associated with growth in research income, as a proxy for research intensity, the University's strategic plan set ambitious targets for the growth in research income from under £23m earned in 2011/12, to a target of £40m per annum by the end of 2018. This target was set to be consistent with the performance of our benchmark group, the small and medium-sized research intensive universities that formerly constituted the '1994 Group'.

Brexit, the launch by the UK Government of its Industry Strategy Challenge Fund and the growing level of investment in the Global Challenges Research Fund have all created a new landscape for research funding. In response to this changing dynamic we have created three challenge led multi-disciplinary themes in sustainable energy, digital transition and resilient communities to bring together expertise from across the University.

As high quality staff remain central to everything we do we have refocused our staff recruitment strategy, now named "Bicentennial Research Leaders", on areas with the greatest potential for growth. Building on our recent successes in robotics (see Achievements section) and our ongoing

development of the Lyell Centre in partnership with the British Geological Survey initial new areas for targeted investment will major on robotics and geothermal energy.

We have continued to build on our excellent track record of translating our research into useful outcomes. Highlights for the current year include: Professor Bhaskar Sen Gupta, working in collaboration with the Bangladesh Green Energy Foundation, opening the world's first fully autonomous, solar-powered plant to safely remove arsenic from a local water supply in the Comilla district of Bangladesh; Professor Suzanne Fitzpatrick has played a leading role in improving homelessness legislation in all three countries in Great Britain, with the Scottish legislation in particular winning international acclaim; in the area of Marine Biodiversity, Dr Bill Sanderson's group worked with Glenmorangie distillery to reintroduce native European oysters to coastal waters in the Firth of Forth.

Heriot-Watt spin-outs continued to grow through securing investment – Optoscribe, a world leader and global supplier of glass-based integrated photonics components, closed a significant series B investment round of £1.8m and Chromacity, a manufacturer of ultrashort lasers across the near and mid-Infrared, successfully closed a second seed investment round of £400,000 to expand its manufacturing capabilities and grow international sales.

Entrepreneurship is an area in which the University is investing heavily, and we recently introduced the Heriot-Watt Enterprise Journey which will provide an insight into taking an idea and scaling it into a successful company. We will be delivering a global extra-curricular

enterprise education: from one-day bootcamps and workshops, to entrepreneur visits, pitching sessions and challenge-led hackathons.

The impact of this new enterprise strategy is far reaching, and it represents not only the future of company formation and commercialisation here at the University, but also the development of global-thinking early-stage entrepreneurs.

We have also opened a new Enterprise Hub, which is a dedicated area for people to access support and be fully immersed in the Heriot-Watt enterprise ecosystem. In addition, we have committed to creating a new c.£19m Discovery and Innovation Centre, which will open in 2019. This investment signals an expansion of our entrepreneurial culture from our academic body to include our research staff and students. The initiative will span all five of our campuses.

These successes have supported the development of new business partnerships and funding relationships. In April 2017, we announced a new five-year, £2.5m partnership between Total and the Institute of Petroleum and Engineering.

Despite Brexit, we have remained active in all EU research funding schemes having secured £7.43m in new funding from Horizon 2020 including three prestigious awards totalling £4.75m from the European Research Council.

The biggest success of the year has been in Robotics where we have secured at least £23m through the innovation strand of the Edinburgh and South East Scotland Region City Deal to develop the UK's National Robotarium. In addition to this we have led a successful £36m bid to the Engineering and Physical Sciences Research Council to create a UK Robotics and Artificial Intelligence Hub for Offshore Energy Asset Integrity Management.

The impact of our research outputs on our scientific peers is also gathering pace and has resulted in an improvement in our ranking in the Times Higher Education World University Ranking, and for the first time we have entered the highly selective Shanghai Jiaotong University ranking of World Universities.

The effectiveness of our strategic plan in relation to research intensification is monitored and evaluated through the University's Key Research Performance Indicators:

Key Performance Indicator		Status, activity and progress towards target
Income from research grants & contracts	primary indication of the volume and scale of research projects being undertaken	Heriot-Watt's performance over the strategic plan period has seen appreciable income growth and an improvement in its relative position. The pipeline for future income, represented by the value of new research awards having exceeded £40m in 2014/15 and 2015/16, was a positive indicator of the likelihood of almost doubling our research grant and contract income to £40m by 2018. However, with those awards reaching only £30m in 2016/17, we now have a lower expectation of achievement of the £40m income target by 2018. From a financial statement perspective, the University's unusually high number of grants and contracts from non-government sources that lack performance conditions, leads to likely fluctuation in reported revenue, so adding to the uncertainty of the achievement of the target.
Research student numbers	significant indication of the volume of research being undertaken	Heriot-Watt has seen an appreciable improvement in its performance to 2.0 PGRs per academic staff, a creditable performance. The University currently has 825 active doctoral degree students, and is optimistic that we will reach the target of 900 students by 2018.
Doctoral degree awards	indication of the scale of outputs from research in the form of trained researchers	With 2016/17 continuing the trend of growth in doctoral student numbers over recent years, and further actions in hand to promote timely PhD completions, we remain on track to achieve the target of 200 annual doctoral awards by 2018.
Research output (publications)	significant as an indication of the scale of the major output of academic research	There has been a trend of modest but sustained increases by Heriot-Watt from the mid-2,000 outputs p.a., tracking the rising UK and Scottish averages, but falling gradually further behind the faster rising pre-1992 university average. Heriot-Watt's 2.81 publications per academic and research staff compares favourably with the UK median of 1.05 and would rank the University within the top 30. While progress toward the target of 2,000 outputs p.a. will undoubtedly be fed by planned growth in our active academic research staff, current performance and the prevailing trend lead to a low expectation of achievement of the 2018 target.
Research impact (citations)	indication of the impact of published research output by measurement of the number of citations in subsequent publications by others in the field	In the years leading up to the most recent result, Heriot-Watt exceeded the UK university average and came close to reaching its 2018 target – to increase the value of the Field-weighted Citation Index for Heriot-Watt to 1.7, a clear long-range settled trend of improvement, comparable to the current UK pre-1992 university average, consistent with our objective to enhance the University's position in international rankings, to which the citations metric is particularly critical. A modest fall, to 1.5, observed in the most recent year, most likely reflects some inherent volatility in this measure.
Research income from industry	indication of the value placed on the research by industry and commerce, including its potential in relation to commercial knowledge exchange	When we set out on our strategic plan, we set ourselves a target of maintaining research income from private sector business and industry as a constant proportion of the rising level of total research income. However, an adverse trend over recent years reflects the extent of our dependence on the oil and gas sector and the severity of current challenges for that sector. There is a low expectation of regaining lost ground until there is a recovery in oil prices; and so no expectation of achieving our target by 2018.

Internationalisation



For more than a decade, the University's rate of growth of income from international student fees – being very much faster than any UK or Scottish benchmark – coupled with the breadth of its international presence and the number of international students, has set Heriot-Watt apart from other UK Higher Education Institutions. Heriot-Watt has a strong track record of extending access to its degree programmes internationally, supporting students to achieve high quality awards through partnerships with overseas institutions and flexible modes of study such as Independent Distance Learning. The addition of international campuses in Dubai (2005) and Malaysia (2013) has strengthened significantly the University's international presence. In the past few years, the establishment of a global student mobility strategy 'Go Global' is providing opportunities for increasing numbers of students to transfer and study between campuses, adding value to the student experience.

The University set itself an ambitious target of doubling the scale of its international activities over the five years of its strategic plan, doubling its income from £45m to £90m; it is on track to achieve that target. In setting out to develop Heriot-Watt as an international university the key aims are:

- > Building on success in Dubai; and securing the success of the Malaysia Campus;
- > Enhancing the internationalisation of research and knowledge exchange activities;
- > Ensuring that Heriot-Watt University qualifications are recognised and respected internationally, providing entry to jobs worldwide;

- > Facilitating international mobility for Heriot-Watt students and staff.

During 2017, Heriot-Watt's internationalisation achievements were recognised when it was named as The Times & Sunday Times 'International University of the year'. In March 2017, the Chinese Ministry of Education (CSCSE) awarded Heriot-Watt University their Global Strategic Partner Award, recognising the quality of the University's partnership work in China. This year also saw a significant improvement in our ranking in the Times Higher Education (THE) World University Ranking and, for the first time, we entered the highly selective Shanghai Jiaotong University Academic Ranking of World Universities.

Heriot-Watt University participated in welcoming international students from across the globe this year through its role in 'Scotland Welcomes the World', a national campaign to celebrate the value and impact of international students and staff in Scottish Universities and across the nation; and to show Scotland's national character as inclusive, diverse and welcoming.

The University's award winning 'Go Global' scheme, promoting inter-campus transfers for undergraduate students is becoming an important feature of internationalisation at Heriot-Watt. Increasingly, students identify this opportunity as a reason for choosing Heriot-Watt as a place to study and participation in the scheme continues to increase, alongside European exchanges and other study abroad options with partner universities. The University won a Gold award from HEIST (which celebrates the excellence and innovation of everyone involved in education marketing) for its 'Go Global' campaign.

The Dubai campus, established in 2005, continues to grow both in terms of the range of academic programmes offered, most recently to include Architecture, which is not currently offered on any of our other campuses; and in the number of students attending, now approaching 4,000, including a growing number of PhD students.

2016/17 marked five years of operation in Malaysia, with our activities having grown to 1,500 students and 200 staff. Representative of the University's objective to work in collaboration with universities around the world in delivering high impact research, the first major research grant in Malaysia was secured with the award of a £2.2m Newton Fund grant to a consortium made up of Dearman, the clean cold technology company, Green Data Center LLP, Heriot-Watt University and Universiti Teknologi Malaysia. The project brings together innovative technologies developed in Malaysia and the UK, aiming to improve the sustainability of data centres by changing the way they are cooled, with an aim to reduce their energy consumption by up to 50%, improve energy security and reduce localised emissions caused by diesel powered backup generators.

We regularly see examples of our staff working across our campuses. This year, the University has seconded a Professor from Edinburgh to Malaysia as Director of Research, with a remit to drive research and development at the Malaysia campus. A key priority is to develop quality research relevant to the needs of Malaysia and the wider region, establishing collaborative research partnerships with regional universities, industry and research funders. The University will forge

stronger connections between researchers across all our campuses and develop the cohorts of PhD students in all locations.

Our recently published vision for our future in Dubai draws on the distinctive characteristics of Heriot-Watt University, as being Global, Specialist, Expert, Innovative and Connected. In Dubai we plan to continue to grow our student population. This growth will benefit from our successful 'Go Global' campaign and our efforts to continually improve and expand learning facilities; but will be fuelled in large part by our intention to refresh and supplement the academic portfolio, to ensure that the programmes being offered are attuned to shifting global and local student demand. In addition, we will see growth in postgraduate research students from the accelerated development of our global research activity. The student number growth

and the associated growth in staff numbers, together with the enhancement of the learning environment will be accommodated by local partner capital investment.

We are confident that Malaysia will continue to prove a popular choice for 'Go Global' students. In 2016/17, 80 students from the Edinburgh Campus went to study in Malaysia. This is not only beneficial in terms of experiencing other cultures and studying and working in inter-cultural teams, but also in terms of developing the graduate attributes that are highly valued by employers and developing skills for future careers. The Malaysian government is highly supportive of the University's success in this area.

Given the scale of our international operations, we are particularly attuned to the range of risks that this activity presents, including those

relating to student recruitment, programme accreditation and the provision of facilities to meet student needs. The University maintains risk registers in relation to the general international environment, specifically with regard to Dubai and Malaysia. We identify, review and manage risks on a regular basis in relation to key projects, as well as taking a view across the whole strategy. This includes 'horizon scanning' of the political and economic environments in Dubai and Malaysia, as well as in other key markets of interest to Heriot-Watt.

The effectiveness of our strategic plan in relation to internationalisation is monitored and evaluated through the following Key Performance Indicators:

Key Performance Indicator		Progress
Income from international (non-EU) student fees	significant as an indication of the scale of involvement in education of non-EU students and the value placed on the education by international students and their sponsors	Heriot-Watt continues the trend, established in the mid-2000s, of accelerating very significantly ahead of sector norms, with new impetus in very recent years as the new income stream from our Malaysia campus starts to build up. Heriot-Watt maintained last year's position as 21st in the UK for the absolute value of income, behind the majority of much larger and mostly very strongly branded Russell Group universities. If normalised, expressing non-EU student fee income as a proportion of total income, HWU's 34% sets it very far apart for the UK average of 10.7% and places the University 2nd in the UK. Progress towards the £90m pa target saw growth resume in 2014/15 and be sustained in 2015/16, with a trend that is estimated to reach the 2018 target.
Trans-national education – students studying outside the UK	significant as an indication of scale of presence in delivery of higher education outside the UK	Over the last two years, even with the growth in student numbers at our own international campuses, our overall trans-national student numbers have remained around 15,000. While that has maintained our place as 5th in terms of the number of students studying outside the UK, we are unlikely to meet our ambitious target within the original timescale. The University is undoubtedly facing competition from other large players and from a growth in the number of institutions participating in trans-national activity. However, as indicated by the previous KPI, erosion of numbers has not been mirrored in terms of erosion of revenues; reflecting both the value of operating on our own campuses and a shift away from high volume-low revenue partnerships to more rewarding activity with collaborative partners and particularly in International Distance Learning. Looking forward, the University has ambitious plans to maintain planned growth in international activity by strengthening the global nature of its post-graduate programmes, offering greater flexibility in subject choice, location and mode of study. In addition, the University is seeking to grow partnerships from its international hubs in Dubai and Malaysia.
International students studying in the UK	significant as an indication of the scale of participation by students from outside the UK (both rest of EU and non-EU), the success of institutions in attracting these students, and the international diversity of the student cohort	The trend at Heriot-Watt in attracting students from abroad to its UK campuses has continued last year's downward turn. This is primarily associated with changes to UK immigration policy which have forced the University to withdraw from its partnership with West London College, meaning the loss of students, mainly from overseas, from fashion and management undergraduate programmes and from the full time MBA programme. The University has, in place, plans to invigorate the recruitment of overseas postgraduates, to its UK campuses, through the introduction of new and refreshed taught post-graduate programmes, including, for the first time at our Edinburgh campus, a full-time on-campus MBA. It seems unlikely, particularly as the West London College students leave us at the conclusion of their studies this year and next, that international student numbers on our UK campuses will recover from the current 3,250 students to our original target of 4,300 students by 2018.

Principal risks and uncertainties

In the foregoing sections, we have recorded the main operational risks associated with delivery of the key elements of the Strategic Plan. There are, however, two overarching significant strategic risks and one emerging risk that the University currently faces:

- > The first of these is the risk that we fail to achieve our income targets. The source of that risk is diverse, but includes risks around Scottish Funding Council funding, the impact of government immigration policy on our recruitment of overseas students to Scotland, the global economic downturn in key functional and geographic markets, uncertainty relating to Brexit and acute competition in overseas markets. We have sought to mitigate these risks by ensuring that our student offering remains attractive, by ensuring that our programmes remain attractive, for example through strengthening the global nature of our programmes; offering greater flexibility in subject choice, location and mode of study; and the introduction of new and refreshed taught post-graduate programmes, including, for the first time at our Edinburgh campus, a full-time on-campus MBA. During the year, the University recognised that these, alone, were insufficient to fully mitigate the risk associated with income shortfall, so instituted a cost saving plan to bring about permanent reductions in the cost base, including a voluntary redundancy scheme.

Our financial plans continue to contain contingency and discretionary elements to provide resilience and flexibility, including explicit contingency against failure to achieve planned tuition fee and net research income; a rolling process of financial performance review of individual academic programmes; borrowing with fixed-interest rates to give greater certainty over debt servicing costs; discretionary elements in potential capital investments; and gateway reviews to maintain future flexibility over decisions to commit capital expenditure across the planning period in the event that financial circumstances or risk profiles change.

- > The second of these is the broader uncertainty arising from the UK's decision to leave the European Union. The consequences of that risk are varied, ranging from the risk to income from EU students and EU Research; through human capital risks associated with the almost 300 EU nationals employed by the University and financial risks arising from economic uncertainty and currency fluctuation; through to risks arising from regulatory compliance (Trade regulations, taxation, procurement, Health & Safety). The University has sought to manage and mitigate those risks through close monitoring of all available sources of information by a recently formed "Brexit Group" and the development of a consequential Brexit Action Plan.
- > The third of these is an emerging risk that relates to the potential growth in employment costs associated with the University's exposure to defined benefit pension schemes. Although the 2017 Universities Superannuation Scheme actuarial valuation is not yet complete, on the basis of the proposed assumptions, the trustee believes there is a deficit of just over £5bn – similar to the figure assessed in March 2014. However, the cost of funding future pensions promises has increased by 35%, which may lead to a requirement for a revised deficit recovery plan for the scheme and, potentially, higher employer contributions. Consideration of any changes to the scheme, such as those around scheme benefits and contribution levels will follow completion of the formal actuarial valuation later this year; and would be subject to consultation with employee members and employers. The University will contribute to the consultation on the proposed actuarial assumptions for the valuation; and on any subsequent consultation on scheme design or contributions that may arise therefrom. The Court will more fully consider the implications of this risk during the coming months.

On page 26, as part of the Corporate Governance Statement, there is a more general description of the University's approach to risk and the framework of risk management.

Corporate Governance Statement

INTRODUCTION

The University aims to achieve best practice in all aspects of its governance. This statement describes the principal governance provisions which are currently in place in support of this aim. The University Court keeps these provisions under review to take account of evolving best practice, and to remain responsive to the needs and expectations of the University's stakeholders. The University seeks to ensure that it conducts its business in accordance with the seven principles identified by the Committee on Standards in Public Life: selflessness; integrity; objectivity; accountability; openness; honesty; and leadership. The commitment of the University Court to these principles is explicit in the Court's Statement of Primary Responsibilities and in advice provided to prospective and new members of the Court and its committees.

The powers of the University and the Court, as its governing body, derive from the University's Charter and Statutes. These are the University's primary constitutional documents. The Charter defines the objects, powers and responsibilities of the University, its principal officers, and the functions of the Court and the Senate of the University. The Statutes prescribe the supporting requirements for enactment: the membership, powers and functions of the Court and the Senate; the appointment, powers, duties and conditions of service of officers and members of staff; and provisions for the formation and approval of the Ordinances and Regulations.

According to the University Charter, subject to the terms of the Charter and the Statutes, and to the powers reserved to the Court, the Court delegates to the Senate all of its powers in relation to academic work and standards. The Senate is therefore the executive body responsible for the academic work and standards of the University. The supporting Ordinances to the Charter and Statutes further clarify the responsibilities delegated by the Court to the Chair of Court, the Principal and the Secretary of the University.

Members of the Court are charity trustees, as defined by the Charities and Trustee Investment (Scotland) Act 2005.

GOVERNING BODY

Responsibilities and delegated authority

The University's Charter defines the powers of the Court as the governing body of the University with general control of the management and administration of the University. The key functions of the Court are to:

- > be ultimately responsible for oversight of the affairs of the University;
- > set and approve the University's strategic direction, vision and mission;
- > ensure the effective management and control of the University's affairs, property and finances through the establishment of systems of internal control;
- > ensure the effective management and administration of the University's staff and the students;
- > determine the structure, staffing and overall composition of the University; and
- > appoint the Chancellor, Pro-Chancellors, Principal, Vice-Principal and the Secretary of the University.

The Court Statement of Primary Responsibilities sets out clearly the responsibilities of the Court, aligned to guidance provided in the Scottish Code. The Statement is published in full at: <http://www1.hw.ac.uk/committees/court/statement-of-primary-responsibilities.pdf>.

The following responsibilities cannot be delegated by the Court to any other body: to determine the objects of the University; to make final decisions on issues of corporate strategy; to appoint or dismiss the Chancellor, a Pro-Chancellor, the Principal, the Vice-Principal or the Secretary of the University and determine their terms and conditions of appointment; to approve the annual business plan, budget, annual report or annual accounts of the University; to make or amend the University Charter, Statutes or Ordinances; to appoint the University's External Auditor; and to decide the remuneration of any member of the Court. The Court, through its Ordinances

in support of the Charter and Statutes, has delegated authority to the Principal and Vice-Chancellor to: lead development of the University's vision, mission, Strategic Plan and supporting Key Performance Indicators, Financial Plan and Values; provide the academic leadership of the University and leadership of the Senate; determine the operational and staffing structure of the University; ensure the existence of appropriate policies and other controls required for delivery of the University's objects and compliance with all relevant legislation and legal and contractual agreements; represent the interests of the University externally; assume primary responsibility for health and safety throughout the University; and undertake other responsibilities as may be determined by the Court which are commensurate with the role of Principal, Chief Accounting Officer and Chief Executive Officer of the University.

In discharging its responsibilities the Court met seven times during the year 2016/17, including at two full 'Strategy Discussion Days'. The first Strategy Discussion Day in the year, held in November 2016, focused primarily on detailed review of the University's performance against the agreed set of Key Performance Indicators aligned to the Strategic Plan and associated institutional strategic risks. Thereby, the Court was provided with background contextual information upon which to draw when considering the 2017 Four-Year Financial Plan.

The Court Strategy Discussion Day held in May each year provides the opportunity for strategic discussions aligned to key institutional priorities. The primary topics for discussion at the May 2017 meeting were new research opportunities and developments, the Learner Journey – in a Scottish higher education policy context, and the transition plan to 2020 and beyond for the Dubai Campus. At that meeting the Court also approved revised Articles of Association and Member Agreement with its wholly-owned subsidiary company, the Edinburgh Business School.

At each of its ordinary meetings in the year being reported, the Court received an executive briefing from the Principal, which updated the Court on topical higher education sector policy issues, matters concerned with the work and progress of the University and the work of the University Executive. In addition, the Court received a regular full report from the Senate and reports from each of the committees of the Court which had met in the preceding period. The full reports from the Court committees, which are presented by the respective committee Chairs are provided to the Court for information, for comment and, where appropriate, for approval. At each ordinary meeting of the Court, the President and the Vice-President Student Union members of the Court are provided with an opportunity to update the Court on items of news and issues of interest to the Student Union and the students it represents. The Court receives the annual report of the Heriot-Watt University Student Union.

The Higher Education Governance (Scotland) Act was passed in 2016. The key provisions of the Act relate to: advertisement, election, appointment, tenure and remuneration of the Chair of Court; composition of and elections and nominations to the Court; composition of and elections to the Senate; and the definition of Academic Freedom. While a few provisions of the Act came into force from 30 December 2016, a transition period applies to many others. The latest date by which full compliance must be met is the end of December 2020. During 2017 the University, led by the Constitutional Review Group established by the Court, has been considering what changes will need to be made to the University's Charter and Statutes to enable full compliance with the Act. This work will continue through the academic year 2017/18. Following approval by the Court, revisions to the University Charter and Statutes must be submitted to the Scottish Government and the Privy Council Office for approval.

Court membership

The Court comprises twenty five members including the Chair, who is one of the thirteen independent lay members of the Court who form the membership majority. A further ten members, both internal and external to the University, have been directly elected to the membership and a further two are ex-officio members. The members of Court are listed on page 22. While a governing body membership of twenty five members is at the upper limit of good governance practice, this number of Court members ensures that there are a sufficient number of individuals with collective broadly based skills and experience available to support the standing Committees of the Court. The University's constitutional rules require that each standing Committee shall include in its membership at least three members of the Court.

Elected members include those from the student body, the alumni body, the Senate and the wider staff of the University. Together with the appointed lay members and the ex-officio staff members of the Court, those members contribute to the wide range of perspectives brought to the work of the Court. This diversity of experience enhances the effectiveness of the Court.

A register of skills is maintained for the appointed lay membership and this information informs the decisions of the Governance and Nominations Committee, both in determining the skill sets and experience sought through advertising of forthcoming vacancies, and in the recommendations for succession planning and appointments that it makes to the Court.

In addition to the Principal and Vice-Principal, who are members of Court, regular further attendees at meetings of the Court include the Secretary of the University (who is Secretary to the Court), the Director of Governance and Legal Services, the Director of Finance, the Vice-Principals (Dubai) and (Malaysia)

and those in Deputy Principal roles. This ensures that relevant additional advice and expertise is readily available to the Court when required during meetings. As and when particular agenda items require input of specific knowledge or expertise to add value to the discussion and the decision-making process, other members of the executive management team have been invited to attend part of an ordinary meeting of the Court to contribute to the discussion on that item of business. During 2016/17, all non-Court members of the University Executive, together with independent lay members of each of the Court's standing committees, were invited to attend Strategy Discussion Day meetings of the Court as full participants at those events.

Equality and Diversity

The Court continues to encourage diversity in its membership, whether this be through independent lay member appointments or encouraging a full diversity of individuals to stand for election in elected positions.

The Court has been very successful in recent years in achieving incremental positive change in the gender balance of the Court membership. In the reporting year, 54% of the appointed independent lay members of the Court were female.

The proportions of female members across the independent lay membership of the standing Committees of Court in 2016/17 were as follows: Audit & Risk 100%, Finance 33%, Global Student Liaison 50%, Governance & Nominations 66%, Remuneration 60%, and Staff 66%. The Court receives an annual report on the gender diversity of Court and Court committee memberships each year.

Members of Court

The following persons served as members of Court during the year to 31 July 2017, and up to the date of approval of these financial statements.

Chair of Court

Dame Frances Cairncross DBE, FRSE¹

Deputy Chair of Court

Mr Tony Strachan MBA, FCIS¹

Principal & Vice-Chancellor

Professor Richard A. Williams OBE, FREng, FRSE

Vice-Principal

Professor Julian D C Jones OBE, FRSE, FOSA, FlnstP, PhD

Senate

Professor Patrick Corbett BSc, MSc, PGDip, PhD, DSc, FRSE, FGS

Dr Amos Haniff BSc, MSc, PhD, MAPM, MCIOM, PGCAP

Professor Isabelle Perez Licence, Diploma, MITI, MIL

Professor James Ritchie BSc, MSc, CEng, FIMechE, MIET, FHEA²

Staff

Ms Pamela Calabrese MA, BA³

Ms Jane Queenan LLB, MBA⁴

Mr Tom Stenhouse

Dr Gillian Menzies BEng, PhD, CEng, CEnv, MEI, FHEA⁵

Dr Amanda Lyness BSc, MSc, PhD⁵

Graduates

Ms Trish Gray MBA, BSc⁴

Mr Roger Murray BSc, MEng⁹

Student Union

Mr Diarmuid Cowan MA

Ms Eloise McNeaney MA³

Ms Aashna Bakshi BA⁶

Co-opted

Ms Tracey Ashworth-Davies BSc¹

Ms Lucy Conan BA¹

Mr Grant Innes FICHEM¹, BSc¹

Ms Morag McNeill LLB, LL.M, DipLP¹

Mr Andrew Milligan BSc¹

Professor John Perkins PhD, CBE, FReng, FICHEM¹, FIET, FIMA¹

Ms Dorothy Shepherd CA, MBA, BAcc^{1,8}

Ms Jandy Stevenson FCA, BSc¹

Professor Ian Wall DSc, FRICS, Hon FRIAS, FRSE¹

Mr Graham Watson LLB, CA, FRSA¹

Ms Rio Watt C.Ed^{1,7}



Effectiveness of the Court

An annual Court Effectiveness Review was conducted in the reporting year. Key outcomes of the review included recommendations which aimed to enhance the focus of the Court on strategic discussions and mechanisms to enable this. A range of recommendations proposed ways in which communication could be enhanced, including communications into, within and out of the Court, initiatives aimed at increasing the visibility of the Court and engagement of its members with internal and external stakeholders, and recommendations with the intent to improve engagement between the executive team and the Court, to promote greater openness and transparency. Recommendations also included augmentation of the Court induction and development processes with the promotion of small group visits to academic Schools to promote both engagement with the academic community and deeper understanding of the University's core academic activities. The Court agreed to adopt the recommendations which will be implemented in 2017/18.

Effectiveness of the Senate

In 2016/17, steps continued to ensure and enhance the effectiveness of the Senate. Each meeting of the Senate has a strategic focus, with themed discussion on a strand of the University Strategy. Following the Midpoint Review of Senate Effectiveness in 2015/16, a new academic governance structure was agreed by the Senate and came into effect on 1 August 2017. The new structure is supported by a suite of documents: a clearly defined 'Senate Statement of Primary Responsibilities and Delegations'; Standing Orders for the Senate and the Standing Committees of the Senate; and an Attendance Policy for Senate and the Committees. An induction programme for members of the Senate is also in place from the start of Session 2017/18, with an emphasis on the privilege of membership of the Senate and the importance of good academic citizenship.

Induction and development opportunities for members

A two day induction programme provides support to all incoming new members of the Court and its standing committees each year. Current members may use this opportunity to refresh their knowledge and members who reach the end of a period of appointment must re-attend Court induction at any renewal point. Opportunities are taken throughout the year to increase members' knowledge and understanding of the University's work and the governance and policy environment in which it operates, through tailored presentations and discussions, "show and tell" events or guided tours.

Court and Court committee members are also regularly informed of upcoming seminars and conferences which are relevant to higher education governance, for example, those provided by the Leadership Foundation for Higher Education (LFHE) through its Governor Development Programme. Court members are also informed via regular briefings of new publications and news items of relevance. The programme of evening meetings throughout the year which are supplementary to the scheduled ordinary meetings and Strategy Days of the Court provide further future opportunities to develop Court members' knowledge and understanding of issues relevant to the University and to higher education more widely, thereby enhancing their effectiveness in their governance role.

Committees of the Court

The standing committees of the Court assist the Court in discharging its responsibilities in the governance oversight of the broad areas of: human resources; estate and campus development; finance and asset management; risk, systems of internal control and audit, student representation and engagement, and effective governance. The Terms of Reference of committees of the Court are approved by the Court, ensuring that there remains clarity around the delegated powers and lines of responsibility between the Court and its committees. The membership of the Committees of Court is listed on page 24. The standing committees of the Court are described below.

- > The Emergency Committee of Court, which is chaired by the Chair of Court, may consider delegable items of business and take decisions on behalf of the Court during the summer recess, or as and when any urgent matter might require attention between ordinary scheduled meetings of the Court.
- > The Audit and Risk Committee met seven times during the period reported with the External and Internal Auditors sitting in attendance at each meeting. The Audit and Risk Committee provides independent oversight of, and advice to the Court on: the adequacy and effectiveness of the University's systems of internal control (including financial systems, accounting procedures, measures to control the risk of fraud or malpractice); risk management arrangements; compliance with statutory Scottish Funding Council and other requirements; and governance arrangements to promote efficiency, effectiveness and value for money. The Committee oversees the process for the appointment and performance monitoring of Internal and External Auditors, and oversees audit review programmes and implementation of emerging recommendations.

- > The Finance Committee met seven times during the period reported. The Committee's primary responsibilities include reviewing, overseeing and advising the Court on: the overall financial strategies of the University; financial forecasting and performance; the University's treasury activities, including investments, borrowing commitments and borrowing terms; fundraising; working capital management; and the financial affairs of the University's trading and commercial activities. The Committee reviews and makes recommendations to the Court on business plans for new ventures, and ensures the development and implementation of finance and procurement policies which meet legislative and regulatory requirements and also reflect best practice. The Finance Committee reviews and approves the annual accounts and financial statements for the whole Heriot-Watt University Group jointly with the Audit and Risk Committee. The Committee also reviews and monitors compliance with the Financial Memorandum with the Scottish Funding Council and other relevant terms and conditions associated with funding grants and rewards. Four committees report to the Finance Committee: the Campus Committee; the Endowments Committee; the University Collections Committee; and the Fees Working Group.
- > The Governance and Nominations Committee met three times during the period reported. The Committee's composition reflects the advice set out in the Scottish Code relating to the membership of a governing body nominations committee. The Governance and Nominations Committee advises the Court on all matters relating to governance and good governance practice, the conduct and effectiveness of Court business and the appointment of independent lay members of the Court and the standing committees of the Court.

¹ Independent lay member of Court

² From 17th May 2017

³ Until 31st May 2017

⁴ Until 31 July 2017

⁵ From 1 August 2017

⁶ From 1 June 2017

⁷ Until 26 October 2017

⁸ Until 4 November 2017

⁹ From 8 November 2017

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The Remuneration Committee met twice during the period reported. The remit of the Committee is to review and determine the salary and other remuneration, including performance reward payments and conditions of service, of the most senior (Grade 10) staff of the University. The membership of the Committee comprises only independent lay members and includes one member who is entirely independent of the work or governance of the University. The University complies with the guidance set out in the Scottish Code in relation to the composition and responsibilities of the committee responsible for remuneration; and with the good governance guidance on remuneration committees published by the Committee of Scottish Chairs.

The Staff Committee met four times during the period reported. The Committee's remit is to advise the Court and make recommendations on the human resources strategy in relation to the University's strategic objectives, legislation and best practice, and to oversee workforce planning and employment policy as well as matters relating to equal opportunities, diversity, the welfare and security of staff, international staff governance and arrangements in place for staff representation.

The Global Student Liaison Committee met three times during the period reported. The Committee provides a means for the Court to consider the effectiveness of the University's global mechanisms in place to review, monitor and continually enhance the student experience, and to ensure that appropriate levels of student feedback and representation are enabled and encouraged across all campuses of the University.

The Ordinances and Regulations Committee is a joint committee of the Court and the Senate and includes members who are appointed separately by both the Court and the Senate. The Committee met four times during the period reported. The purpose of the Committee is to advise the Court and the Senate on matters related to the Ordinances and Regulations of the University and to keep under review the University's Charter, Statutes and underpinning Ordinances and Regulations.
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The full terms of reference of each Court committee can be accessed via the following webpage: <https://www.hw.ac.uk/services/secretariat/university-committees-a-z.htm>.

Membership of Committees of Court

The following persons served on the committees of court during the financial year reported in these accounts.

AUDIT AND RISK COMMITTEE

Ms Jandy Stevenson (Chair)	Ms Susan O'Brien
Ms Trish Gray	Ms Rio Watt
Ms Morag McNeill	Ms Suzanne Wilson

EMERGENCY COMMITTEE

Dame Frances Cairncross (Chair)	Mr Tony Strachan
Ms Tracey Ashworth-Davies	Professor Ian Wall
Professor Patrick Corbett	Mr Graham Watson
Professor Julian Jones	Professor Richard A. Williams
Ms Jandy Stevenson	

FINANCE COMMITTEE

Mr Graham Watson (Chair)	Mr George Morton
Dame Frances Cairncross	Ms Marta Phillips
Mr Gerard Cassels	Ms Dorothy Shepherd
Professor Patrick Corbett	Mr Tony Strachan
Professor Julian Jones	Professor Ian Wall
Mr Andrew Milligan	Professor Richard A. Williams

GLOBAL STUDENT LIAISON COMMITTEE

Ms Rio Watt (Chair)	Mr Corto Pimenta
Mr Liam Burns	Mr Tony Strachan
Dame Frances Cairncross	Mr Franklin Thankachan
Mr Nicholas Chong	Professor Richard A. Williams
Mr Diarmuid Cowan	Mr Mohd Naeqeb Zahiedin
Ms Lucy Graham	

GOVERNANCE AND NOMINATIONS COMMITTEE

Dame Frances Cairncross (Chair)	Ms Jandy Stevenson
Ms Tracey Ashworth-Davies	Mr Tony Strachan
Mr Diarmuid Cowan	Mr Graham Watson
Professor Julian Jones	Ms Rio Watt
Professor Isabelle Perez	Professor Richard A. Williams

REMUNERATION COMMITTEE

Mr Tony Strachan (Chair)	Ms Evelyn Stevenson
Ms Tracey Ashworth-Davies	Mr Graham Watson
Dame Frances Cairncross	

STAFF COMMITTEE

Ms Tracey Ashworth-Davies (Chair)	Professor Julian Jones
Dame Frances Cairncross	Ms Jane Queenan
Ms Lucy Conan	Ms Lorrie Secrest-Osman
Dr James Evans ¹	Mr Tony Strachan
Dr Amos Haniff	Professor Richard A. Williams
Mr Grant Innes	

CAMPUS COMMITTEE

Professor Ian Wall (Chair)	Mr Thomas Stenhouse
Dame Frances Cairncross	Ms Vicki Stott
Ms Pamela Calabrese	Mr Tony Strachan
Mr Diarmuid Cowan	Mr Allan Thomson
Professor Julian Jones	Mr Norrie Westbrook
Ms Morag McNeill	Professor Richard A. Williams

¹ Member from 6 May 2016 – 7 November 2016.
Dr Evans resigned from the membership of the Staff Committee on 7 November 2016

Court and committee attendance record during year to 31 July 2017

Name	Dates to/from	Court	Audit & Risk Committee	Campus Committee	Finance Committee	Global Student Liaison Committee	Governance & Nominations Committee	Remuneration Committee	Staff Committee
		7 meetings	7 meetings	6 meetings	7 meetings	3 meetings	3 meetings	2 meetings	4 meetings
Dame Frances Cairncross		7/7		2/6	7/7	3/3	3/3	2/2	3/4
Ms Tracey Ashworth-Davies		4/7					2/3	2/2	4/4
Ms Aashna Bakshi	Member from 1 June 2017	1/1*							
Ms Pamela Calabrese	Member until 31 May 2017	3/6*		3/5*					
Ms Lucy Conan		6/7							2/4
Professor Patrick Corbett		7/7			6/7				
Mr Diarmuid Cowan		7/7		6/6		3/3	3/3		
Ms Trish Gray		6/7	7/7						
Dr Amos Haniff		7/7							3/4
Mr Grant Innes		7/7							4/4
Professor Julian Jones		7/7		6/6	4/7		3/3		4/4
Ms Eloise McNeaney	Member until 31 May 2017	5/6*							
Ms Morag McNeill		6/7	5/5*	4/6					
Mr Andrew Milligan		5/7			4/7				
Professor Isabelle Perez		6/7					3/3		
Professor John Perkins		7/7							
Ms Jane Queenan		6/7							3/4
Professor James Ritchie	Member from 17 May 2017	1/2*							
Ms Dorothy Shepherd		7/7			4/7				
Mr Tom Stenhouse		5/7		5/6					
Ms Jandy Stevenson		6/7	7/7				3/3		
Mr Tony Strachan		7/7		5/6	7/7	3/3	2/3	2/2	2/4
Professor Ian Wall		7/7		6/6	6/7				
Mr Graham Watson		6/7			7/7		3/3	1/2	
Ms Rio Watt		6/7	7/7			3/3	2/3		
Professor Richard A. Williams		6/7		1/6	6/7	1/3	2/3	1/2	1/4
Mr Liam Burns		~				1/3			
Mr Gerard Cassels		~			6/7				
Dr James Evans	Member until 7 November 2016	~							0/1*
Mr George Morton		~			4/7				
Ms Susan O'Brien	Member until 25 August 2016	~	1/1*						
Ms Marta Phillips		~			7/7				
Ms Lorrie Secrest-Osman		~							4/4
Ms Evelyn Stevenson		~						2/2	
Ms Vicki Stott		~		2/6					
Mr Allan Thomson		~		6/6					
Mr Norrie Westbrook		~		4/6					
Ms Suzanne Wilson		~	7/7						

* Indicates total number of meetings held during period of membership

Independence

The Court is satisfied as to the independence of the appointed lay membership of the Court. Appointments are made following open advertising and against clear criteria, taking into account the requirements of independence and diversity.

Reporting of Interests

The Group has taken the necessary steps to ensure compliance with Financial Reporting Standard 102's provisions on Related Party transactions. Any interests which, under this accounting standard, would require to be disclosed by members of the Court would be so disclosed, with appropriate recording in the Court minutes.

The University's Ethical Business: Conflict of Interest Policy applies to all members of the Court and its committees. The accompanying register of Court members' interests is updated annually and published on the University's website.

RISK MANAGEMENT

The University acknowledges the risks inherent in its activities, and is committed to managing those risks both to create value in times of uncertainty and to address those that pose a significant threat to the achievement of its academic and business objectives, its financial health or its reputation. The systems for risk management and internal controls exist to manage and control the risk of failure to achieve academic and business objectives and can only provide reasonable but not absolute assurance against material misstatement or loss. There is a continuous process for identifying, evaluating and managing the significant risks faced by the University and these risks are reviewed regularly by the Risk & Project Management Strategy Group, the University Executive, the Audit and Risk Committee and the Court.

The Court, advised by the Audit and Risk Committee, has overall responsibility for reviewing the effectiveness of the systems of internal control and risk management. The University has developed and adopted a formal and structured risk management policy and system to ensure that key risks are identified, prioritised and managed consistently across the University. The policy and system are reviewed and updated on a regular basis. Reports documenting the policy, system and procedures and issues arising are reported to the Audit and Risk Committee on a regular basis.

The Risk and Control Framework

The University Executive (UE) and the Risk & Project Management Strategy Group, which reports to the UE, lead the University's risk management process. Ownership of each identified strategic risk lies with a named member of the senior management group. At the operational level, the Heads of Schools and Heads of Directorates identify and manage risk and review risk in their areas of responsibility on a regular basis.

The UE and the Risk & Project Management Strategy Group receive and review the University's strategic risk register at quarterly intervals. The Audit and Risk Committee reviews, quarterly, the effectiveness of the University's risk management framework and the content and appropriateness of its strategic risk register. In addition, the Court reviews the risk and control framework annually.

The key elements of the University's risk management strategy are:

- > a documented and communicated process of identifying and evaluating risks, assessing risk appetite, identifying and implementing suitable responses to risks, providing ongoing assurance about the effectiveness of the framework and processes to embed and review risk awareness. The risk management strategy is reviewed on a three yearly cycle by the Risk & Project Management Strategy Group, the University Executive and the Audit and Risk Committee;
- > multi-level review and reporting processes throughout the risk cycle, involving staff, Heads of Schools, Directors and managers, the University Executive, Internal Audit, the Audit and Risk Committee and the Court; and
- > identification and regular review of both the continuing appropriateness of the risks and responses identified and of the ongoing status of the identified or planned responses to risks.

The key ways in which risk management is embedded across the University are:

- > the link between strategic and operational planning and the risk management processes;
- > including risk in routine, regular operational reporting processes;
- > the ownership, management and oversight of risks by the Risk & Project Management Strategy Group, University Executive, Heads of Schools, Directors and managers;
- > involving the Audit and Risk Committee and the Court in agreeing and reviewing strategic and operational risks;
- > using risk registers for each of the University's Schools, Services and Projects; and
- > the monthly, quarterly and annual reviews of strategic and operational risk profiles.

The key controls that are built into routine processes are:

- > ensuring appropriately skilled and experienced staff are responsible for business processes;
- > documented procedures exist for all key business processes;
- > management and independent checking ensure quality of processing; and
- > management information is available to assess the volume, timeliness and quality of processing.

More generally, the University is committed to a process of continuous development and improvement. In February 2017, the Risk and Project Management Services were combined to form the new Assurance Services, which provides greater enhancement of the management of risk across the entire portfolio. Assurance Services have completed a thorough review of the HWU Group's insurance provision to secure cover that reflects the recent growth of the Edinburgh estate and provides fit for purpose cover for all our campuses, in light of the different international legislative requirements. This review has delivered value for money with greater cover and reduced premiums for both Dubai and Malaysia.

INTERNAL CONTROL

The Purpose of the System of Internal Control

The system of internal control is designed to manage risk to a reasonable level rather than to eliminate all risk of failure to achieve policies, aims and objectives. It can therefore only provide reasonable and not absolute assurance of effectiveness. The system of internal control is based on an ongoing process designed to identify and prioritise the risks, including information risks, to achieving strategic and operational aims and objectives; to evaluate the likelihood of those risks being realised and the impact should they be realised; and to manage them efficiently, effectively and economically. The wider system of internal control is based on an ongoing process designed to identify the principal risks to achieving the University's policies, aims and objectives; to evaluate the nature and extent of those risks; and to manage them efficiently, effectively and economically. The system of internal control has been in place in the University for the year ended 31 July 2017, and up to the date of approval of the annual report and accounts.

Review of effectiveness of the internal control system

The University's internal audit service throughout the reporting period was provided by PricewaterhouseCoopers LLP.

The Internal Auditor reports directly to the Secretary of the University on the system of internal control. Internal Audit ultimately exists to support the University in achieving its objectives and is one of the key sources of assurance on which the Audit and Risk Committee and the Secretary of the University rely.

In order to discharge its responsibilities effectively, Internal Audit develops an audit strategy and plan which outlines their program of work. The audit plan takes into consideration the entire governance framework and the other assurance mechanisms and processes which include the risk management processes developed and maintained by University management.

It is the responsibility of the University Executive to:

- > ensure a thorough and regular evaluation of the nature and the extent of the risks to which the University is exposed and the establishment and embedding of effective risk management processes and systems of control; and
- > receive, comment on and act on the University Internal Audit forward plan; audit reports on reviews undertaken; reports on the University's progress in actioning internal audit recommendations; and the Internal Auditor's Annual Report.

Internal Audit provides regular reports to the Audit and Risk Committee on:

- > the status of audits/reviews outlined in the approved Internal Audit Plan;
- > key findings/themes and trends emerging from work undertaken;
- > management implementation of agreed recommendations and actions; and
- > significant changes to the Internal Audit Plan based on new/ emerging risks.

These include the Internal Auditor's independent opinion on the adequacy and effectiveness of the University's system of internal control and recommendations for improvement. The Audit and Risk Committee regularly receives progress reports on the implementation of Internal and External Audit recommendations.

The University's Internal Auditor issues an annual Assurance Statement which provides the University with an opinion on the adequacy and effectiveness of the internal control system and the extent to which it can be relied on.

For the year to the end of 31 July 2017, it reported that it was satisfied that sufficient internal audit work has been undertaken to allow them to draw a conclusion as to the adequacy and effectiveness of Heriot-Watt University's governance, risk management and control. In the Internal Auditor's opinion governance, risk management and control was generally satisfactory with some improvements required. Their annual internal audit report notes that there were no critical-graded findings and only two high-rated findings: relating to IT disaster recovery and the lack of a University-wide IT business impact analysis and that management have agreed appropriate actions to address the individual findings and mitigate the risks identified.

The External Auditor also reports to the Director of Finance, the University Executive and the Audit and Risk Committee on any internal control issues that they identify during their normal audit activities.

The Audit and Risk Committee's review of the effectiveness of the system of internal control is informed by:

- > the comprehensive management information received by the University Executive on all of University's operational activities;
- > the controls that exist over planned expenditure and the regular reporting of actual expenditure and regular review of budgets and forecasts;
- > the managers within the University who are responsible for developing and maintaining the internal control framework. In a new development, the Secretary of the University now provides the Committee with an annual presentation on risk management and systems of internal control;
- > the work of the internal auditor, who submits to the Audit and Risk Committee regular reports which include the independent and objective opinion on the adequacy and effectiveness of University's systems of internal control, together with recommendations for improvement; and
- > comments made by the external auditor in its management letter and other reports.

RESPONSIBILITIES OF THE UNIVERSITY COURT IN RELATION TO THE ACCOUNTS

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 governing instruments, the Statement of Recommended Practice (SORP): Accounting for Further and Higher Education, Accounts Directions from Scottish Funding Council (SFC) and other relevant accounting standards. In addition, within the terms and conditions of a Financial Memorandum agreed between the SFC 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.

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

- a. they are prepared on a going concern basis in that the Court is satisfied that the Group has adequate resources to continue in operation for the foreseeable future;
- b. suitable accounting policies are selected and applied consistently;
- c. judgements and estimates are made that are reasonable and prudent; and
- d. applicable accounting standards are followed, subject to any material departures being disclosed and explained in the Accounts.

The Court has taken reasonable steps to:

- a. 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;
- b. 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;
- c. safeguard the assets of the Group and prevent and detect fraud;
- d. secure the economical, efficient and effective management of the Group's resources and expenditure;
- e. ensure that the Group's Executive 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; and
- f. maintain a safe and secure environment for the staff and students.

Professor Richard A. Williams
Principal and Vice-Chancellor
15 December 2017

The Court believes that the delivery of its mission by its charitable activities provides continuing public benefit and it aims to comply with the Office of the Scottish Charity Regulator's regulatory requirements, including the requirement to maintain independent control by its trustees.

THE SCOTTISH CODE OF GOOD HIGHER EDUCATION GOVERNANCE

During the reporting year the University operated in compliance with the 2013 Scottish Code of Good Higher Education Governance. Over the course of the coming year it will be working to achieve compliance with some new provisions included in the 2017 update of the Code.

GOING CONCERN

The University's activities and the factors likely to affect its future development, performance and position are set out in the Strategic Report on pages 6-19. Its financial performance for the year to 31 July 2017 is described in the Financial Review on pages 34-40; and the income and expenditure, assets, liquidity and cash flows are set out in more detail in the Financial statements on pages 42-45 and in the Notes to the Financial Statements on pages 51-69. With current forecasts and projections that show it to be well placed to manage its activities successfully having taken account of risk and uncertainty, the University Court considers that the University has adequate resources to continue in operation for the foreseeable future and for this reason, it continues to adopt the going concern basis of accounting in preparing the annual financial statements.

Dame Frances Cairncross
Chair of Court
15 December 2017



Corporate issues



OUTCOME AGREEMENT

Outcome agreements, which are negotiated individually between the Scottish Funding Council and institutions, are framed to ensure delivery of improved outcomes in specific areas, including notably widening access to increase the number of students from deprived areas of Scotland entering the University; new pathways for increased numbers of students to progress from Scottish further education colleges to the University; increasing skills training in various topics; increasing various aspects of equality and diversity in the University; increasing Scottish universities' global research competitiveness; increasing university/industry collaboration in Scotland; and increasing Scottish universities' contributions to environmental sustainability.

The University continues to welcome this opportunity to demonstrate alignment of its activities with Government priorities and, through the negotiation of Outcome Agreements over a number of years now, has secured additional resources from SFC to advance the targeted outcomes. The Agreement negotiated between the University and Funding Council in 2016/17 marks the beginning of a new three-year Outcome Agreement cycle and sets out a new medium-term framework that continues this positive approach to advancing the well-aligned objectives of the University and the Scottish Government in education, research and innovation.

COLLEAGUE COMMUNICATION

Colleagues continue to be kept up-to-date during the year with strategy development, implementation and financial and academic performance through a variety of communication channels. These include regular electronic and online communications

including the e-newsletter; the Professional Services Leadership Board Bulletin; messages to staff and students; and the Principal's Outlook – a series of articles from our Principal. Local communication between managers and their teams is also supported through guidance and resources to support managers in their role to be prepared and to support their teams through change.

Due to the confluence of a number of challenges, including the impact of Brexit and greater financial pressures, our communications to colleagues have been focused on reducing uncertainty and delivering timely, open and honest communications. We have provided open sessions and specialist immigration advice and support for all our non-UK colleagues working at our UK campuses. We have also kept colleagues up-to-date during the year with regular updates on the financial situation of the University, the required savings against future plans and the implementation of a voluntary redundancy scheme.

Our channels included forums for open discussions where the Principal and Senior Managers were available to answer questions about the voluntary redundancy scheme or the financial landscape of the University more generally; a dedicated email and frequently asked questions section on the staff intranet. Colleagues have been continuously encouraged to send their questions and share their views on the implementation of the plans.

EQUALITY AND DIVERSITY

Heriot-Watt University is committed to equality and diversity in an environment that promotes a culture of "Inclusion for All". This holistic approach helps us maintain an open and accessible working, living and learning environment where all are supported to reach their full potential.

Consistent with meeting our legal requirements, in April 2017 the University published a range of material that outlines how we respond to the equality and diversity agenda. Those publications, which are summarised below, can all be found at www.hw.ac.uk/equality:

- > **Inclusion for All: Mainstreaming Equality. Equality Outcomes 2017-21:** This updates progress on our 2013-17 Equality Outcomes and outlines our plans covering 2017-21, including our Equality Outcomes action plan.
- > **Heriot-Watt University Equal Pay Statement:** This builds on the last four years; our Equal Pay Statement includes pay gap data by gender, ethnicity and race and includes our Equal Pay action plan covering 2017-21.
- > **Heriot-Watt University Employee Information:** We publish employee information under separate cover, with data covering recruitment, promotion, pay and remuneration, training and development, return after maternity leave, return to work of disabled employees following sick leave relating to their disability, appraisal, grievances (including about harassment), disciplinary action (including for harassment) and dismissals and other reasons for leaving.
- > **Heriot-Watt University Student Information:** We annually publish data online to show our student intake by protected characteristic.

Our Equality Outcomes cover two overarching areas:

- > **Fundamentals for Success:** addressing those activities we will be progressing over the period 2017-2021, covering underpinning areas such as data collection and reporting.
- > **Equality and Diversity Interventions:** sets out a range of project related work, usually spanning two-year timeframes, for review and refresh in 2019.

The University is particularly committed to progressing through the Athena SWAN Charter Awards. We recently renewed our University-wide Bronze Award and three of our academic schools (the School of Energy, Geoscience, Infrastructure and Society; the School of Mathematical and Computer Sciences; and the School of Engineering and Physical Sciences) currently hold Bronze awards. The School of Energy, Geoscience, Infrastructure and Society initiated their renewal activity in April 2017 with a view to submission in April 2018. The School of Engineering and Physical Sciences and the School of Mathematical and Computer Sciences initiated their renewal activity in November 2017 and submit in November 2018. Edinburgh Business School, the School of Social Sciences and the School of Textiles and Design are all currently being supported in developing their plans for progressing toward Athena SWAN Bronze submissions. Further information relating to our Athena SWAN activities can be found at www.hw.ac.uk/athenaswan.

Equality and diversity activity is also embedded in our Outcome Agreement with SFC, supplemented by our Gender Equality Action Plan, which pulls together actions relating to addressing gender balance in the student population across subject areas.

EMPLOYMENT OF DISABLED PERSONS

The University is an accredited Disability Confident Employer, as such we have been able to demonstrate progression against a set of standards in support of taking positive action to attract, recruit and retain people with disabilities. We are committed to:

- > ensuring that people with disabilities receive full and proper consideration throughout the whole recruitment process;
- > guaranteed interviews for those who meet the minimum essential criteria; and
- > providing practical equipment or modification to enable disabled people to undertake full employment.

In the event of existing employees becoming disabled every effort is made to ensure that their employment with the Group continues and that appropriate support is made available in partnership with the employee and their manager. It is the policy of the Group that the recruitment, training, career development and promotion of people with disabilities should, as far as possible, equal that of other employees.

PENSIONS

The Group's employees are members of one of five pension schemes: the Universities Superannuation Scheme (USS), the Lothian Pension Fund (LPF) the Scottish Teachers Superannuation Scheme (STSS), Heriot-Watt Services Limited defined contribution pension scheme and the National Employment Savings Trust (NEST).

Both USS and LPF published their latest triennial valuation reports, for which the reference date is 31 March 2014, in December 2015 and February 2015 respectively. Both schemes are currently engaged in a valuation as at 31 March 2017, with publication expected later this year or early next year. Valuation of STSS was completed by the Government Actuary's Department on behalf of the Scottish Government on 27 February 2015, based on scheme data as at 31 March 2012. The next valuation will be as at 31 March 2016 and this will set contribution rates from 1 April 2019. These schemes provide benefits to members based on final pensionable pay. The other pension schemes are both defined contribution schemes.

Details of the accounting policies are set out on page 42 and further disclosures are set out in note 26.

For USS, the institution has entered into an agreement (the Recovery Plan) that determines how each employer within the scheme will fund the overall deficit, and so recognises, as a provision in its balance sheets, a liability for the net present value of the future contributions payable that arise from the agreement. During the year that provision fell by £1.6m to £18.3m (note 18).

For the Lothian Pension Fund the net value of the deficit between the underlying assets and liabilities of the University's share of the fund is identifiable as a provision in the University's balance sheet. During the year that provision fell by £3.7m to £26.8m (note 18).

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. 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.

ENVIRONMENTAL SUSTAINABILITY

The University is committed to operating its facilities in a responsible way with concern for the environment and for the communities in which it operates. In order to achieve this objective the University considers environmental issues within investment and business decisions and plans sustainability improvement initiatives across key areas including:

Utilities and Climate Change

- > Reduce energy consumption and related greenhouse gas emissions by promoting effective and efficient reduction methods, throughout the whole estate.
- > Reduce water consumption by promoting conservation methods throughout the whole estate, aspiring towards best practice through effective monitoring and targeting systems.

Resource Efficiency

- > Minimise waste and ensure that there is effective control, which promotes reuse and recycling where possible and provides responsible disposal elsewhere.
- > Avoid the use of non-replaceable resources wherever possible.

Sustainable Procurement

- > Influence our suppliers and contractors to ensure that goods and services procured support our environmental policy and, in turn, that all suppliers and contractors progressively improve their own environmental performance.

Campus, Landscape and Community

- > Continue to recognise the value of biodiversity and the importance of protecting and enhancing the diverse range of species and habitats present on campus.
- > Involve and inform staff, students, visitors and other stakeholders to develop their awareness of environmental issues.
- > Liaise with local communities and their representatives where the University operates on environmental matters.

Travel

- > Develop and implement green transport plans for business and commuter travel.
- > Promote modal shift from single occupancy private car use by encouraging and facilitating car sharing, better use of public transport and the provision of facilities for pedestrians and cyclists.

The University also promotes enhanced environmental sustainability via a significant proportion of its teaching and research. To establish the best framework in which to continue to improve sustainability performance, the University will work towards the development of Environmental and Energy Management Systems consistent with the ISO 14001 and ISO 50001 standards, including the completion of an initial gap analysis during 2017.

During 2016/17 the University's environmental sustainability initiatives have included:

- > Completion of numerous energy efficiency projects under the University's Salix energy efficiency recycling fund, including replacement of fluorescent lighting with LED across several buildings and works to reduce gas consumption across much of the estate.
- > Development of a draft Travel Strategy and the completion of a comprehensive staff and student travel survey for the Edinburgh Campus. During 2017/18 a Travel Plan will be finalised for the Campus, informed by outputs from the Travel Strategy and travel survey exercises and including comprehensive measures to enhance the uptake of active and sustainable travel.
- > Investigation of low carbon heat opportunities for buildings at the Edinburgh Campus, to support the attainment of carbon reduction objectives described in the University's Carbon Management Plan. Decarbonising heat is a fundamental national challenge, and presents opportunities for significant reductions in emissions. Low carbon heat technologies include heat pumps, biomass and geothermal heat: the University is developing studies in relation to candidate technologies to permit commercial and technical evaluation and the development of detailed proposals in 2017/18.

PAYMENT OF SUPPLIERS

Unless special terms are agreed, it is Group policy to pay valid invoices at the end of the month following the month in which the invoice is dated. At 31 July 2017 there were 16 days (2016: 13 days) of purchases in trade creditors. No interest was payable under the terms of the Late Payment of Commercial Debts (Interest) Act 1998.

MINORITY INVESTMENTS

For a number of years the Group has had 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 31 July 2017 there were 12 investments (2016: 12) in a range of different companies. The market value of these investments is not reflected in the Group's financial statements.



Financial Review

FINANCIAL STRATEGY

The Strategic Plan's enabling strategy set targets to develop income growth of over 50%, from £150m to £235m, over five years; and to achieve annual operating surpluses of at least 7% of income within the five year period of the Strategic Plan. The planned growth in total income is underpinned by growth in student numbers and in income from Research Grants and Contracts. Income growth will be supported by strong recruitment trends for fee paying students in Edinburgh, Dubai, and particularly Malaysia.

Consistent with that plan, the University has seen rapid and sustained growth. Significant contributions to the teaching income have come from the development of post-graduate and trans-national activities, while research income increases have been stimulated by academic recruitment under the 'Global Platform' initiative. In more recent times, however, the rate of growth in both tuition fee and research income has slowed, and a range of risks to the pace of growth has become clearer. Our recent financial plans, therefore, have been developed with contingency comparable to the scale of envisaged risk, based on a combination of resilience in individual budgets (an ability to reduce expenditure if expected income failed to materialise), an ability to slow medium-term investments if required (e.g., in staffing) and an explicit centrally-held contingency. Nevertheless, as the 2016/17 year began, the risks crystallised with a scale and pace at the upper limit of what had been envisaged. While the contingency level had been judged appropriately, given the scale of the challenges faced, the desired level of contingency could not realistically be maintained over the duration of our forward financial plans. It was apparent that delivering long-term financial sustainability would only be practical with significant reductions in cost in future years, including pay expenditure, relative to the previous plans. Accordingly, during the year, an enhanced voluntary severance programme was initiated. In the short term, while we make the adjustment to staff numbers, and incur the costs associated with a redundancy scheme, operating surpluses will be compromised, but our future plans indicate that beyond 2018/19 we should return to surpluses of around 5%; consistent, alongside our new long-term financing arrangements, with our provisional future assessment of financial sustainability.

Historically the University has been relatively conservative in its borrowing, however, its continued ambition to grow requires a degree of risk, and further investment, particularly to create a physical environment that is capable of accommodating the growth in student numbers that we have planned for; of providing the quality of research environment that is consistent with our ambitions for research growth and intensification; and meeting the expectations and needs of students and staff going forward. To that end, in December 2016, the University benefited from the establishment of a long-term debt funding arrangement by way of a private placement with three UK and US institutional investors which enabled restructuring of the then current debt portfolio and consequent significant reduction in applicable rates of interest and simplification of covenants. The net proceeds of the £112m investment have been used to repay all existing borrowings and to contribute £63.5m towards the funding of future University wide development.

Investment in the University's estate and infrastructure is well underway. Before this year we had already completed the development of a new Malaysian Campus; the opening of Oriam, Scotland's National Performance Centre for Sport; the opening of the Sir Charles Lyell Centre, a new centre for earth and marine science and technology; the delivery of the "Learning Commons" space, providing a variety and choice of supported learning and study settings; the start of a series of improvements and refurbishment of a range of learning and teaching spaces across the Edinburgh campus; the first significant inroads into the development of laboratory facilities to support our research growth and to accommodate global platform appointments, notably in the School of Engineering and Physical Sciences; new student residential accommodation in Edinburgh and Galashiels; and the start of a rolling programme of refurbishment of existing student residences. The University has also continued to invest in its core information systems, the main elements this year being continuation of the project to revitalise a broad suite of student administration and support systems.

Going forward, our capital plans will continue, through a rolling programme of refurbishment, to focus on the investment required in order

to provide capacity for new research activities and to provide for increased quality and quantity of teaching and learning space to meet the needs of growing student numbers and of higher student expectations. The most significant investments will be seen in the conversion of the James Watt conferencing facilities to provide additional and enhanced teaching capacity along with additional capacity for supported learning and study and the construction of a Discovery and Innovation Centre, a pioneering innovation building, integrating twenty-first century learning and teaching spaces, research laboratories and workspaces, innovation and enterprise space, all developed around the latest models for "open space collaboration" and utilising the latest digital technology to accelerate innovation and foster the co-creation of ideas. Our capital plans also include improvements to the Edinburgh Business School building; the refurbishment of the historic Panmure House, the last home of Adam Smith; and Edinburgh Business School's investment in the preparation of new learning materials.

While there are inevitable risks associated with the execution of such a significant scale of capital investment, we will continue to ensure that appropriate project management, resource and financial planning will be directed to ensure that projects can be delivered within an overall pre-agreed programme. More critical is likely to be the delivery against a financial plan that relies on strong income growth and generation of surplus, which, in turn, are subject to risks associated with the success in international activity and on broader risks around government funding, student fees and research concentration. However, our revised financial plans still contain significant contingency and discretionary elements to provide resilience and flexibility, including explicit contingency against failure to achieve planned tuition fee and net research income; discretionary elements in potential capital investments; and gateway reviews to maintain future flexibility over decisions to commit capital expenditure across the planning period in the event that investment priorities, financial circumstances or risk profiles change. We have traditionally employed interest rate hedging to achieve certainty over debt servicing costs and looking ahead, will gain the same certainty from our available refinancing funds, making use of fixed interest bonds.

SCOPE OF THE FINANCIAL STATEMENTS

The financial statements which have been approved by the Court for the year-ended 31 July 2017 comprise the consolidated results of the University and its subsidiary undertakings, together the “Group”. These accounts have been prepared in accordance with the Statement of Recommended Practice (SORP): Accounting for Further and Higher Education 2015; and in accordance with Financial Reporting Standards (FRS 102).

FINANCIAL PERFORMANCE

Results for the year

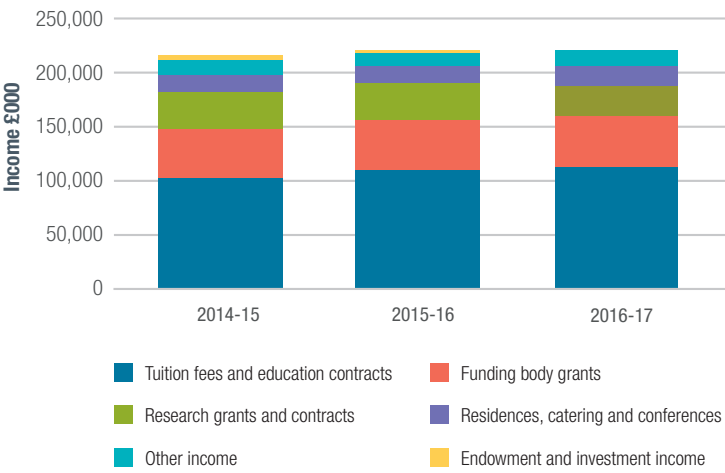
The group reported a loss, before other gains and losses of £6.9m. After other gains on investment the reported loss for the year was £4.1m. A tax charge of £1.1m (much of which is anticipated to be recovered in the following year) took the loss for the year to £5.2m, which, after recognition of the actuarial gain on pension schemes, took the total comprehensive income for the year to £1.7m.

Although 2016/17 saw risks to the University's income crystallise at a scale and pace at the upper limit of what had been envisaged; particularly in relation to its recruitment of overseas students, challenges around public funding of research and the impact of the economic climate and oil price on the ability of industry to sponsor research programmes; the mitigation offered by the contingency and discretion that we had included in our financial plans had been judged appropriately. However, it was clear that such a level of contingency could not be maintained in the long-term and in any case would be stretched as the impact of those risks compounded year-on-year. It was clear that planning for a financially sustainable future depended on significant reductions in expenditure in future years, notably pay, relative to our existing plans. Accordingly, a voluntary redundancy programme was initiated. The reported results for the year, therefore, were impacted by £5.9m of cost associated with achieving the staff restructuring (note 7). Additionally, changes to accounting practice in Malaysia during this year saw a £1.7m increase in the reported lease costs and the opening of ORIAM precipitated a £3.2m impairment of an existing building in the group's accounts.

The inclusion of certain unrealised gains and losses and differences in income recognition, because of recent changes in accounting practice, makes comparison of operating surpluses against our 7% target and against prior-years difficult. However, it is clear that the result of staff restructuring costs was to return a loss for the year of £4.1m rather than the surplus of £1.8m (0.8% of total income) it would have been otherwise.

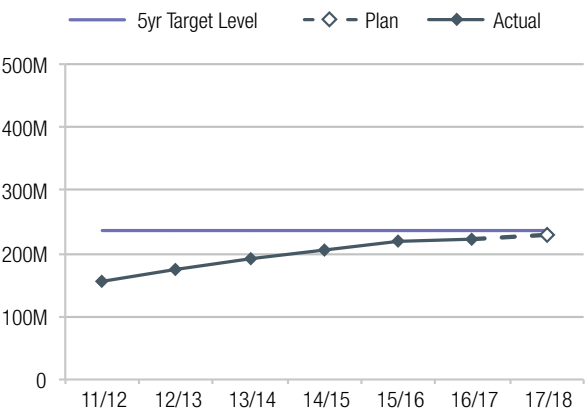
Income

In 2016/17 the Group achieved total income growth of 0.7% with total income increasing by £1.6m to £221.1m (2016: £219.1m). That growth was driven primarily by continued growth in tuition fee income, funding body grants, and other income. Growth was offset to some extent by a reduction in research grant and contract income and in income from endowments and donations.



The University's strategic plan set the aim of growing income by more than 50% over the five year strategic planning period, so establishing a target total income of £235m by 2017/18, which, depending on competitor growth rates, would move the University well into the sector's second quartile. At £221m, actual performance in 2016/17 indicates that we are likely to come close to that target. At £220m in 2015/16 (the most recently available sectoral figures), Heriot-Watt moved into 51st place in the UK rank order, continuing a trend of increasing its position in that rank order over a number of years. When normalised to total staff numbers (to give a measure of the efficiency of income generation), the University's £123k per staff FTE ranks 7th in the UK (2015 £101k; 18th).

KPI: Total income



Continued growth in student numbers and associated tuition fees, saw that category of income grow by £2.3m over the year to £112.9m (2016: £110.6m).

On Scottish campuses, the fee income growth, at £0.2m was modest, with the growth from undergraduate Home/EU students and undergraduate students attending Heriot-Watt from England, Wales and Northern Ireland, being all but eradicated by the £4.2m reduction in fees received from a diminished population of international students, predominantly at post graduate level.

In Dubai, a £0.9m reduction in income reflected the fall in student numbers after a disappointing recruitment cycle; a trend that appears to have been reversed in the next academic year.

Our Malaysian campus, in its early years of operation, continues to see growth in student numbers associated with adding additional year-groups. The growth in fee income at that campus in the year was £3.3m

Following the downturn in the fortunes of Edinburgh Business School reported last year, associated with currency fluctuation, conflicts, keen competition and the closure of its programmes at West London College; the reduction in income slowed to £0.2m in the current year. Plans to halt and reverse that trend should begin to bear fruit in early course, with strong applications for its innovative new full time MBA which starts, in the coming year, with students based on the Edinburgh campus, with one term studying in Dubai; but will continue to develop by harnessing the global reach of Heriot-Watt University.

Student numbers associated with Independent Distance Learning and Approved Learning Partners have diminished. This reduction arises both from changes to UK immigration policy which have forced the University to withdraw from its partnership with West London College; and from a shift away from high volume-low revenue partnerships to more rewarding activity with accredited partners.

The recent trend of generally increasing funding body grants continued this year, with Scottish Funding Council grants reaching £47.4m (2016: £45.5m); boosted by continued support for additional funded places to widen access and for strategically important subjects in undergraduate and postgraduate programmes and by the continued staged increase in the Research Excellence Grant as a result of the University's success

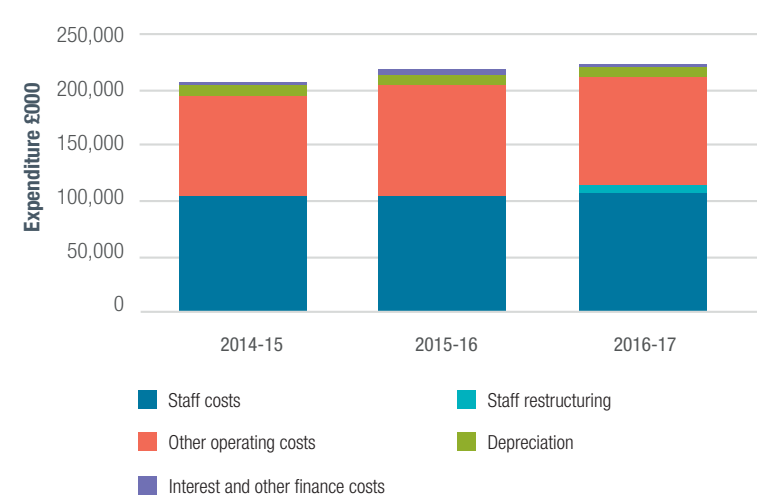
Student numbers

	2015/16	Change	2016/17
Scottish Campuses			
Undergraduates	6,695	3.2%	6,910
Taught Postgraduates	1,512	-5.6%	1,427
Research Postgraduates	1,093	-0.5%	1,087
	9,300	1.3%	9,424
Dubai Campus			
Undergraduates/foundation	2,492	-12.2%	2,187
Taught Postgraduates	1,366	-2.2%	1,336
Research Postgraduates	7	100.0%	14
	3,865	-8.5%	3,537
Malaysia Campus			
Undergraduates/foundation	966	34.0%	1,294
Taught Postgraduates	233	-10.3%	209
	1,199	25.4%	1,503
TOTAL ON-CAMPUS	14,364	0.7%	14,464
Independent Distance Learners and Students at Approved Learning Partners			
Undergraduates	1,653	-23.8%	1,259
Taught Postgraduates	13,977	-8.4%	12,800
Research Postgraduates	298	1.3%	302
	15,928	-9.8%	14,361
GRAND TOTAL	30,292	-4.8%	28,825

in the Research Excellence Framework 2014, which will see its Research Excellence Grant grow from £9.9m in 2014/15 to £12.1m by 2017/18. At 21.4% (2016: 20.7%), of total income, Heriot-Watt's proportion of income derived from the Scottish Funding Council is likely to remain among the lowest in Scotland, reflecting the diversity of our income streams.

This year saw an apparent fall in research grant and contract income to £27.0m (2016: £33.2m). That fall can be attributed to last year's inclusion of a single grant which, consistent with the change in accounting policy arising out of the implementation of FRS 102, saw the immediate recognition of £4.3m for that grant which lacked performance conditions; and the inclusion of £4.1m arising from the Research and Development Expenditure Credit, a tax relief which is no longer available to universities.

The University's other income grew, in the period, to £31.9m (2015: £27.8m). This underlying growth in operating income includes that from residence and catering income of £1.8m, primarily associated with the opening of the new student residences in Edinburgh. One-off contributions to growth in other income are £1.8m arising from a tenant's disposal of its long-term rental obligation and a £1.8m gain arising from the redemption of the interest rate swap associated with previous loan arrangements. Set against that growth in income are reductions associated with some EC funded programmes coming to their natural end and with the planned winding down of certain consultancy operations.



Expenditure

At £108.0m (2016: £105.1m), total staff costs, excluding any restructuring costs, rose by 2.7%. The underlying salary costs of £86.7m (2016: £83.4m) represented a rise of 4.1% on the previous year. The main contributors to that growth were investment in new active research academics, growth at our overseas campuses and automatic increments in pay scales; however, that growth was constrained, to some extent, by the continued sectoral restraint on wages. Social security costs for the year increased by 18% over the year. This was reflective of the first full-year effect of the loss of relief on Employers' National Insurance Contributions for staff contracted out of the additional state pension scheme and the introduction, in April, of the apprenticeship levy.

During the year, the University instituted a cost saving plan to bring about permanent reductions in the cost base, including a voluntary redundancy scheme. Edinburgh Business School also instituted a staff restructuring scheme during the year. By the end of the year, a number of staff had left the Group by way of voluntary redundancy, with that cost (£1.8m) being included in this year's income statement; and a number of staff having committed to leaving in the coming year, that cost (£4.1m) being accrued in this year's income statement.

The University's contributions to various pension schemes grew to £13.7m (2016: £12.5m), the 9.7% growth reflecting the propensity of new and existing staff to join those schemes and the introduction of the opportunity for members of the newly opened defined contribution section of the USS to take advantage of additional employer contributions to match additional personal contributions. The reduction in the USS deficit reduction provision reflected a change in the actuarial assumptions, notably in the discount rate, used to calculate that provision.

At £99.0m (2016: £99.5m), the reduction in other operating expenditure, reflects in-year efforts to make cost savings.

At £2.5m (2016: £5.9m) interest and other finance costs are lower than in the previous year. That overall movement conceals the detail of a growth in loan interest during the year and the transition from a loss to gain in relation to the derivatives that historically protected the University from interest rate volatility on its bank loans. That loan interest growth to £2.8m (2016: £1.7m) is attributable to the expansion of the University's borrowing facilities, to £112m, replacing and supplementing £45m of pre-existing bank loans and to meet the cost of redeeming the interest rate swaps in relation to those loans. The growth in that interest was mitigated by the reduction in interest rates that came from the refinancing. Additionally, the £1.8m gain that crystallised upon disposal of the interest rate swap derivative was in contrast to the £2.8m unrealised loss that arose from the revaluation of that derivative at last year's balance sheet date.

FINANCIAL POSITION

Net assets

At the end of the year, the Group had net assets of £55.9m (2016: £54.5m), an increase of £1.4m on the previous year.

The £8.5m net increase in fixed assets to £201.3m reflects the continued capital investment in the estate on our Edinburgh campus, including the term-time repurposing of the James Watt conference centre for learning and teaching purposes along with a range of other improvements to the learning and teaching environment, a residue of expenditure on Oriam and the new Edinburgh student residences and the ongoing commitment to rolling refurbishment of existing student residences. As well as the normal depreciation charges, that growth was offset by an impairment of an existing building upon the opening of the new Oriam facility.

£2.4m growth in investment assets to £33.5m, reflects unrealised gains arising from the revaluation of investment property (£1m); from the year-end valuation of the investment assets underpinning our endowment funds (£0.8m); and from invested funds (£0.8m).

A net reduction of £1.0m in trade and other receivables largely reflects movements arising from an exercise to identify and match unapplied receipts.

The £13.2m fall in creditors falling due within one year arises from a £5.2m reduction in unsecured bank loans, those having been repaid and replaced with long-dated liabilities as part of our refinancing arrangements; and the movement of a deferred capital grant associated with the construction of Oriam, transferred to long-term creditors on completion of the construction of the asset.

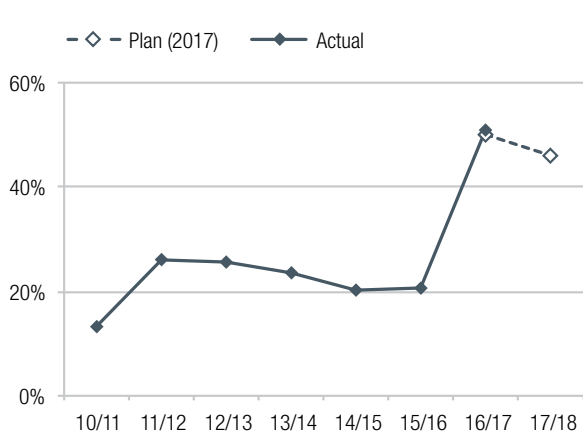
In addition to the reclassification of that deferred capital grant referred to above, the £92.7m increase in creditors falling due after more than one year, to £189.2m, is otherwise almost entirely associated with the refinancing that took place during the year. The University started the year with term loans from the Clydesdale Bank and Barclays both fully drawn, along with £3m drawn on a revolving credit facility from Barclays. In December 2016, in recognition of the strategic need for major capital investment to accommodate the student numbers and quantity and quality of research that underpin

the University's strategic plan, the University established long-term debt funding through a private placement with three UK and US institutional investors. The net proceeds of the £112m investment, have been used to repay all of the existing borrowings, and to redeem the liability associated with the interest rate swaps that protected the University from the revenue impact of financial market volatility on the floating interest rates of the pre-existing loan arrangements. The resultant net proceeds of £63.5m are to be used to contribute to the funding of the campus development already described in this document, including creation of a new flexible academic building that as well as enhancing teaching and research capacity will create facilities for discovery, innovation and incubation; redevelopment and modernisation of existing facilities to create high quality teaching laboratories and highly serviced research facilities; and continual improvements to the existing residential estate.

Measuring long-term borrowings as a percentage of income gives an indication of the level of borrowings relative to the size of the institution and gives both an indication of both the institution's exploitation of its potential to support development and the risks associated with servicing repayments and interest on such debt. Having raised £112m by way of a private placement, Heriot-Watt's borrowings now represent 50.7% (2016: 20.4%) of the University's total income. Borrowing at that level is likely to place Heriot-Watt in the top quartile of most highly geared UK institutions. The University has committed to this further borrowing solely to raise capital that will supplement internally generated surpluses and endowment funds for the development of its estate. It has done this to generate capacity in its teaching and learning environment that will accommodate its planned growth in on-campus student numbers; and to create the facilities required to continue to grow and intensify its research, and only to do so where there is a demonstrable return on capital investment. The University currently has no plans to borrow beyond this private placement.

The £6m reduction in pension provisions to £41.1m (2016 £47.1m) reflects the £1.6m reduction in our year-end assessment of the University's long term obligation to fund its share of the USS recovery plan; and the actuarially assessed £4.4m reduction in the year-end net liability in relation to the Lothian Pension Fund.

KPI: Gearing



Reserves

The Group's reserves grew by £2.2m to £56.7m (2016:£4.5m) during the year.

Disaggregating that movement:

- > Endowment reserves grew by £0.7m to £10.7m (2016 £10.0m) during the year (note 19). That growth being attributable to £365,000 income from endowment investments, an £831,000 increase in the market value of endowment investments set against £487,000 of expenditure from the endowment funds.
- > Restricted reserves fell by £3.9m to £10.5m (2016 £14.4m) during the year (note 20). That fall was attributable to receipt of £2.3m of new non-government research grants without performance conditions, £0.7m of new philanthropic donations and £0.1m increase in the market value of invested donations; offset by expenditure of £5.8m relating to non-government research grants received without performance conditions for which the income was recognised as restricted in the current or previous years and £1.2m spent from donations that had been recognised in the current or previous years.
- > Unrestricted reserves grew by £5.5m to £32.5m (2016 £27.0m) during the year. That growth being attributable an unrestricted loss of £6.6m being offset by a £6.9m actuarial gain arising from the year-end Lothian Pension Fund valuation and the release of £5.2m of income, previously restricted, to match the expenditure arising from non-government research grants received without performance conditions and to match donations, both of which had been recognised in the current or previous years.

CASH FLOW

At 1 July 2017 cash and cash equivalents sat at £81.6m, representing 37% (2016: 7%) of total income; or net liquidity of 142 days (2016: 30 days).

Chief among the contributors to the increase of £66.0m in cash and cash equivalents was the receipt of £112m fixed-interest long-dated private placement funding net of the £40.0m utilised to repay existing borrowing and the £6.2m cost of redeeming the interest-rate swap. The proceeds of the private placement are currently held as liquid assets to ensure their ready availability and to minimise the risk of depreciation of the capital sum. While the short term nature of the investment of these funds boosts the University's apparent liquidity, looking forward, even as that funding is consumed in construction of assets, the lower reliance on internally generated funds to meet capital expenditure will increase the availability of cash to meet working capital requirements and so improve actual liquidity.

That new borrowing carries a lower interest rate, however, the expansion of the borrowing to fund our capital programme meant that the £2.8m interest payments were a step up from the £1.7m spent in the previous year. This year's £18.4m continuation of investment in tangible assets on our Edinburgh campus, utilised both cash generated from operating activities and from the private placement funding.

On top of the loss for the year of £1.4m, charges for depreciation, improvement in debtor and creditor positions and a range of unrealised gains and losses conceal net cash inflow from operating activities of £18.2m; essential to fuel both the University's internally-generated continued contribution to its capital programme and to fund the servicing of the private placement borrowing.

Independent auditor’s report to the University Court of Heriot-Watt University

REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS

Opinion

We have audited the financial statements of Heriot-Watt University (“the University”) for the year ended 31 July 2017 which comprise the Consolidated and University Statements of Comprehensive Income and Expenditure, the Consolidated and University Statements of Changes in Reserves, the Consolidated and University Balance Sheets, the Consolidated Statement of Cash Flows and related notes.

In our opinion the financial statements:

- > give a true and fair view of the state of the Group's and the University's affairs as at 31 July 2017, and of the Group's and the University's income and expenditure, gains and losses and changes in reserves, and of the Group's cash flows, for the year then ended;
- > have been properly prepared in accordance with UK accounting standards, including FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*, and with the 2015 *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).

Basis for opinion

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.

We conducted our audit in accordance with International Standards on Auditing (UK) (“ISAs (UK)”) and applicable law. Our responsibilities are described below. We have fulfilled our ethical responsibilities under, and are independent of the group in accordance with, UK ethical requirements including the FRC Ethical Standard. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion.

Going concern

We are required to report to you if we have concluded that the use of the going concern basis of accounting is inappropriate or there is an undisclosed material uncertainty that may cast significant doubt over the use of that basis for a period of at least twelve months from the date of approval of the financial statements. We have nothing to report in these respects.

Other information

The University Court of Heriot-Watt University is responsible for the other information, which comprises the Strategic Report, Corporate Governance Statement, Corporate Issues and Financial Review. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work, we have not identified material misstatements in the other information.

Matters on which we are required to report by exception

Under the Charities Accounts (Scotland) Regulations 2006 (as amended) we are required to report to you if, in our opinion:

- > the University has not kept proper accounting records; or
- > the financial statements are not in agreement with the accounting records; or
- > we have not received all the information and explanations we require for our audit.

We have nothing to report in these respects.

University Court of Heriot-Watt University responsibilities

As explained more fully in their statement set out on page 28, the University Court of Heriot-Watt University is responsible for: the preparation of the financial statements and for being satisfied that they give a true and fair view; such internal control as it determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the group and parent University's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless it either intends to liquidate the group or the parent University or to cease operations, or has no realistic alternative but to do so.

Auditor’s responsibilities

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue our opinion in an auditor’s report. Reasonable assurance is a high level of assurance, but does not guarantee that an audit conducted in accordance with ISAs (UK)

will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

A fuller description of our responsibilities is provided on the FRC’s website at www.frc.org.uk/auditorsresponsibilities.

Report on other legal and regulatory requirements

We are required under the terms of our engagement to report on the following matters.

In our opinion, in all material respects:

- > funds from whatever source administered by the Group or the University 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;
- > funds provided by the Scottish Funding Council have been applied in accordance with the Financial Memorandum with Higher Education Institutions.

The purpose of our audit work and to whom we owe our responsibilities

This report is made solely to the University Court of Heriot-Watt University, in accordance with the Charters and Statutes of the institution, and, in the University Court’s role as charity trustees, in accordance with section 44(1)(c) of the Charity 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 them 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 and the University Court of Heriot-Watt University for our audit work, for this report, or for the opinions we have formed.

Andrew Shaw

For and on behalf of KPMG LLP, Statutory Auditor

Chartered Accountants
Saltire Court, 20 Castle Terrace,
Edinburgh, EH1 2EG

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

December 2017

Consolidated Statement of Comprehensive Income and Expenditure for the year ended 31 July 2017

		Consolidated		University	
		2017	2016	2017	2016
	Note	£000	£000	£000	£000
Income					
Tuition fees and education contracts	1	112,909	110,606	93,408	94,121
Funding body grants	2	47,428	45,453	47,427	45,450
Research grants and contracts	3	27,107	33,209	27,064	33,188
Other income	4	31,909	27,849	26,375	24,581
Investment income	5	968	777	948	805
Endowments and donations	6	897	1,626	807	1,493
		221,218	219,520	196,029	199,638
Expenditure					
Staff costs	7	107,972	105,107	96,819	95,788
Staff restructuring	7	5,909	-	5,647	-
Other operating expenses	9	98,962	99,486	79,912	89,618
Depreciation and impairment		12,741	8,630	7,697	7,663
Interest and other finance costs	8	2,526	5,956	2,594	6,025
		228,110	219,179	192,669	199,094
(Loss)/Surplus before other gains and losses		(6,892)	341	3,360	544
Loss on disposal of fixed assets		-	(37)	-	(37)
Gain/(loss) on investment property		1,030	(280)	1,030	(280)
Gain on investments		1,761	258	959	258
Loss/(surplus) before tax		(4,101)	282	5,349	485
Taxation	10	(1,127)	(1,187)	(572)	(909)
Loss for the year		(5,228)	(905)	4,777	(424)
Actuarial gain/(loss) in respect of pension schemes	26	6,911	(935)	6,724	(1,595)
Total comprehensive income/(expenditure) for the year		1,683	(1,840)	11,501	(2,019)
Represented by:					
Endowment comprehensive income for the year		709	279	574	263
Restricted comprehensive income for the year		(3,948)	1,286	(3,759)	1,272
Unrestricted comprehensive income for the year		4,922	(3,405)	14,686	(3,554)
		1,683	(1,840)	11,501	(2,019)

All items of income and expenditure relate to continuing activities.

The accounting policies on pages 46-50 and the notes on pages 51-68 form an integral part of these financial statements.

Statement of Changes in Reserves for the year ended 31 July 2017

	Income and Expenditure reserve			Revaluation Reserve	Total
	Endowment £000	Restricted £000	Unrestricted £000	£000	£000
Consolidated					
Balance at 1 August 2015	9,732	13,164	30,118	3,058	56,072
Surplus from income and expenditure statement	1,638	5,354	(7,897)	-	(905)
Other comprehensive income	-	-	(935)	-	(935)
Transfers between restricted and unrestricted reserve	-	(5,427)	5,427	-	-
Transfers between endowment and restricted reserve	(1,359)	1,359	-	-	-
Balance at 1 August 2016	10,011	14,450	26,713	3,058	54,232
Surplus/(deficit) from income and expenditure statement	1,197	795	(7,220)	-	(5,228)
Other comprehensive income	-	-	6,911	-	6,911
Transfers between restricted and unrestricted reserve	-	(5,231)	5,231	-	-
Transfers between endowment and restricted reserve	(488)	488	-	-	-
Total comprehensive income for the year	709	(3,948)	4,922	-	1,683
Balance at 31 July 2017	10,720	10,502	31,635	3,058	55,915
University					
Balance at 1 August 2015	8,054	12,989	19,163	2,875	43,081
Surplus/(deficit) from income and expenditure statement	1,622	5,340	(7,386)	-	(424)
Other comprehensive income	-	-	(1,595)	-	(1,595)
Transfers between restricted and unrestricted reserve	-	(5,427)	5,427	-	-
Transfers between endowment and restricted reserve	(1,359)	1,359	-	-	-
Balance at 1 August 2016	8,317	14,261	15,609	2,875	41,062
Surplus/(deficit) from income and expenditure statement	980	731	3,066	-	4,777
Other comprehensive income	-	-	6,724	-	6,724
Transfers between restricted and unrestricted reserve	-	(4,896)	4,896	-	-
Transfers between endowment and restricted reserve	(406)	406	-	-	-
Total comprehensive income for the year	574	(3,759)	14,686	-	11,501
Balance at 31 July 2017	8,891	10,502	30,295	2,875	52,563

The accounting policies on pages 46-50 and the notes on pages 51-68 form an integral part of these financial statements

Consolidated and University Balance Sheet for the year ended 31 July 2017

	Note	Consolidated		University	
		2017 £000	2016 £000	2017 £000	2016 £000
Non-current assets					
Fixed Assets	11	201,344	192,898	158,889	150,225
Investments	12	33,531	31,112	31,291	29,877
		234,875	224,010	190,180	180,102
Current Assets					
Stock	13	6	6	-	-
Trade and other receivables	14	51,989	52,997	66,689	62,884
Investments	15	962	1,660	600	650
Cash and cash equivalents		81,648	15,609	73,050	12,164
		134,605	70,272	140,339	75,698
Less Creditors: amounts falling due within one year	16	83,208	96,378	76,143	69,564
Net current assets/(liabilities)		51,397	(26,106)	64,196	6,134
Total assets less current liabilities		286,272	197,904	254,376	186,236
Creditors: amounts falling due after more than one year	17	189,220	96,497	161,672	99,201
Provisions					
Pension provisions	18	41,137	47,175	40,141	45,973
Total net assets		55,915	54,232	52,563	41,062
Restricted reserves					
Income and expenditure – endowment reserve	19	10,720	10,011	8,891	8,317
Income and expenditure – restricted reserve	20	10,502	14,450	10,502	14,261
Unrestricted reserves					
Income and expenditure - unrestricted		31,636	26,713	30,295	15,609
Revaluation reserve		3,058	3,058	2,875	2,875
Total reserves		55,915	54,232	52,563	41,062

The accounting policies on pages 46-50 and the notes on pages 51-68 form an integral part of these financial statement, which were approved by the University Court on 15 December 2017 and signed on its behalf by:

Professor Richard A. Williams
Principal and Vice-Chancellor

15 December 2017

Dame Frances Cairncross
Chair of Court

15 December 2017

Andrew Menzies
Director of Finance

15 December 2017

Consolidated Statement of Cash Flows for the year ended 31 July 2017

	Consolidated & University	
	2017 £000	2016 £000
Cash flow from operating activities		
Loss for the year	(5,228)	(905)
Adjustment for non-cash items		
Depreciation and impairment of tangible fixed assets	12,741	8,630
Increase in fixed asset investments	(2,419)	(414)
Decrease in short term investments	698	10,344
Decrease/(increase) in debtors	1,008	(123)
Increase in creditors	11,875	8,087
(Decrease)/increase in provisions	(6,038)	2,648
(Gain)/loss on investments	(1,761)	2,276
(Gain)/loss on derivatives	(1,766)	2,792
(Gain)/loss on investment land revaluation	(1,030)	280
Actuarial gain/(loss) in respect of pension schemes	6,911	(535)
Adjustment for investing or financing activities		
Interest receivable	(563)	(353)
Net return on pension assets	1,012	1,375
Interest payable	2,845	1,739
Loss on disposal of tangible fixed assets	-	37
Net cash inflow from operating activities	18,285	35,878
Cash flows from investing activities		
Payments to acquire fixed assets	(16,282)	(48,805)
Interest receivable	563	353
Net return on pension assets	(1,012)	(1,375)
	(16,731)	(49,827)
Cash flows from financing activities		
Interest payable	(2,845)	(1,739)
Net amounts drawn down	112,200	3,557
Repayments of amounts borrowed	(44,870)	(2,304)
	64,485	(486)
Increase/(Decrease) in cash and cash equivalents in the year	66,039	(14,435)
Cash and cash equivalents at beginning of the year	15,609	30,044
Cash and cash equivalents at end of the year	81,648	15,609

The accounting policies on pages 46-50 and the notes on pages 51-68 form an integral part of these financial statements

Statement of accounting policies

1. Basis of preparation

These financial statements have been prepared on a going concern basis under the historical cost convention as modified by the revaluation of fixed assets and financial instruments; in accordance with the Statement of Recommended Practice (SORP): Accounting for Further and Higher Education 2015; and in accordance with Financial Reporting Standards (FRS 102). The University is a public benefit entity and therefore has applied the relevant public benefit requirement of FRS 102. The financial statements also conform to guidance published by the Scottish Funding Council. The financial statements are prepared in sterling and rounded to the nearest thousand pounds.

2. Basis of consolidation

The consolidated financial statements include the University and all of its subsidiaries for the financial year to 31 July 2017. The results of subsidiaries acquired or disposed of during the period are included in the consolidated statement of income and expenditure from the date of acquisition or up to the date of disposal. Intra-group transactions are eliminated on consolidation.

The consolidated financial statements do not include the income and expenditure of the Students' Union as the University does not exert control or dominant influence over policy decisions.

3. Income recognition

a. Tuition fees and education contracts

Fee income is stated gross of any expenditure and credited to the Consolidated Statement of Income and Comprehensive Expenditure over the period in which students are studying. Bursaries and scholarships are accounted for gross as expenditure and not deducted from income.

b. Funding body grants

Recurrent grants from Funding Bodies are credited to income in the period in which they are receivable.

Government revenue grants including funding council teaching, research and other grants are recognised in income over the periods in which the University recognises the related costs for which the grant is intended to compensate. Where part of a government grant is deferred it is recognised as deferred income within creditors and allocated between creditors due within one year and due after more than one year as appropriate.

Capital grants from Funding Bodies are recognised in income over the expected useful life of the asset.

c. Research grants and contracts

Research revenue income from government sources are recognised in income over the periods in which the University recognises the related costs for which the grant is intended to compensate. Where part of such a grant is deferred it is recognised as deferred income within creditors and allocated between creditors due within one year and due after more than one year as appropriate. Research capital grants from government sources are recognised in income over the expected useful life of the asset.

Research revenue income from other sources are recognised when they are receivable and when performance conditions have been met. Income received in advance of performance conditions being met is included in creditors as deferred income. Where there are no performance conditions, income is recognised when it is receivable. Research capital grants from other sources are recognised in income when the University is entitled to the funds subject to any performance related conditions being met.

Research development and expenditure credits are included in research grant and contracts income.

d. Other income

Income from the sale of goods and services is credited to income when the goods or services are supplied to the external customers against the orders received or the terms of the contract have been satisfied.

e. Investment income

Investment income is credited to income on a receivable basis.

f. Donations and endowments

Non exchange transactions without performance related conditions are donations and endowments.

Donations with no restrictions are recognised in the financial statements when the donation has been received.

Where a donor has specified that a donation must be used for a particular objective it is classified as a restricted donation and is recognised in income when the University is entitled to the funds. Income is retained within the restricted reserve until such time that it is utilised in line with the restrictions, at which time it is released to general reserves.

Where donations are to be retained to the benefit of the University beyond the current year for purposes specified by the donors, other than the purchase or construction of tangible fixed assets, they are considered to be endowments. They are recognised as income when the University is entitled to the funds. Income is retained in the endowment reserve until such time that it is utilised in line with the terms of the endowment, at which time it is released to general reserves.

Where the University has the power to use the capital portion of an endowment it is categorised as an expendable endowment; where the donor has specified that the fund is to be permanently invested to generate an income stream to be applied to a particular objective it is categorised as a permanent endowment.

Investment income and appreciation of endowments is recorded in income in the year in which it arises and as either restricted or unrestricted income according to the terms other restriction applied to the individual endowment fund.

g. Amounts received as agent

Funds the University receives and disburses as paying agent on behalf of a funding body are excluded from the income

and expenditure of the University where the University is exposed to minimal risk or enjoys minimal economic benefit related to the transaction.

4. Accounting for 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).

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).

The Group has implemented arrangements to meet the UK statutory requirement for employers to automatically enrol certain workers who are not already pension scheme members into a qualifying pension scheme. In addition to the existing pension schemes, both the University and Edinburgh Business School allow staff to opt to join the National Employment Savings Trust (NEST).

Staff on Heriot-Watt Services Ltd contracts of employment are entitled to contribute to a defined contribution scheme.

None of the Group's other subsidiary undertakings operates any other pension schemes.

The accounting policies relating to each of the schemes are:

a. USS

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. The University is therefore exposed to actuarial risks associated with other institutions' employees and is unable to identify its share of the underlying assets and liabilities in full in USS on a consistent and reasonable basis and therefore, as required by FRS 102, the University accounts for the scheme as if it were a defined contribution scheme. As a result the amount charged to the Statement of Comprehensive Income and Expenditure is equal to the total of contributions payable by the employer in the year.

Since the institution has entered into an agreement (the Recovery Plan that determines how each employer within the scheme will fund the overall deficit), the institution has established a provision for the contributions payable that arise from the agreement to the extent that they relate to the deficit and the resulting expense in the statement of comprehensive income. The costs of the USS deficit recovery plan have been estimated based on a model devised by the USS and the British Universities Finance Directors Group. The model uses the additional costs included in the deficit recovery plan and discounts based on corporate bond levels having a maturity similar to the length of the recovery plan (15 years as at 31 July 2017). The scheme actuary reviews the funding of the USS every

year and undertakes a formal actuarial valuation every three years, at which time the deficit recovery plan may be amended.

b. 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. The institution has established a provision to recognise the net value of those assets and liabilities.

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.

c. STSS

Heriot-Watt University participates in the Scottish Teachers' Superannuation Scheme, an unfunded multi-employer defined benefit statutory public service pension scheme with benefits underwritten by the UK Government. Because of the nature of the scheme, the University is unable to identify its share of the underlying assets and liabilities on a consistent and reasonable basis and therefore, as required by FRS 102, the University accounts for the scheme as if it were a defined contribution scheme. As a result the amount charged to the Statement of Comprehensive Income and Expenditure is equal to the total of contributions payable by the employer in the year.

d. National Employment Savings Trust (NEST)

The scheme is a defined contribution scheme into which both the employer and the employee make a contribution. The cost charged to the statement of comprehensive Income and Expenditure is equal to the total of contributions payable by the employer in the year.

e. Heriot-Watt Services Limited defined contribution pension scheme

Employees of Heriot-Watt Services can join that company's defined contribution pension scheme, into which both the employer and the employee make a contribution. Being a defined contribution scheme, the cost charged to the statement of comprehensive Income and Expenditure is equal to the total of contributions payable by the employer in the year.

5. Employment benefits

Short term employment benefits such as salaries and compensated absences are recognised as an expense in the year in which the employees render service to the University. Any unused benefits, such as holiday entitlements earned but not taken at the balance sheet date, are accrued and measured as the additional amount the University expects to pay as a result of the unused entitlement.

6. Finance leases

Leases in which the University assumes substantially all the risks and rewards of ownership of the leased asset are classified as finance leases. Leased assets acquired by way of finance lease and the corresponding lease liabilities are initially recognised at an amount equal to the lower of their fair value and the present value of the minimum lease payments at inception of the lease.

Minimum lease payments are apportioned between the finance charge and the reduction of the outstanding liability. The finance charge is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

7. Operating leases

Costs in respect of operating leases are charged on a straight-line basis over the lease term. Any lease premiums or incentives are spread over the minimum lease term.

8. Foreign currency

Transactions in foreign currencies are translated to the respective functional currencies of Group entities at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to the functional currency at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are retranslated to the functional currency at foreign exchange rates ruling at the dates the fair value was determined.

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on consolidation, are translated to the Group's presentational currency, Sterling, at foreign exchange rates ruling at the balance sheet date. The revenues and expenses of foreign operations are translated at an average rate for the year where this rate approximates to the foreign exchange rates ruling at the dates of the transactions. Exchange differences arising from this translation of foreign operations are reported as an item of other comprehensive income.

9. Fixed assets

Fixed assets are stated at cost less accumulated depreciation and accumulated impairment losses. Certain items of fixed assets that had been revalued to fair value on or prior to the date of transition to FRS 102, are measured on the basis of deemed cost, being the revalued amount at the date of that revaluation.

No depreciation is charged on assets in the course of construction.

Where parts of a fixed asset have different useful lives, they are accounted for as separate items of fixed assets.

a. Land

On adoption of FRS 102 the Group adopted the transitional provisions to measure land at fair value on the date of transition, and to use that fair value as its deemed cost. Land held at 31 July 2014 is shown in the balance sheet at

the valuation on that date; land acquired after 31 July 2014 is shown at cost.

Costs incurred in relation to land after initial purchase and prior to valuation are capitalised to the extent that they increase the expected future benefits to the University.

Land is not depreciated as it is considered to have an indefinite useful life.

b. Buildings

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

External fabric:	50 years
Internal fabric:	35 years
Mechanical & Engineering:	25 years

Costs incurred in relation to buildings after initial purchase or construction are capitalised to the extent that they increase the expected future benefits to the University.

c. Equipment

Equipment, including computers and software, costing less than £20,000 is recognised as expenditure. All other equipment is capitalised.

Capitalised equipment is stated at cost and depreciated over its expected useful life as follows:

Equipment acquired for specific research projects:	3-5 years
Administrative IT systems:	7 years
Other equipment:	5 years

Depreciation methods, useful lives and residual values are reviewed at the date of preparation of each Balance Sheet.

d. Borrowing costs

Borrowing costs are recognised as expenditure in the period in which they are incurred.

10. Heritage assets

Works of art and other valuable artefacts are capitalised and recognised at the cost or value of the acquisition, where such a cost or valuation is reasonably obtainable. The assets held by the University are held at nil value as cost and valuation are not available.

11. Investment properties

Investment property is land and buildings held for rental income or capital appreciation rather than for use in delivering services. Investment properties are measured initially at cost and subsequently at fair value with movements recognised in the income statement. Properties are not depreciated but are revalued or reviewed annually according to market conditions as at 31 July each year.

12. Investments

Non-current asset investments are held on the Balance Sheet at amortised cost less impairment.

Investments in subsidiaries are carried at cost in the University's accounts.

Current asset investments are held at fair value with movements recognised in the Surplus or Deficit for the year.

13. Stock

Stock is stated at the lower of the cost and net realisable value. Where necessary, provision is made for obsolete, slow-moving and defective stock.

14. Cash and cash equivalents

Cash includes cash in hand, cash at bank, deposits repayable on demand. Deposits are repayable on demand if they are in practice available within 24 hours without penalty.

Cash equivalents are short term, highly liquid investments that are readily convertible to known amounts of cash or repayable within 3 months with insignificant risk of change in value. They can include term deposits at banks or investments in gilts.

15. Provisions, contingent liabilities and contingent assets

Provisions are recognised in the financial statements when:

- a. the University has a present obligation (legal or constructive) as a result of a past event;
- b. it is probable that an outflow of economic benefits will be required to settle the obligation; and
- c. a reliable estimate can be made of the amount of the obligation.

A contingent liability arises from a past event that gives the University a possible obligation whose existence will only be confirmed by the occurrence or otherwise of uncertain future events not wholly within the control of the University. Contingent liabilities also arise in circumstances where a provision would otherwise be made but either it is not probable that an outflow of resources will be required or the amount of the obligation cannot be measured reliably.

A contingent asset arises where an event has taken place that gives the University a possible asset whose existence will only be confirmed by the occurrence or otherwise of uncertain future events not wholly within the control of the University.

Contingent assets and liabilities are not recognised in the Balance Sheet but are disclosed, where they arise, in the notes to the accounts.

16. Taxation

The University is an exempt Charity within the meaning of the Charities and Trustee Investment (Scotland) Act 2005 and, as such, is a charity within the meaning of Section 506 (1) of the Income and Corporation Taxes Act 1988. The University is recognised as a charity by HM Revenue & Customs and is recorded on the index of charities maintained by the Office of Scottish Charity Regulator. It is therefore a charity within the meaning of Para 1 of schedule 6 to the Finance Act 2010 and accordingly, the University is potentially exempt from taxation in respect of income or capital gains received within categories covered by section 478-488 of the Corporation Tax Act 2010 (CTA 2010) 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.

Neither the University nor its subsidiaries receive any exemption in respect of Value Added Tax. Irrecoverable VAT on inputs is included in the costs of such inputs. Any irrecoverable VAT allocated to fixed assets is included in their cost.

The University's subsidiaries are not exempt from taxation. The subsidiaries, other than Edinburgh Business School and Heriot-Watt Malaysia Sdn Bhd, pay to the University, under the Gift

Aid scheme, amounts as agreed by the directors of each subsidiary company. The charge for taxation is based on the taxable profit or loss for the year after the cost of any Gift Aid payment payable to the University.

17. Derivatives and financial instruments

Historically, the Group has purchased interest rate swaps to manage interest rate risk volatility. Following the refinancing of the existing loans in December 2016, the interest rate swaps were redeemed.

At 31 July 2016, the Interest rate swaps were held on the Balance Sheet at fair value, with the deficit movement in fair value to that date having been recorded as other expenditure in the Statement of Comprehensive Income and Expenditure.

On redemption of the interest rate swaps in December 2016, the gain arising from the difference between the book value and the cost of the redemption was recorded as other income in the Statement of Comprehensive Income and Expenditure.

18. Reserves

Reserves are classified as restricted or unrestricted. Restricted endowment reserves include balances which, through endowment to the University, are held as a permanently restricted fund which the University must hold in perpetuity.

Other restricted reserves include balances where the donor has designated a specific purpose and therefore the University is restricted in the use of these funds.

19. Key sources of estimation uncertainty and critical judgements in applying accounting policies

The preparation of the financial statements requires management to make judgements, estimates and assumptions that affect the amounts reported for assets and liabilities as at the balance sheet date and the amounts reported for revenues and expenses during the year. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates. The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future period.

a. Key sources of estimation uncertainty:

- **Fixed Assets**
Fixed assets, other than investment properties, are depreciated over their useful lives taking into account residual value, where appropriate. The actual lives of assets and any residual value are assessed annually and may vary depending on a number of factors. In reassessing asset lives, factors such as technological innovation and maintenance programmes are taken into account.
- **Investment property**
Investment properties are revalued according to market conditions as at 31 July each year. That valuation is informed by an externally sourced, professional property valuation.
- **Impairment of debtors**
The University makes an estimate for the recoverable value of trade and other debtors. When assessing impairment of trade and other debtors, management considers factors including the

ageing profile of debtors and historical experience of collection success.

- **Defined benefit pension**

The group has obligations to pay pension benefits to certain employees and to reflect the net funding position of the Lothian Pension Fund and of certain unfunded legacy pension arrangements. The cost of these benefits and the present value of the obligation depend on a number of factors, including; life expectancy, salary increases, asset valuations and the discount rate on corporate bonds are determined using actuarial valuations. The actuarial valuation involves making assumptions about discount rates, future salary increases, mortality rates and future pension increases. Due to the complexity of the evaluation, the underlying assumptions and the long term nature of these plans, such estimates are subject to significant uncertainty.

- **Provision for the USS Deficit Recovery plan**

The Group has made a provision in the financial statements, related to the contractual obligation to fund the past USS deficit. The costs of the USS deficit recovery plan have been estimated based on a model devised by the USS and the British Universities Finance Directors Group. The model uses the additional costs included in the deficit recovery plan, adjusts according to management judgement of estimated changes in staffing levels and pay increases, and is discounted based on corporate bond levels having a maturity of a similar length to the recovery plan. The scheme actuary reviews the funding of the USS every year and undertakes a formal actuarial valuation every three years, at which time the deficit recovery plan may be amended.

- **Critical accounting judgements in applying the accounting policies**

There are no such judgements in either the current or prior year.

Notes to the accounts

1. Tuition fees and education contracts

	Consolidated		University	
	2017 £000	2016 £000	2017 £000	2016 £000
Home and EU Students	18,622	17,415	18,468	17,415
Rest of UK Students	13,506	12,176	13,506	12,176
International Students	67,072	66,744	58,238	60,966
Higher education contracts	7,847	7,770	-	-
Research training support grants	1,479	1,582	1,479	1,582
Short course fees	448	1,093	363	990
Examination and graduation fees	3,935	3,826	1,354	992
	112,909	110,606	93,408	94,121

2. Funding body grants

	Consolidated		University	
	2017 £000	2016 £000	2017 £000	2016 £000
SFC teaching grants	26,907	26,745	26,907	26,745
SFC research & knowledge exchange grants	16,438	15,268	16,439	15,268
Release of deferred capital grants	2,109	2,605	2,107	2,603
Other grants	1,974	835	1,974	834
	47,428	45,453	47,427	45,450

3. Research grants and contracts

	Consolidated		University	
	2017 £000	2016 £000	2017 £000	2016 £000
Research councils	13,937	13,229	13,937	13,229
Charities	1,567	1,174	1,567	1,174
UK Government	1,952	1,844	1,952	1,844
UK Industry	2,490	1,664	2,490	1,664
EU Commission	3,829	3,860	3,829	3,862
EU other	622	480	622	480
Other overseas	1,827	5,771	1,827	5,771
Other sources	883	5,187	840	5,164
	27,107	33,209	27,064	33,188

4. Other income

	Consolidated		University	
	2017 £000	2016 £000	2017 £000	2016 £000
Residences, catering and conferences	17,711	15,916	16,952	15,024
Income from governments and other funding bodies	1,513	1,542	1,020	1,318
Release of deferred capital grants	1,508	881	806	833
Other commercial income	4,573	5,279	982	1,059
Other income, including foreign currency gains	6,604	4,231	6,615	6,347
	31,909	27,849	26,375	24,581

5. Investment income

	Consolidated		University	
	2017 £000	2016 £000	2017 £000	2016 £000
Investment income on endowments	366	387	284	307
Investment income on restricted reserves	40	37	40	37
Other investment income	562	353	624	461
	968	777	948	805

6. Endowments and donations

	Consolidated		University	
	2017 £000	2016 £000	2017 £000	2016 £000
New endowments	-	218	-	218
Donations with restrictions	660	905	599	772
Unrestricted donations	237	503	208	503
	897	1,626	807	1,493

7. Staff costs

	Consolidated		University	
	2017 £000	2016 £000	2017 £000	2016 £000
Salaries	86,740	83,359	77,204	75,768
Social security costs	7,588	6,415	7,097	5,995
Staff restructuring costs	5,909	-	5,647	-
Other severance costs	55	45	55	45
Employer's pension contributions (note 26):				
USS	9,928	8,937	9,368	8,230
LPF	3,214	3,143	3,143	3,064
Other	584	438	42	42
Movement in pension provisions (note 18):				
(Decrease)/Increase in USS provision	(1,970)	1,629	(1,873)	1,545
(Decrease)/Increase in LPF pension deficit	1,861	1,166	1,811	1,128
(Decrease) in other pension provisions	(28)	(25)	(28)	(29)
Total staff costs	113,881	105,107	102,466	95,788
Analysed between staff working in:				
Academic schools	81,064	77,694	72,672	70,513
Administrative & central service functions	23,910	19,062	21,033	17,006
Premises functions	3,799	4,674	3,739	4,612
Residences & catering	5,108	3,677	5,022	3,657
Total staff costs	113,881	105,107	102,466	95,788

The average number of persons employed in those areas, expressed as full-time equivalents, was:

	Consolidated		University	
	2017 Number	2016 Number	2017 Number	2016 Number
Academic schools	1,356	1,303	1,167	1,155
Administrative & central service functions	490	470	382	385
Premises functions	166	158	160	151
Residences & catering	130	122	127	121
Total staff costs	2,142	2,053	1,836	1,812

EMOLUMENTS OF PRINCIPAL AND VICE-CHANCELLOR**Professor Richard A Williams, Principal from 1 September 2015**

Salary	265	206
Bonus	10	-
Benefits	10	9
Pension contributions to USS*	-	34
	285	249

Professor Julian Jones, for his period as Acting Principal 13 March 2015 to 31 August 2015

Salary	-	17
Bonus	-	3
Pension contributions to USS*	-	3
	-	23

Total emoluments of the Principals

Salary	265	223
Bonus	10	3
Benefits	10	9
Pension contributions to USS*	-	37
	285	272

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

KEY MANAGEMENT PERSONNEL

Aggregate key management personnel compensation, including salary, benefits and employers' pension contributions

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the University. Staff costs include compensation paid to key management personnel. Heriot-Watt University defines its key management personnel as being the Principal and Vice-Chancellor, the Vice-Principal and Deputy Vice-Chancellor and the Secretary of the University.

REMUNERATION OF HIGHER PAID STAFF, excluding pension contributions**Consolidated**

£100,001 - £110,000	16
£110,001 - £120,000	8
£120,001 - £130,000	9
£130,001 - £140,000	5
£140,001 - £150,000	1
£150,001 - £160,000	2
£160,001 - £170,000	1
£170,001 - £180,000	-
£180,001 - £190,000	1
£200,001 - £210,000	-
£280,001 - £290,000	1
	3

Key management personnel	2017 Number	2016 Number	
	Other staff	Key management personnel	Other staff
-	16	-	13
-	8	-	8
-	9	1	3
1	5	-	2
-	1	-	1
-	2	-	1
-	1	-	-
-	-	1	-
1	1	-	1
-	-	1	-
1	-	-	-
3	43	3	29

REMUNERATION OF HIGHER PAID STAFF (continued)

University

£100,001 - £110,000
£110,001 - £120,000
£120,001 - £130,000
£130,001 - £140,000
£140,001 - £150,000
£150,001 - £160,000
£170,001 - £180,000
£180,001 - £190,000
£200,001 - £210,000
£280,001 - £290,000

2017		2016	
Key management personnel	Other staff	Key management personnel	Other staff
-	16	-	13
-	8	-	8
-	8	1	3
1	3	-	1
-	1	-	1
-	2	-	-
-	-	1	-
1	1	-	1
-	-	1	-
1	-	-	-
3	39	3	27

MEMBERS OF THE UNIVERSITY COURT AND ITS COMMITTEES

Members of the University Court are the trustees for charitable law purposes. The membership of the Court and its committees is laid out on pages **Error! Bookmark not defined.** and 24 of these financial statements. No Court member, nor any co-opted member of a Court Committee, received any remuneration nor waived any payments in respect of their membership of the University Court or of its committees during the year (2016; nil).

8. Interest payable and other finance costs

	Consolidated		University	
	2017 £000	2016 £000	2017 £000	2016 £000
Loan interest	2,845	1,739	2,987	1,874
Net charge on pension assets	1,012	1,375	983	1,359
(Gain)/loss on derivatives	(1,766)	2,792	(1,766)	2,792
Investment management charges	435	50	390	-
	2,526	5,956	2,594	6,025

9. Analysis of operating expenses by activity

	Consolidated		University	
	2017 £000	2016 £000	2017 £000	2016 £000
Academic departments	17,953	20,774	10,564	10,887
Academic services	8,197	8,106	7,840	7,882
Administration and central services	36,640	36,534	29,820	38,782
Premises	19,899	18,593	15,980	16,940
Residences, catering and conferences	4,494	4,319	3,915	3,967
Research grants and contracts	11,779	11,160	11,793	11,160
	98,962	99,486	79,912	89,618
Other operating expenses include:				
External auditor's remuneration - audit	65	87	31	58
External auditor's remuneration – non-audit services	45	106	45	64
Internal auditor's remuneration	93	108	93	108
Operating lease rentals				
- Land & Buildings	2,225		1,702	
- Other	163		163	

10. Taxation

	Consolidated & University	
	2017 £000	2016 £000
UK Corporation tax at 19.67% (2016: 22.33%)	559	1,187
Provision for withholding tax	568	-
	1,127	1,187

11. Fixed assets

Consolidated	Land and Buildings	Equipment	Assets in the course of construction	Total
	£000	£000	£000	£000
Cost or valuation				
At 1 August 2016	204,894	54,786	58,936	318,616
Additions	9	666	21,075	21,750
Transfers	62,220	4,278	(66,498)	-
Foreign exchange movement	(134)	(158)	-	(292)
Disposals	-	(340)	-	(340)
At 31 July 2017	266,989	59,232	13,513	339,734

Depreciation

At 1 August 2016	80,871	44,847	-	125,718
Charge for year	6,487	3,023	-	9,510
Impairment	3,232	-	-	3,232
Foreign exchange movement	(18)	(52)	-	(70)
Disposals	-	-	-	-
At 31 July 2017	90,572	47,818	-	138,390

Net Book Value

At 31 July 2017	176,417	11,414	13,513	201,344
At 1 August 2016	124,023	9,939	58,936	192,898

University

Cost or valuation

At 1 August 2016	193,421	50,731	27,391	271,543
Additions	-	205	17,324	17,529
Transfers	30,313	4,278	(34,491)	-
Disposals	(1,881)	(340)	-	(2,221)
At 31 July 2017	221,853	54,874	10,124	286,851

Depreciation

At 1 August 2016	78,295	43,023	-	121,318
Charge for year	5,359	2,339	-	7,698
Disposals	(1,054)	-	-	(1,054)
At 31 July 2017	82,600	45,362	-	127,962

Net Book Value

At 31 July 2017	139,253	9,512	10,124	158,889
At 1 August 2016	115,126	7,708	27,391	150,225

The land and buildings of Heriot-Watt Services Ltd and the 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 £13,513,000 (2016: £58,936,000) relating to assets in the course of construction, of which £11,603,000 (2016: £57,271,000) relates to freehold land and buildings and £1,910,000 (2016: £1,665,000) relates to equipment.

At 31 July 2017 land and buildings for the group included £5,160,000 (31 July 2016, £5,160,000) in respect of freehold land which is not depreciated.

12. Non-current investments

	Long/ medium term investments	Investment in UK subsidiaries	Heriot-Watt University Malaysia Sdn Bhd	Minority investments in unquoted companies	Investment properties	Total
	£000	£000	£000	£000	£000	£000
Consolidated						
At 1 August 2016	20,657	-	-	35	10,420	31,112
Additions	-	-	-	-	-	-
Appreciation	1,594	-	-	-	1,030	2,624
Disposals	(205)	-	-	-	-	(205)
At 31 July 2017	22,046	-	-	35	11,450	33,531
University						
At 1 August 2016	8,666	7,000	3,756	35	10,420	29,877
Additions	-	-	-	-	-	-
Appreciation	792	-	(203)	-	1,030	1,619
Disposals	(205)	-	-	-	-	(205)
At 31 July 2017	9,253	7,000	3,553	35	11,450	31,291

The University investment in subsidiary companies is stated at cost.

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

13. Stock

	Consolidated		University	
	2017 £000	2016 £000	2017 £000	2016 £000
General consumables	6	6	-	-
	6	6	-	-

14. Trade and other receivables

	Consolidated		University	
	2017 £000	2016 £000	2017 £000	2016 £000
Amounts falling due within one year:				
Research grants receivables	16,358	17,671	16,359	17,671
Trade receivables	26,774	25,315	24,512	22,910
Trade debt provision	(4,248)	(3,756)	(3,501)	(3,050)
Prepayments and accrued income	10,931	11,322	10,374	10,048
Amounts due from group undertakings	-	-	7,491	5,310
	49,815	50,552	55,235	52,889
Amounts falling due after more than one year:				
Loans by parent undertakings	-	-	9,280	7,550
Prepayments and accrued income	2,174	2,445	2,174	2,445
	51,989	52,997	66,689	62,884

Included in prepayments and accrued income is £2,174,000 (2016: £2,445,000) 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 1 February 2008, the practical completion date for the redevelopment of the site.

15. Current investments

	Consolidated		University	
	2017 £000	2016 £000	2017 £000	2016 £000
Short term deposit	962	1,660	600	650
	962	1,660	600	650

16. Creditors: amounts falling due within one year

	Consolidated		University	
	2017 £000	2016 £000	2017 £000	2016 £000
Unsecured loans	142	5,304	142	5,304
Grants in advance for research	32,864	22,572	32,839	22,563
Other grants in advance	460	27,868	460	3,718
Other creditors	-	248	-	248
Trade creditors	3,964	2,890	3,870	2,482
Other taxation and social security	4,576	2,896	3,997	2,621
Accruals and deferred income	41,202	34,600	33,807	30,517
Amounts owed to subsidiary undertakings	-	-	1,028	2,111
	83,208	96,378	76,143	69,564

17. Creditors: amounts falling due after more than one year

	Consolidated		University	
	2017 £000	2016 £000	2017 £000	2016 £000
Unsecured bank loans	-	39,566	-	39,566
Other unsecured loans	112,267	557	114,764	5,557
Derivatives	-	7,971	-	7,971
Deferred income	76,824	48,274	46,779	45,978
Other creditors	129	129	129	129
	189,220	96,497	161,672	99,201
Analysis of secure and unsecured bank loans				
Due within one year or on demand	266	2,304	266	2,304
Due between one and two years	-	2,304	-	2,304
Due between two and five years	-	6,913	-	6,913
Due in five years or more	112,000	30,349	114,498	30,349
	112,267	44,870	114,764	44,870

18. Provisions for liabilities

	Pension Provisions			
	Obligation to fund USS deficit ¹ £000	Lothian pension fund deficit ² £000	Unfunded pension benefits ³ £000	Total £000
Consolidated				
At 1 August 2016	19,937	26,842	395	47,175
Utilised in year	(9,929)	(3,214)	(28)	(13,171)
Additions in 2016/17	8,303	(1,169)	-	7,133
At 31 July 2017	18,311	22,459	367	41,137
Analysis of net movement in provision				
Charged to staff costs (note 7)	(1,970)	1,861	(28)	(137)
Net charge on pension assets (note 8)	345	667	-	1,012
Actuarial gain on pension schemes	-	(6,911)	-	(6,912)
Total movement	(1,625)	(4,383)	(28)	(6,037)
University				
At 1 August 2016	19,178	26,400	395	45,973
Utilised in year	(9,472)	(3,143)	(28)	(12,643)
Additions in 2016/17	7,926	(1,115)	-	6,811
At 31 July 2017	17,632	22,142	367	40,141
Analysis of net movement in provision				
Charged to staff costs (note 7)	(1,873)	1,811	(28)	(90)
Net return on pension assets (note 8)	328	655	-	983
Actuarial gain on pension schemes	-	(6,724)	-	(6,724)
Total movement	(1,545)	(4,258)	(28)	(5,831)

¹The obligation to fund the past deficit on the Universities Superannuation Scheme (USS) arises from the contractual obligation with USS for total payments to March 2031 relating to benefits arising from past performance. The provision has been calculated by estimating future employer pension payments and applying the deficit recovery contributions outlined in the USS deficit recovery plan published in June 2015. The weighted average discount factor over the remainder of the 17 year deficit recovery plan applied is 1.91% (31 July 2016, 1.71%).

²The assets and liabilities of LPF 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. The institution has established a provision to recognise the net value of those assets and liabilities.

³This provision meets the cost of legacy pension benefits that are unfunded and paid, as and when they arise, direct to retired members by the University. The cost is charged against the provision established to meet the cost as it arises.

19. Endowment reserves

	Restricted permanent endowments £000	Unrestricted permanent £000	Expendable endowments £000	Consolidated	
				2017	2016
				Total £000	Total £000
Balances at 1 August 2016					
Capital	6,054	1,694	1,888	9,636	9,279
Accumulated Income	(2)	-	377	375	453
	6,052	1,694	2,265	10,011	9,732
New endowments	-	-	-	-	218
Investment income	210	82	73	365	387
Expenditure	(168)	(82)	(237)	(487)	(683)
	6,094	1,694	2,101	9,889	9,654
Increase in market value of investments	524	135	172	831	357
As at 31 July 2017	6,618	1,829	2,273	10,720	10,011
Represented by:					
Capital	6,054	1,829	1,888	9,771	9,636
Accumulated income	564	-	385	949	375
	6,618	1,829	2,273	10,720	10,011
Analysis by type and purpose:					
Lectureships				2,165	2,049
Scholarships and bursaries				3,962	3,766
Research support				-	-
Prize funds				1,243	1,135
General				3,350	3,061
				10,720	10,011
Analysis by assets:					
Current and non-current asset investments				9,993	9,650
Cash and cash equivalents				727	361
				10,720	10,011

20. Restricted reserves

	Unspent capital grants £000	Research grants £000	Donations £000	Consolidated	
				2017 Total £000	2016 Total £000
Balances at 1 August 2016	20	12,732	1,698	14,450	13,164
New grants	-	2,312	-	2,312	1,665
New donations	-	-	660	660	646
Investment income	-	-	40	40	37
Capital grants utilised	(20)	-	-	(20)	(500)
Expenditure	-	(5,831)	(1,204)	(7,035)	(609)
Increase in market value of investments	-	-	95	95	47
	(20)	(3,519)	(409)	(3,948)	1,286
As at 31 July 2017	-	9,213	1,289	10,502	14,450
Analysis of other restricted funds/donations by type and purpose:					
Lectureships				-	-
Scholarships and bursaries				30	23
Research support				9,213	12,732
Prize funds				1	5
General				1,258	1,690
				10,502	14,450

21. Cash and cash equivalents

	Consolidated & University	
	2017 £000	2016 £000
Balances at 1 August	15,609	30,004
Cash flows, in year	66,039	(14,435)
As at 31 July	81,648	15,609

22. Capital and other commitments

	Consolidated & University	
	2017 £000	2016 £000
Provision has not been made for the following capital commitments at 31 July 2017:		
Commitments contracted	7,412	9,058
Authorised but not contracted	34,516	5,421
	41,928	14,479

23. Lease obligations

At 31 July 2017 commitments under operating leases as follows:

	31 July 2017			2017	2016
	Land and buildings £000	Plant and machinery £000	Other leases £000	Total £000	Total £000
Consolidated					
Payable during the year	2,225	74	89	2,388	2,121
Future minimum lease payments due:					
Not later than 1 year	2,198	232	112	2,542	2,387
Later than 1 year and not later than 5 years	14,100	328	162	14,590	12,433
Later than 5 years	81,812	-	-	81,812	85,931
Total lease payments due	100,335	634	363	101,332	102,872
University					
Payable during the year	1,702	74	89	1,865	1,598
Future minimum lease payments due:					
Not later than 1 year	1,675	38	112	1,825	1,828
Later than 1 year and not later than 5 years	5,172	-	162	5,334	5,971
Later than 5 years	3,939	-	-	3,939	4,923
Total lease payments due	12,488	112	363	12,963	14,320

24. Events after the reporting period

There are no material post balance sheet events

25. Subsidiary undertakings

The subsidiary companies (all of which are registered in Scotland), wholly-owned or effectively controlled by the University are as follows:

Company	Principal activity	Number of shares	Percentage owned
Edinburgh Business School (Limited by Guarantee)	The advancement of education in any aspect of corporate or strategic management techniques, education and research through the establishment and running of a business school	-	100%
Edinburgh Conference Centre Limited	Dormant	100	100%
Heriot-Watt Services Limited	The management and operation of the National Performance Centre for Sport	100	100%
Heriot-Watt Sports Village Limited	Operation of Heriot Watt's Sports Academy (under licence from Heriot-Watt Services Limited, prior to that activity being fully absorbed into Heriot-Watt Services Limited from 1 August 2017)	5,000,000	100%
Heriot-Watt Trading Limited	The provision of consultancy, pipeline technology, language translation and interpretation services, management and business training and the manufacture of finished goods	2,000,000	100%
Scottish College of Textiles Limited	Dormant	6	100%

The group also wholly owns and effectively controls the following overseas business:

Company	Principal activity	Number of shares	Percentage owned
Heriot-Watt University Malaysia Sdn Bhd	A private Higher Education Institution, registered by the Malaysian Ministry of Higher Education	20,000,000	100%

26. Pension schemes

All 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).

The scheme currently available to staff on Heriot-Watt Services Limited contracts of employment is the Heriot- Watt Services Limited defined contribution pension scheme.

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

The amount charged to the statement of comprehensive income 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.

The total pension charge in the financial statements reflects the costs incurred by the group during the year of £14,601,000 (2016 - £16,663,000); and is analysed as follows:

	Employers’ pension contributions (note 7)	Net charge on pension assets (note 8)	Provision movement (note 18)	Consolidated	
				2017	2016
				£000	£000
Universities Superannuation Scheme	9,928	345	(1,970)	8,303	11,088
Lothian Pension Fund	3,214	667	1,861	5,742	5,162
Scottish Teachers Superannuation Scheme	43	-	-	43	42
Other pension costs	541	-	(28)	513	371
	13,726	1,012	(137)	14,601	16,663

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 31 March 2014, of the Scottish Teachers Superannuation Scheme on 31 March 2012 and of the Supplementary Pension Scheme (SPS) on 31 July 2004.

a. USS

Heriot-Watt participates in the Universities Superannuation Scheme (the scheme).The scheme was a defined benefit only pension scheme until 31 March 2016, after which it was a hybrid defined benefit/defined contribution 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. 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, currently 18% (2016: 18%). The institution 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 Section 28 of FRS 102 “Employee benefits”, accounts for the scheme as if it were a defined contribution scheme. As a result, the amount charged to the statement of comprehensive income represents the contributions payable to the scheme in respect of the accounting period. Since the institution has entered into an agreement (the Recovery Plan that determines how each employer within the scheme will fund the overall deficit), the institution recognises a liability for the contributions payable that arise from the agreement to the extent that they relate to the deficit and the resulting expense in the statement of comprehensive income.

FRS 102 makes the distinction between a Group Plan and a multi-employer scheme. A Group Plan consists of a collection of entities under common control typically with a sponsoring employer. A multi-employer scheme is a scheme for entities not under common control and represents (typically) an industry-wide scheme such as that provided by USS. The accounting for a multi-employer scheme where the employer has entered into an agreement with the scheme that determines how the employer will fund a deficit results in the recognition of a liability for the contributions payable that arise from the agreement (to the extent that they relate to the deficit) and the resulting expense is recognised in profit or loss. The University is satisfied that the scheme provided by USS meets the definition of a multi-employer scheme and has therefore recognised the discounted fair value of the contractual contributions under the funding plan in existence at the date of approving the financial statements.

The University is required to contribute a specified percentage of payroll costs to the pension scheme to fund the benefits payable to the company’s employees. From 1 April 2016 the percentage was 18%, prior to that date it was 16%.

The total cost charged to the statement of comprehensive income is £ 8,303,000 (2016: £11,088,000) as shown above. Since the institution cannot identify its share of scheme assets and liabilities, the following disclosures reflect the position from the financial statements for the scheme as a whole.

The latest available full actuarial valuation of the scheme was at 31 March 2014 (“the valuation date”), which was carried out using the projected unit method.

The 2014 valuation was the third valuation for USS under the 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 cover their technical provisions. At the valuation date, the value of the assets of the scheme was £41.6 billion and the value of the scheme’s technical provisions was £46.9 billion indicating a shortfall of £ 5.3 billion. The assets therefore were sufficient to cover 89% of the benefits which had accrued to members after allowing for expected future increases in earnings. Defined benefit liability numbers for the scheme have been produced using the following assumptions:

	2017	2016
Discount rate	2.57%	3.6%
Pensionable salary growth	N/A	N/A
Pension increases (CPI)	2.41%	2.2%

The main demographic assumption used relates to the mortality assumptions. Mortality in retirement is assumed to be in line with the Continuous Mortality Investigation’s (CMI) S1NA tables as follows:

Male members’ mortality	98% of S1NA [“light”] YoB tables – No age rating
Female members’ mortality	99% of S1NA [“light”] YoB tables – rated down 1 year

Use of these mortality tables reasonably reflects the actual USS experience. To allow for further improvements in mortality rates the CMI 2014 projections with a 1.5% pa long term rate were also adopted. The current life expectancies on retirement at age 65 are:

	2017	2016
Males currently aged 65 (years)	24.4	24.3
Females currently aged 65 (years)	26.6	26.5
Males currently aged 45 (years)	26.5	26.4
Females currently aged 45 (years)	29.0	28.8

	2017	2016
Scheme assets	£60.6bn	£49.8bn
Total scheme liabilities	£77.5bn	£58.3bn
FRS 102 total scheme deficit	£17.5bn	£8.5bn
FRS 102 total funding level	77%	85%

b. 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 comprehensive income represents the service cost expected to arise from employee service in the current year.

An actuarial valuation exercise has been undertaken by a qualified independent actuary in order to calculate pension expense as at 31 July 2017.

The major categories of plan assets as a percentage of total plan assets:

	2017	2016
Equities	78%	68%
Bonds	12%	21%
Property	6%	8%
Cash	4%	3%

The major assumptions at 31 July 2017 used by the actuary were:

	2017	2016
Pension increase rate	2.5%	1.9%
Salary increase rate	4.5%	4.4%
Discount rate	2.7%	2.4%

Life expectancy is based on the Fund’s Vita Curves with improvements in line with the CMI2012 model assuming current rates of improvement have peaked and will converge to a long term rate 1.25% p.a.

	Males	Females
Current Pensioners	22.1 years	23.7 years
Future Pensioners*	24.2 years	26.3 years

* Figures assume members aged 45 as at the last formal valuation date.

Life expectancies for the prior period end are based on the Fund’s Vita Curves. The allowance for future improvements is shown below:

Period ending	Prospective pensioners	Pensioners
	CMI2012 model assuming current rates of improvement have peaked and will converge to a long term rate 1.25% p.a.	CMI2012 mode; assuming current rates of improvement have peaked and will converge to a long term rate 1.25% p.a.
31 July 2016		

The mortality assumptions are identical to those used in the previous accounting period.

An allowance is included for future retirements to elect to take 50% of the maximum additional tax-free cash up to HMRC limits for pre-April 2009 service and 75% of the maximum tax-free cash for post-April 2009 service.

Changes in the fair value of plan assets, defined benefit obligation and net liability for year:

Period Ended 31 July	2017			2016		
	Assets	Obligations	Net Asset/ (Liability)	Assets	Obligations	Net Asset/ (Liability)
	£000	£000	£000	£000	£000	£000
Opening Position as at 31 July, previous year						
Fair value of plan assets	110,158	-	110,158	89,671	-	89,671
Present value of funded liabilities	-	(136,759)	(136,759)	-	(112,530)	(112,530)
Present value of unfunded liabilities	-	(241)	(241)	-	(242)	(242)
	110,158	(137,000)	(26,842)	89,671	(112,772)	(23,101)
Defined benefit costs recognised in Profit or (Loss)						
Service Cost						
Current service cost*	-	(5,071)	(5,071)	-	(4,292)	(4,292)
Past service cost (including curtailments)	-	(4)	(4)	-	(17)	(17)
	-	(5,075)	(5,075)	-	(4,309)	(4,309)
Net interest						
Interest income on plan assets	2,652	-	2,652	3,239	-	3,239
Interest cost on defined benefit obligation	-	(3,319)	(3,319)	-	(4,092)	(4,092)
	2,652	(3,319)	(667)	3,239	(4,092)	(853)
	2,652	(8,394)	(5,742)	3,239	(8,401)	(5,162)
Cashflows						
Plan participants’ contributions	793	(793)	-	775	(775)	-
Employer contributions	3,200	-	3,200	3,128	-	3,128
Contributions in respect of unfunded benefits	14	-	14	15	-	15
Benefits paid	(3,316)	3,316	-	(3,422)	3,422	-
Unfunded benefits paid	(14)	14	-	(15)	15	-
	677	2,537	677	481	2,622	3,143
Expected closing position	113,487	(142,857)	(29,370)	93,391	(118,511)	(25,120)
Remeasurements			-			
Changes in financial assumptions	-	(3,816)	(3,816)	-	(19,426)	(19,426)
Other experience	-	21	21	-	937	937
Return on assets excluding amounts included in net interest	10,706	-	10,706	16,767	-	16,767
Changes in asset ceiling	-	-	-	-	-	-
Total remeasurements recognised in Other Comprehensive Income (OCI)	10,706	(3,795)	6,911	16,767	(18,489)	(1,722)
Closing Position as at 31 July 2017	124,193	(146,652)	(22,459)	110,158	(137,000)	(26,842)
Represented by:						
Fair value of plan assets	124,193	-	124,193	110,158	-	110,158
Present value of funded liabilities	-	(146,437)	(146,437)	-	(136,759)	(136,759)
Present value of unfunded liabilities**	-	(215)	(215)	-	(241)	(241)
Closing position as at 31 July	124,193	(146,652)	(22,459)	110,158	(137,000)	(26,842)

* The current service cost includes an allowance for administration expenses of 0.3% of payroll.

** The liability compromises of approximately £215,000 in respect of LGPS unfunded pensions £0 in respect of Teachers’ unfunded pensions. For unfunded liabilities as at 31 July 2017, it is assumed that all unfunded pensions are payable for the remainder of the members life. It is further assumed that 90% of pensioners are married (or cohabiting) at death and that their spouse (cohabitee) will receive a pension between 37.5% and 50% of the member’s pension as at the date of the member’s death.

Information about the defined benefit obligation

	Liability split £(000) as at 31 July 2017	Liability split (%) as at 31 July 2017	Weighted average duration at previous formal valuation
Active members	107,252	73.2%	22.6
Deferred members	16,121	11.0%	23.0
Pensioner members	23,064	15.8%	11.0
Total	146,437	100.0%	18.3

The figures, above, are for the funded obligations only and do not include any unfunded pensioner liabilities. The durations are as they stood at the previous formal valuation as at 31 March 2017.

Analysis of projected amount to be charged to operating profit for the period to 31 July 2018

Period Ended 31 July 2018	Assets £000	Obligations £000	Net (liability)/asset £000 % of pay	
Projected Current service cost*	-	(5,513)	(5,513)	(41)%
Total Service Cost	-	(5,513)	(5,513)	(41)%
Interest income on plan assets	3,359	-	3,359	25 %
Interest cost on defined benefit obligation	-	(3,996)	(3,996)	(29.8)%
Total Net Interest Cost	3,359	(3,996)	(637)	(4.8)%
Total Included in Profit and Loss	3,359	(9,509)	(6,150)	(45.8)%

*The current service cost includes an allowance for administration expenses of 0.3% of payroll. The monetary value is based on a projected payroll of £13,447,000.

The contributions paid by the Employer are set by the Fund Actuary at each triennial actuarial valuation (the most recent being as at 31 March 2014), or at any other time as instructed to do so by the Administering Authority. The contributions payable over the period to 31 March 2018 are set out in the Rate and Adjustments certificate.

The Employer's contributions are estimated for the period to 31 July 2018 to be approximately £3,161,000.

The above figures should be treated as estimates and may need to be adjusted to take account of:

- any material events, such as curtailments, settlements or the discontinuance of the Employer's participation in the Fund;
- any changes to accounting practices;
- any changes to the Scheme benefit or member contribution rates; and/or
- any full funding valuation that may have been carried out on the Employer's behalf.

The monetary amount of the projected service cost for the period to 31 July 2018 may be adjusted to take account of actual pensionable payroll for the period.

Sensitivity analysis

The sensitivities regarding the principal assumptions used to measure the scheme liabilities are set out below:

Change in assumptions at 31 July 2017:	Approximate % increase to Employer Liability	Approximate monetary amount (£000)
0.5% decrease in Real Discount Rate	11%	16,392
0.5% increase in the Salary Increase Rate	4%	5,513
0.5% increase in the Pension Increase Rate	7%	10,381

In order to quantify the impact of a change in the financial assumptions used, the value of the scheme liabilities as at 31 July 2017 has been calculated and compared on varying bases. The approach taken is consistent with that adopted to derive the FRS 102 figures provided in this report.

The principal demographic assumption is the longevity assumption (i.e. member life expectancy). For sensitivity purposes, we estimate that a one year increase in life expectancy would approximately increase the Employer’s Defined Benefit Obligation by around 3-5%. In practice the actual cost of a one year increase in life expectancy will depend on the structure of the revised assumption (i.e. if improvements to survival rates predominantly apply at younger or older ages).

Please note the above figures have been derived based on the membership profile of the Employer as at the date of the most recent actuarial valuation.

The approach taken in preparing the sensitivity analysis shown is consistent with that adopted in the previous year.

c. STSS

Heriot-Watt University participates in the Scottish Teachers' Superannuation Scheme, an unfunded multi-employer defined benefit statutory public service pension scheme with benefits underwritten by the UK Government. The scheme is financed by payments from employers and from those current employees who are members of the scheme and paying contributions at progressively higher marginal rates based on pensionable pay, as specified in the regulations. The rate of employer contributions is set with reference to a funding valuation undertaken by the scheme actuary. The

last four-yearly valuation was undertaken as at 31 March 2012. The next valuation will be as at 31 March 2016 and this will set contribution rates from 1 April 2019.

Because of the nature of the scheme, the University is unable to identify its share of the underlying assets and liabilities on a consistent and reasonable basis and therefore, as required by FRS 102, the University accounts for the scheme as if it were a defined contribution scheme. As a result the amount charged to the Statement of Comprehensive Income and Expenditure is equal to the total of contributions payable by the employer in the year.

The amount charged to the Statement of Comprehensive Income and Expenditure represents the employer’s contributions payable to the scheme in respect of the year. The total contribution made for the year ended 31 July 2017 was £ 73,000 (2016: £72,000), of which employer’s contributions totalled £43,000 (2016: £42,000) and employee’s contributions totalled £30,000 (2016: £30,000). The employer’s contributions include £2,949 (2016: £3,566) of outstanding contributions at the balance sheet date. The employer contribution rate from 1 September 2015 was 17.2% of pensionable pay, which includes a supplementary rate of 4.5% of employers pension contributions (for fifteen years from 1 April 2015) to meet a shortfall of £1.3 billion was identified in the notional fund at the last valuation. While the employee rate applied is a variable it will provide an actuarial yield of 9.6% of pensionable pay.

The University has no obligation for other employers’ obligations to the multi-employer scheme.

As the scheme is unfunded there can be no deficit or surplus to distribute on the wind-up of the scheme or withdrawal from the scheme.

d. National Employment Savings Trust (NEST)

The University and Edinburgh Business School have implemented arrangements to meet the UK statutory requirement for employers to automatically enrol certain workers who are not already pension scheme members into a qualifying pension scheme. In addition to the existing pension schemes, staff can opt to join NEST.

A total of 202 employees were active members at the year end. The employer’s costs for the year ended 31 July 2017 was £7,114 (2016: £5,145).

e. Heriot-Watt Services Limited defined contribution pension scheme

Employees on Heriot-Watt Services Ltd contracts of employment are entitled to contribute to a defined contribution scheme.

The employer’s costs for the year ended 31 July 2017 was £28,764 (2016: £4,061).

27. Financial instruments

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

a. 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 1 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.

	Carrying amount	Contractual cash flows	Within one year	After more than one year
	£000	£000	£000	£000
Financial liabilities				
Trade creditors and other payables (less accruals)	41,993	-	41,864	129
Other financial liabilities	112,409	-	142	112,267
	154,402	-	42,006	112,396

b. 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	
	2017 £000	2016 £000
Financial assets		
Trade debtors and other receivables	38,884	39,230
Cash and cash equivalents	81,648	15,609
Current investments	962	1,660
	121,494	56,499

c. 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

During the current year, the University redeemed the long term loans held with Clydesdale Bank and Barclays; and accepted £112,000,000 by way of private placement fixed interest bonds from three investors.

At the balance sheet date the market risk of the group’s interest bearing financial instruments was as follows:

	2017 £000	2016 £000
Fixed rate instruments		
Financial assets	-	-
Financial liabilities	(112,000)	(32,500)
	(112,000)	32,500
Variable rate instruments		
Financial assets	23,008	10,913
Financial liabilities	-	(12,500)
	23,008	(1,587)

The fair value of the hedging instruments is determined by establishing a market value for the swaps at the balance sheet date, such value being reflected in Balance sheet creditors and the movements being reflected in the Statement of comprehensive income and expenditure. As part of its refinancing arrangements during the year, the University disposed of all of its interest rate swaps.

	2017 £000	2016 £000
Fair value of swaps at 1 August	7,971	5,179
Change in fair value	-	2,792
Redemption of swaps	(7,971)	
Fair value of swap at 31 July	-	7,971

• Currency risk

The 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 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.

d. 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	
	2017 £000	2016 £000
Trade debtors and other receivables	38,884	39,230
Cash and cash equivalents	81,648	15,609
Current investments	962	1,660
Trade creditors and other payables	(41,993)	(56,603)
Other financial liabilities	(112,407)	(53,397)
	(32,906)	(53,501)

The following methods and assumptions were used to estimates 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

28. Access funds

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. The unspent balances repayable to the Funding council are recorded on the Balance Sheet as a Cash asset and an equal liability in Creditors - amounts falling due within one year.

	Childcare	Group hardship	Total
	£000	£000	£000
At 1 August 2016	40	185	225
Repaid to funding body	(40)	(185)	(225)
Funding council grants	71	276	347
Disbursed to students	(145)	(142)	(287)
Vired between funds	110	(110)	-
Balance unspent at 31 July 2017	36	24	60
Repayable to funding body	36	24	60

29. Related party transactions

Due to the nature of the University’s activities and the composition of Court (being drawn from public and private sector organisations) transactions may take place with organisations in which a member of Court may have an interest. From time to time, as supporters of the University, Court members may make donations of varying amounts to assist the University in achieving its goals. All transactions involving organisations in which a member of Court may have an interest are conducted at arm’s length and in accordance with the University’s financial regulations and normal procurement procedures. The registered interests of court members can be accessed on the University’s website at <https://www.hw.ac.uk/about/profile/governance/court.htm>.

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