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Network accounts 2005-2006

[Enterprise and New Towns \(Scotland\) Act 1990](#)

Accounts of Highlands and Islands Enterprise prepared pursuant to section 30(1) of the Enterprise and New Towns (Scotland) Act 1990, for the year ended 31 March 2006 together with the independent auditor's report to the members of Highlands and Islands Enterprise, the Scottish Parliament and the Auditor General for Scotland.

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Management commentary

Background and principal activities

Statutory background

Highlands and Islands Enterprise (HIE) was established in 1991 in accordance with the provisions of the Enterprise and New Towns (Scotland) Act 1990.

Strategic aims

The HIE network's stated aim, as set out in 'A Smart, Successful Highlands and Islands', is to enable people living in the Highlands and Islands to realise their full potential on a long-term sustainable basis. In order to achieve this, the Network pursues four broad strategic objectives: strengthening communities, developing skills, making global connections and growing businesses.

The Network report provides further details of the specific aims and strategy of the Network for 2006/2007.

Principal activities

It was established for the purpose of preparing, concerting, promoting, assisting and undertaking measures for the economic and community development of the Highlands and Islands, maintaining and enhancing skills and capacities relevant to employment, assisting people to establish themselves as self-employed and furthering improvement of the environment in the Highlands and Islands.

Board membership

Mr W Roe, chairman
Mr J R A Cumming CBE, chief executive
Mrs W Campbell OBE
Mr S Graham
Mr D MacInnes MBE
Mr A Mackenzie
Mr D Ratter
Mr A Rogers
Mr G Sword
Mrs S Torrance
Mr G Campbell
Mrs L Forbes

Statement of Highlands and Islands Enterprise's responsibilities

Under section 30(1) of the Enterprise and New Towns (Scotland) Act 1990, Highlands and Islands Enterprise is required to prepare a statement of accounts in the form and on the basis determined by Scottish Ministers. The accounts are prepared on an accruals basis and must give a true and fair view of Highlands and Islands Enterprise's state of affairs at the year end and of its income and expenditure and cash flows for the financial year.

In preparing the accounts, Highlands and Islands Enterprise is required to:

- Observe the accounts direction issued by Scottish Ministers, including the relevant accounting and disclosure requirements, and apply suitable accounting policies on a consistent basis;
- Make judgements and estimates on a reasonable basis;
- State whether applicable accounting standards have been followed, and disclose and explain any material departures in the financial statements;
- Prepare the financial statements on the going concern basis, unless it is inappropriate to presume that the entity will continue in operation.

Financial performance

Results

The results for the year to 31 March 2006 are contained in the attached accounts which have been prepared in accordance with section 30 (1) of the Enterprise and New Towns (Scotland) Act 1990 and are in the form directed by Scottish Ministers.

The Network report provides more detailed information regarding the results for the year. A review of key performance targets is included in the Network report.

Sources of finance

Highlands and Islands Enterprise is mainly financed by Scottish Ministers through the Scottish Executive Enterprise, Transport and Lifelong Learning Department. In addition, it has receipts in the form of rents, interest, loan repayments, European Union funding and proceeds received from the sale of assets. The funding provision and payments for the year ended 31 March 2006 on a cash basis were:

	Provision £m	Actual £m
Funding		
Grant-in-aid	88	88
Receipts	18	20
Utilisation of cash at bank	-	(1)
	106	107
Payments		
Growing businesses	28	25
Making global connections	29	32
Developing skills	15	16
Strengthening communities	10	10
Administration costs	24	24
	106	107

Financial commentary

Highlands and Islands Enterprise achieved its primary financial target on a resource accounting basis (RAB) established by the Scottish Executive for the first time in 2005/06. In overall terms, income for 2005/06 was lower by £6.7 million, primarily due to property sales being lower by £3.5 million and grant-in-aid reducing by £2.3 million. The reduction in grant-in-aid included an offset payment by the Scottish Executive of £3 million towards its centrally funded scheme for developing broadband across Scotland.

Expenditure was correspondingly lower as a result of the income changes. However, lower management administration costs, down £0.9 million to £24.5 million, did enable part of this reduction to be offset into core investment and development activities. The reduction of management and administration costs was primarily due to lower provisions for bad debts and losses.

On 1 March, 2006, the Network launched an organisational review which is examining Network architecture and operations and which includes a rationalisation of office premises and a review of staffing across the Highlands and Islands. This is in line with the Scottish Executive's efficient government initiative and will ensure that management and administration operations and costs remain effective and efficient.

Pension liabilities and funding also showed a significant improvement in 2005/06 as a result of improved stock market returns and fund management performance resulting in an actuarial gain of £11.954 million. The pension liability has reduced from £16.6 million to £5.3 million in 2005/06.

One potential contingent liability remains unresolved in relation to the 2004/05 European audit on the Objective One programme. This report remains in draft and the Network has responded in full to all the requests for further information and supporting documentation.

Future developments

The 2005-06 Network report includes a section on key measures of progress 2006-09, together with details of primary measures for each of the organisation's four strategic objectives. Future developments include:

- Implementation of the Highlands and Islands network's organisational review
- Continued integration of Careers Scotland with the Highlands and Islands Enterprise network, together with a property rationalisation programme to create integrated LEC and Careers Scotland offices across the network
- Ongoing construction of the Centre for Health Science
- Supporting communities to own and manage assets
- Address the economic and business needs of Moray post the RAF rationalisation under the Moray 2020 project
- Taking forward in partnership a strategic framework and action plan for the Caithness economy, addressing the shorter Dounreay rundown timescale

Post balance sheet events

A consortium led by HIE has been selected as the successful tenderer for delivery of the Growing Community Assets (GCA) fund which will replace the Scottish Land Fund. GCA will provide £50 to £75 million over a three-year period to community groups throughout rural and urban Scotland for acquisition and development of a wide range of assets. The community land unit will manage the contract, with an enhanced administrative team based in Auchtertyre. Service delivery will commence on the 3rd July, and will be fully operational on 1st October 2006.

As a result of the HIE network organisational review, boundary changes were made, which impacted on three local enterprise companies (LECs).

- The geographical area which was formerly the responsibility of Ross and Cromarty Enterprise Limited was re-allocated to the other companies as noted below. Ross and Cromarty Enterprise Limited ceased to be an operational LEC.
- The areas of Easter Ross and the Black Isle were transferred to Inverness, Nairn, Badenoch and Strathspey Local Enterprise Company Limited and its name was changed to HIE Inverness and East Highland.
- The area of Wester Ross was transferred to Skye and Lochalsh Local Enterprise Company Limited and its name was changed to HIE Skye and Wester Ross.

These changes were effective from 3 April, 2006.

Fixed assets

During the year, Highlands and Islands Enterprise network spent £16 million on site development and construction of factory buildings.

At 31 March 2006, the net book value of the Network's tangible fixed assets was £38 million. Commercial properties were valued at market value. Loans and share investments amounted to £2.2 million for Highlands and Islands Enterprise; the Network's investments amounted to £7.6 million.

European Union

In addition to the funding from grant-in-aid, funds amounting to £8.9 million were received from the European Union in support of the operations of the Highlands and Islands Enterprise network. The local enterprise companies received £0.4 million of the total European Union funding and the balance of £8.5 million was received by Highlands and Islands Enterprise.

Payment to creditors

The HIE network observes the Government's policy for prompt payment under the Better Payment Practice Code and is committed to paying suppliers within one month of receipt of a valid invoice, where no other contract timetable applies.

During the year ended 31 March 2006, the HIE network paid 99 per cent of all invoices received within the terms of this payment policy.

Key performance indicators

Key measures of progress

Through identifying a range of projects which reflect the essence of what the Network does and by reporting primarily against these, this year has seen a significant change of focus for the Network.

These key measures of progress in HIE's results show major strategic projects which made progress in 2005-06 by meeting or approaching the milestones identified for them. Highly satisfactory progress has been recorded for UHI, the Centre for Health Science, broadband, renewable energy, the Community Energy Company, Dounreay decommissioning and Highland 2007. Each project has either met or is well on course to meet the milestones identified for them. Progress with Arnish, ABSL and Eden Court Theatre redevelopment has been satisfactory but slightly less than hoped for in some aspects, although this has largely been due to circumstances which are outwith the Network's influence.

Primary measures of progress

Group	Measure	Target	Actual	Performance %
Strengthening communities	New/enhanced community assets	450	559	124
	Community groups with increased capacity	115	178	155
Developing skills	People supported to move towards and into sustainable work	2,405	2,999	125
	Businesses supported to engage in developing the skills of those in work	655	983	150
Growing businesses	New business starts	500	576	115
	Business growth projects	355	356	100
Making Global connections	Private sector earnings (%)	108	117	108
	Businesses engaging in international business development	115	166	144

Details of both the key and primary measures of performance are provided in the Network report.

Corporate governance

Overview

The Highlands and Islands Enterprise network has in place procedures which ensure that the highest standards of corporate governance are maintained at all times.

Risk assessment

The Highlands and Islands Enterprise network, in line with best practice, has robust procedures in place for the systematic identification and management of risk. A risk management strategy highlights that effective risk management is essential to the achievement of the Network's objectives. Implementation of the strategy includes a quarterly assessment of risk by management and the assessment of risk at individual project level. Where appropriate, action plans are put in place to address significant risks. The chief executive, as accountable officer, is pleased to report that these procedures have been complied with throughout the year.

The board

At 31 March 2006, the board of Highlands and Islands Enterprise comprised the chairman, ten non-executive members and one executive member who is the chief executive. Board members are appointed by Scottish Ministers and their remuneration is determined by the Scottish Executive Enterprise, Transport and Lifelong Learning Department.

The board meets at least eight times a year. The role of the board is the strategic oversight of the Network, ensuring that it is carrying through its statutory remit. The board has specific responsibility for approving the overall strategy and operating plans, ensuring that the executive has thorough arrangements for appraisal, monitoring and evaluation of programmes and seeing that targets are set and met.

As a board member, the chief executive also has a pivotal role in assisting the board to develop policies and priorities and in ensuring that they are implemented effectively.

Audit committee

Highlands and Islands Enterprise has an audit committee composed of four non-executive members of the board, one of whom acts as its chairman. The chief executive in his role as accountable officer, a representative of the Scottish Executive departmental accountable officer, the director of corporate services, having specific responsibility for finance, and the head of internal audit normally attend the meetings of the committee which are held no fewer than four times per year.

The members of the audit committee during the year were:

Mr A Mackenzie (chair)
Mr G Sword
Mrs S Torrance
Mr G Campbell

The combined code

While the remuneration and the service contracts of board members are set by the Scottish Executive Enterprise, Transport and Lifelong Learning Department, the recommendations of the combined code have been applied in so far as they are appropriate to Highlands and Islands Enterprise. Full details of all elements in the remuneration package of each board member are disclosed in the remuneration report.

Conflicts of interest procedures

The HIE network operates strict and comprehensive procedures to deal with potential conflicts of interest. These include the HIE core and each LEC holding, and updating at least annually, registers of interests covering not only board members/directors but also members of staff. These registers are available to any member of the public who wishes to examine them. Interests which must be registered, in terms of the name and nature of the organisation in which the interest is held, include: remuneration, related undertakings, contracts, houses, land and buildings, shares and securities, non-financial interests, gifts and hospitality.

Whenever a board member/director or member of staff has an interest in an application for assistance, they are required to declare the interest and thereafter to take no part in the investigation, processing or approval of the case. Such declarations by board members/directors are recorded in the minutes of the appropriate board meetings.

Additional procedures are invoked when a LEC chair declares an interest (such cases are referred to HIE for processing and decision).

Public interest reporting

Complaints

The HIE network has in place a clear policy for dealing with complaints. Where it is not possible to resolve the complaint internally a complainant is entitled under the terms of the Scottish Public Services Ombudsman Act 2002 to have their complaint considered by the Scottish Public Services Ombudsman. Further details of complaints are provided in the Network report.

Openness

The HIE network believes it is fully compliant with the Freedom of Information (Scotland) 2002 Act. The HIE network is committed to being as open as possible, recognising the need to balance openness with being able to conduct its business effectively and in accordance with the remit laid down by the Scottish Executive.

Customer service

The HIE network regularly monitors progress in meeting the Government's customer service standards such as Charter Mark and, if necessary, takes action to ensure that effective performance is maintained or achieved. The HIE network was awarded Charter Mark status for the fourth time in December 2004 and, following a further, independent on-site review in December 2005, Charter Mark assessors found that the HIE network had demonstrated ongoing compliance with the Charter Mark standards.

Statement of chief executive's responsibilities

The accountable officer for the Scottish Executive Enterprise, Transport and Lifelong Learning Department has designated the chief executive as the accountable officer for Highlands and Islands Enterprise. His relevant responsibilities as accountable officer, including his responsibility for the propriety and regularity of the public finances and for the keeping of proper records, are set out in the Memorandum to Accountable Officers of other Public Bodies issued by Scottish Ministers.

Diversity and equal opportunity

The Highlands and Islands Enterprise network's aim is to help the people, businesses and communities of the Highlands and Islands to realise their full potential. The network wants this aspiration to be within the reach of every single resident of our area.

We have a very broad remit which means we work with individuals (helping them to acquire the skills they need to succeed in the labour market, offering careers advice and guidance), businesses (assisting the establishment of new enterprises and the growth of existing ones). We also support community groups to acquire assets and develop the confidence needed to fulfil their aspirations.

Our commitment to equal opportunities goes beyond a desire to comply with legislation. Our aspiration for the population of this region to grow by around 65,000 over the next twenty years means we need to be proactive in ensuring assistance from our Network is accessible to all people who choose to live, work and study here.

We have also expressed our desire for this region to be a shop window for the best that Scotland has to offer. This means we need to work to encourage a tolerant society and to celebrate diversity in all its forms.

Equality statement

HIE aims to be an equal opportunities employer and is committed to treating all existing and prospective employees in the same way, regardless of sex, race, ethnic origin or nationality, religion or belief, age, sexual orientation, disability or any other factor irrelevant to the ability to do the job. Monitoring of equality information for both current and potential employees enables HIE to ensure adherence to the legal framework and to propose best practice arrangements.

There are currently nine employees in the Highlands and Islands Enterprise network who have declared a disability.

Employee involvement and communication

The Highlands and Islands Enterprise network values the contribution of all employees and encourages a culture of open, two-way communication. As an Investor in People employer, the Network places great emphasis on learning and development and provides opportunities for personal development and further education.

Employees are kept up to date through formal and informal communication. Regular briefings from the management group on key issues and decisions are available to all employees of the network. Weekly team meetings are encouraged throughout the network to cascade information and facilitate discussion, and employees have the opportunity to attend quarterly presentations each year on current Network performance and future priorities. These meetings also provide employees with the opportunity to raise other issues with the chief executive and the senior management team. In addition, new developments are introduced through workshops and presentations to all, or groups of employees. Regular updates, office notices and newsletters are published on the intranet.

Formal consultation takes place through the Joint Negotiating Committee (JNC), which involves members of HIE management, local trade union representatives and full-time officials from the Public and Commercial Services Union (PCS) and UNISON. The JNC meets at least five times a year.

Pension costs

All staff with contracts of three months or more are eligible to join the Highlands and Islands Enterprise superannuation scheme. Further details are provided in the remuneration report.

Appointment of auditors

The accounts of Highlands and Islands Enterprise are audited by auditors appointed by the Auditor General for Scotland. The appointed auditor for the year ended 31 March 2006 was Hugh Hall, managing director of audit services, Audit Scotland. Fees chargeable for audit services provided by Audit Scotland amounted to £129,200 (2005 - £128,200).

J R A Cumming
Highlands and Islands Enterprise
21 September 2006

Remuneration report

General

Highlands and Islands Enterprise's sponsoring body, the Scottish Executive, approves changes to Highlands and Islands Enterprise's staff terms and conditions, including pay. Highlands and Islands Enterprise's pay structure covers all employees within the HIE network, including Careers Scotland and aims to address organisational challenges such as recruitment and retention and organisational change. This ensures continuation of the modernisation process, which commenced in 2002 with the introduction of a new pay and grading structure. This structure guarantees pay progression based on inflation rate changes, plus an element of performance-related progression linked to Highlands and Islands Enterprise's performance management system, introduced in April 2004.

Highlands and Islands Enterprise has not yet established a remuneration committee but it is reviewing the position later in the year.

Board members

Board members of Highlands and Islands Enterprise are appointed by Scottish Ministers normally for a period of three years. Board members are eligible for reappointment for a second term. Their remuneration is set by the Scottish Executive and is not pensionable. No benefits in kind were made to members of the board during the year ended 31 March 2006.

The remuneration of HIE board members was as follows for the year ended 31 March 2006:

	2006 £	2005 £
Mr W Roe (chairman – appointed 1 September 2004)	49,002	26,475
Dr James Hunter, CBE (chairman – resigned 31 August 2004)	-	22,967
Mrs M Campbell (resigned 11 October 2004)	-	5,630
Mrs W Campbell, OBE	9,812	9,651
Mr S Graham	9,812	9,651
Mr A Mackenzie	9,812	9,651
Mr D MacInnes, MBE	9,812	9,651
Mr D Ratter	9,812	9,651
Mr A Rogers	9,812	9,651
Mr W Roe	-	4,021
Mr G Sword	9,812	9,651
Mrs S Torrance	9,812	9,651
Mr G Campbell (appointed 12 October 2004)	9,812	4,550
Mrs L Forbes (appointed 12 October 2004)	9,812	4,550

The above figures represent emoluments earned as board members during the relevant financial year. The figure for Mr Roe includes £2,304 of travel expenses which have been subject to tax and national insurance.

Highlands and Islands Enterprise is also required to meet the pension benefits due to former full-time chairmen and board members of Highlands and Islands Development Board and those of Highlands and Islands Enterprise who were not members of the superannuation scheme. During the year ended 31 March 2006, £76,652 (2005 - £75,050) was paid to these former members.

Chief executive

The chief executive's contract of employment was signed on 1 November 2000. This is a permanent contract with a 12-month notice period. There are no early termination payment clauses within the contract. No benefits in kind were made to the chief executive.

The remuneration of Mr J R A Cumming, chief executive, for the year ended 31 March 2006 was as follows:

	2006 £	2005 £
Salary	97,754	95,370
Performance-related bonus	9,537	9,350
Pension contributions	19,942	19,455
	127,233	124,175

The chief executive is an ordinary member of the Highlands and Islands Enterprise superannuation scheme. Under the terms of the chief executive's contract of employment, an annual bonus, subject to performance review, of up to 10 per cent (2005 - 10 per cent) of basic salary, is payable. The review, conducted by the chairman, measures the chief executive's performance during the financial year against a series of targets set at the beginning of that year and relates to the performance of the HIE network as a whole.

Senior members of the HIE management group

The contracts of senior members of the HIE management group are permanent and have a three-month notice period. There are no early termination payment clauses within these contracts. No benefits in kind were made to senior members of the HIE management group.

The remuneration of senior members of the HIE management group for the year ended 31 March 2006 was as follows:

	2006 £	2005 £
A B Brady	62,605	60,734
F Duthie	56,403	54,590
J D MacDiarmid	61,493	60,883
M Haswell (resigned 22 April 2004)	-	3,021
S Myles (appointed 1 June 2004)	46,841	38,040
A Paterson	57,102	56,532
W P Sylvester	53,364	51,578
J A Watt	49,765	48,012
J F Wright	53,480	52,118
D Yule (appointed 1 January 2006)	15,000	-

The above figures represent emoluments earned as directors during the relevant financial year with the exception of performance-related payments which are disclosed on a paid basis.

Pension benefits

	Accrued pension at age 60 as at 31/3/06 and related lump sum	Real increase in pension and related lump sum at age 60 31/3/05	CETV at 31/3/06	CETV at 31/3/05	Real increase in CETV
	Bandings of £5,000	Bandings of £5,000	£'000	£'000	£'000
J R A Cumming	35-40 Lump sum 110-115	0-5 Lump sum 0-5	652	532	105
A B Brady	20-25 Lump sum 65-70	0-5 Lump sum 0-5	400	321	71
F Duthie	5-10 Lump sum 25-30	0-5 Lump sum 0-5	128	95	30
J D MacDiarmid	25-30 Lump sum 75-80	0-5 Lump sum 0-5	424	339	75
A Paterson	0-5 Lump sum 5-10	0-5 Lump sum 0-5	36	21	13
W P Sylvester	5-10 Lump sum 15-20	0-5 Lump sum 0-5	116	87	27
J A Watt	10-15 Lump sum 40-45	0-5 Lump sum 0-5	250	198	47
J F Wright	0-5 Lump sum 5-10	0-5 Lump sum 0-5	35	21	13
S Myles (appointed 1/6/04)	0-5 Lump sum 0-5	0-5 Lump sum 0-5	11	4	6
D Yule (appointed 1/1/06)*	5-10 Lump sum 15-20	0-5 Lump sum 0-5	76	72	4

* Mr D Yule joined the Highlands and Islands management group on 1 January 2006. The increase in benefit figures shown above in respect of Mr Yule relate to the period between 1 January 2006 and 31 March 2006.

The chief executive and senior members of the HIE management group are members of the Highlands and Islands Enterprise superannuation scheme. This scheme provides benefits based on final pensionable salary. The assets of the scheme are held separately from those of Highlands and Islands Enterprise and are invested with independent investment managers agreed by the scheme's trustees.

Employee contributions are currently set at a rate of 1.5 per cent of pensionable earnings. The level of employee contributions for new members joining the scheme is to be reviewed during the year ahead. Highlands and Islands Enterprise meets the contributions that are necessary to meet the full balance of the cost of the benefits provided by the scheme as well as the costs of running the scheme.

Benefits accrue at the rate of one eightieth (1/80) of pensionable salary for each year of service subject to a maximum of 40 years. In addition, a lump sum equivalent to three years' pension is payable on retirement.

Cash equivalent transfer values (CETV)

A cash equivalent transfer value (CETV) is the actuarially assessed capitalised value of the pension scheme benefits accrued by a member to a particular point in time. The benefits valued are the member's benefits and any contingent spouse's pension payable from the scheme. A CETV is a payment made by a pension scheme or arrangement to secure pension benefits in another pension scheme or arrangement when the member leaves a scheme and chooses to transfer the benefits accrued in the former scheme. The pension figures shown relate to the benefits that the individual has accrued as a consequence of their total membership of the pension scheme, not just their service in a senior capacity to which disclosure applies.

Real increase in CETV

This reflects the increase in CETV effectively funded by the employer. It takes account of the increase in accrued pension due to inflation, contributions paid by the employee (including the value of any benefits transferred from another pension scheme or arrangement) and uses common market valuation factors for the start and end of the period.

J R A Cumming
Highlands and Islands Enterprise
21 September 2006

Statement on internal control

1 As accountable officer, I have responsibility for maintaining a sound system of internal control that supports the achievement of Highlands and Islands Enterprise's policies, aims and objectives, set by Scottish Ministers, whilst safeguarding the public funds and assets for which I am personally responsible, in accordance with the responsibilities assigned to me.

2 The system of internal control is designed to manage rather than eliminate the risk of failure to achieve policies, aims and objectives; it can therefore only provide reasonable and not absolute assurance of effectiveness.

3 The system of internal control is based on an ongoing process designed to identify the principal risks to the achievement of the organisation's policies, aims and objectives, to evaluate the nature and extent of those risks and to manage them efficiently, effectively and economically. This process has been in place for the year ended 31 March 2006 and up to the date of approval of the annual report and accounts, and accords with guidance from the Scottish Executive.

4 As accountable officer, I also have responsibility for reviewing the effectiveness of the system of internal control. The following processes have been established for the HIE network:

- A management group which normally meets weekly. Major executive decisions are taken by myself in consultation with that group.
- A board which normally meets eight times a year. The board is comprised of a part-time chairman, 10 non-executive members and myself. The board is responsible for the overall direction of the organisation within the strategic and funding framework set by Scottish Ministers. It has a general corporate responsibility for:
 - ensuring that Highlands and Islands Enterprise complies with any statutory or administrative requirements for the use of public funds and, in so doing, satisfying itself that Highlands and Islands Enterprise operates within the delegated authorities agreed with the Scottish Executive Enterprise, Transport and Lifelong Learning Department;
 - ensuring that high standards of corporate governance are observed at all times;
 - ensuring that its aims and objectives are explained to and understood by staff; and
 - overseeing the delivery of planned results by monitoring performance against agreed corporate objectives, measures and targets on both an in-year and longer-term basis.
- An audit committee, chaired by a non-executive board member, which meets no fewer than four times a year and which reviews the effectiveness of the internal control system. Minutes of the audit committee are copied to the full board.
- A health and safety committee, chaired by a non-executive board member, exists to review the Network's compliance with health and safety legislation. This committee met four times in the past year. Minutes of the health and safety committee are copied to the full board.
- Highlands and Islands Enterprise has a robust risk management strategy in place. This strategy highlights that effective risk management is essential to the achievement of the Network objectives. Implementation of this strategy includes:
 - the quarterly assessment of risk by management;
 - the maintenance of organisation-wide risk registers;
 - the maintenance of a strategic risk register;
 - assessment of risk at individual project level;
 - gateway reviews for high risk projects;
 - action plans with clear accountability and timescales to address significant risks.
 - the Highlands and Islands Enterprise board and the Scottish Executive are made aware of the key risks for the Network on a quarterly basis.
 - formal project appraisal training has been provided to senior management and board members. This includes detailed training on risk assessment and management.
 - corporate governance workshops on ethical standards held for senior executive staff and non-executives.
 - setting targets to measure financial and other business objectives.

5 Highlands and Islands Enterprise has an internal audit and compliance team which is independent of any operational group. The head of internal audit and compliance reports directly to me as accountable officer.

The work of the internal audit and compliance team is informed by an analysis of the risk to which the HIE network is exposed and annual internal audit plans are based on this analysis. The plan is endorsed by the HIE audit committee.

The head of internal audit and compliance provides me with regular reports on internal audit activity and provides me with an annual report which includes the head of internal audit and compliance's independent opinion on the adequacy and effectiveness of the system of internal control together with recommendations for improvement.

The internal audit and compliance team supports the Network's continuous improvement activities through the identification of action points arising from on-going audit activity. These actions cover all aspects of the Network's operations.

During the last financial year, the HIE network has continued to undergo significant operational change. The internal audit and compliance team has worked with management to identify areas for improvement and make recommendations on any actions required with respect to the internal control environment.

The internal audit plan includes cyclical reviews of the implementation of the HIE network risk management strategy.

6 My review of the effectiveness of the system of internal control is informed by the work of the internal auditors; the audit committee, which oversees the work of the internal audit and compliance team; the executive managers within the organisation who have responsibility for the development and maintenance of the internal control framework and comments made by the external auditors in their management letters and other reports.

7 Recent internal audit reviews have highlighted the following area for improvement in the internal control environment:

- Compliance with European audit requirements in respect of retention of supporting documentation for EU funded schemes and European direct funded projects. A working group has been set up to address this issue.

J R A Cumming
Accountable officer
21 September 2006

Independent auditor's report

To the members of Highlands and Islands Enterprise, the Auditor General for Scotland and the Scottish Parliament

I have audited the financial statements of Highlands and Islands Enterprise for the year ended 31 March 2006 under the Enterprise and New Towns (Scotland) Act 1990. These comprise the Income and Expenditure Account, Balance Sheets, the Cash Flow Statement and Statement of Total Recognised Gains and Losses and the related notes. These financial statements have been prepared under the accounting policies set out within them.

This report is made solely to the parties to whom it is addressed in accordance with the Public Finance and Accountability (Scotland) Act 2000 and the Code of Audit Practice approved by the Auditor General for Scotland and for no other purpose as set out in paragraph 43 of the Statement of Responsibilities of Auditors and of Audited Bodies prepared by Audit Scotland, dated July 2001.

Respective responsibilities of the Board of Highlands and Islands Enterprise, the Chief Executive and Auditor

The Board and Chief Executive are responsible for preparing the annual report and the financial statements in accordance with the Enterprise and New Towns (Scotland) Act 1990 and directions made thereunder by the Scottish Ministers. The Chief Executive is also responsible for ensuring the regularity of expenditure and receipts. These responsibilities are set out in the Statement of Accountable Officer's Responsibilities.

My responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and with International Standards on Auditing (UK and Ireland) as required by the Code of Audit Practice approved by the Auditor General for Scotland.

I report my opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with the Enterprise and New Towns (Scotland) Act 1990 and directions made thereunder by the Scottish Ministers. I also report whether in all material respects the expenditure and receipts shown in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers. I also report if, in my opinion, the Management Commentary is not consistent with the financial statements, if the body has not kept proper accounting records, if I have not received all the information and explanations I require for my audit, or if information specified by relevant authorities regarding remuneration and other transactions is not disclosed.

I review whether the Statement on Internal Control reflects the body's compliance with the Scottish Executive's guidance. I report if, in my opinion, it does not comply with the guidance or if it is misleading or inconsistent with other information I am aware of from my audit of the financial statements. I am not required to consider, nor have I considered, whether the statement covers all risks and controls. Neither am I required to form an opinion on the effectiveness of the body's corporate governance procedures or its risk and control procedures.

I read the other information contained in the annual accounts and consider whether it is consistent with the audited financial statements. This other information comprises only the Management Commentary and the unaudited part of the Remuneration Report. I consider the implications for my report if I become aware of any apparent misstatements or material inconsistencies with the financial statements. My responsibilities do not extend to any other information.

Basis of audit opinions

I conducted my audit in accordance with the Public Finance and Accountability (Scotland) Act 2000 and International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board as required by the Code of Audit Practice approved by the Auditor General for Scotland. An audit includes examination, on a test basis, of evidence relevant to the amounts, disclosures and regularity of expenditure and receipts included in the financial statements. It also includes an assessment of the significant estimates and judgements made by the Board and Chief Executive in the preparation of the financial statements, and of whether the accounting policies are appropriate to the body's circumstances, consistently applied and adequately disclosed.

I planned and performed my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence to give reasonable assurance that the financial statements and the part of the Remuneration Report to be audited are free from material misstatement, whether caused by fraud or error, and that in all material respects the expenditure and receipts shown in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers. In forming my opinion I also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the Remuneration Report to be audited.

Opinion

Financial statements

In my opinion:

- the financial statements give a true and fair view, in accordance with the Enterprise and New Towns (Scotland) Act 1990 and directions made thereunder by the Scottish Ministers, of the state of affairs of Highlands and Islands Enterprise and the Highlands and Islands Enterprise network as at 31 March 2006 and of the excess of expenditure over income, total recognised gains and losses and cash flows for the year then ended; and
- the financial statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with the Enterprise and New Towns (Scotland) Act 1990 and directions made thereunder by the Scottish Ministers.

Regularity

In my opinion in all material respects the expenditure and receipts shown in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers.

Hugh Hall
Managing Director
Audit Scotland
110 George Street
Edinburgh
EH2 4LW

27 September 2006

Network income and expenditure account

for the year ended 31 March 2006

	Notes	2006 £000	2005 £000
Income from operating activities	2	16,854	17,193
Expenditure on operating activities	3	(77,073)	(77,121)
Administration and management charges	4	(24,529)	(25,486)
Excess of expenditure over income on operating activities		(84,748)	(85,414)
Share of associates' operating loss		(353)	(68)
Notional interest charge	5	(1,718)	(1,609)
Investment income	6	32	(132)
Share of associates' investment income		164	353
Interest payable	7	-	(10)
Excess of expenditure over income on ordinary activities before taxation		(86,623)	(86,880)
Taxation	10	(27)	(48)
Excess of expenditure over income on ordinary activities after taxation		(86,650)	(86,928)
Notional interest credit	5	1,718	1,609
Excess of expenditure over income for the year	21	(84,932)	(85,319)

All income and expenditure for each of the two years ended 31 March 2006 and 2005 arises from continuing activities.

Network statement of total recognised gains and losses

for the year ended 31 March 2006

	Notes	2006 £000	2005 £000
Excess of expenditure over income for the year		(84,932)	(85,319)
Unrealised (deficit)/surplus on revaluation of property	21	(62)	29
Actuarial gain	21	11,954	554
Grant-in-aid received during the year	21	85,020	90,248
Total recognised gains for the year		11,980	5,512

Network and Highlands and Islands Enterprise balance sheets

as at 31 March 2006

	Notes	Network		HIE	
		2006 £000	2005 £000	2006 £000	2005 £000
Fixed assets					
Tangible assets	11	37,822	39,436	37,275	38,825
Investments	12	7,622	5,258	2,177	703
Investment in associate		664	1,019	-	-
		46,108	45,713	39,452	39,528
Current assets					
Stocks	13	-	-	-	-
Debtors	14	10,058	6,965	18,694	14,040
Cash at bank and in hand	15	2,464	3,101	1,209	1,887
		12,522	10,066	19,903	15,927
Current liabilities					
Creditors: amounts falling due within one year	16	8,133	6,056	11,727	8,327
Net current assets		4,389	4,010	8,176	7,600
Total assets less current liabilities		50,497	49,723	47,628	47,128
Creditors: amounts falling due after more than one year	17	1,081	951	1,081	951
		49,416	48,772	46,547	46,177
Pension liability	18	5,309	16,645	5,309	15,018
Net assets		44,107	32,127	41,238	31,159
Reserves					
Revaluation reserve	21	157	219	157	219
Other reserve	21	400	320	-	-
Pension reserve	21	(5,309)	(16,645)	(5,309)	(15,018)
General reserve	21	48,859	48,233	46,390	45,958
		44,107	32,127	41,238	31,159

J R A Cumming
Accountable Officer
21 September 2006

Network cash flow statement

for the year ended 31 March 2006

	Notes	2006 £000	2005 £000
Net cash outflow from operating activities	22	(74,216)	(78,517)
Returns on investments and servicing of finance	23	958	439
Taxation	23	(14)	(9)
Capital expenditure and financial investment	23	(15,493)	(14,481)
Net cash outflow before financing		(88,765)	(92,568)
Financing	23	88,128	93,054
(Decrease)/increase in cash		(637)	486
Reconciliation of net cash flow to movement in net funds			
(Decrease)/increase in cash		(637)	486
Cash outflow from lease financing		-	-
Movement in net funds		(637)	486
Net funds at 1 April 2005		3,101	2,615
Net funds at 31 March 2006	24	2,464	3,101

Notes to the accounts

1. Accounting policies

Basis of preparation

The accounts have been prepared in a form determined by Scottish Ministers, in accordance with Section 30(1) of the Enterprise and New Towns (Scotland) Act 1990.

The accounts are prepared under the historical cost convention, modified to include the open market value of land and buildings held for industrial and commercial use.

They are prepared on a basis that takes account of the functions and objectives of Highlands and Islands Enterprise and its subsidiaries which, without limiting the information given, meet the requirements of the Companies Act 1985 and applicable accounting standards.

Basis of consolidation

The Network accounts consolidate the accounts of Highlands and Islands Enterprise and its subsidiary undertakings drawn up to 31 March each year.

One of these, Careers Trust Scotland Limited is funded in partnership with Scottish Enterprise. The consolidated accounts include the results of Careers Trust Scotland Limited in respect of its activities relating to the Highlands and Islands Enterprise network.

The results of Highlands and Islands Community Energy Company Limited, a wholly owned subsidiary of Highlands and Islands Enterprise, are consolidated within the accounts of the HIE network.

The results of Hi-Wide Limited, a wholly owned subsidiary of Highlands and Islands Enterprise, are not consolidated within the accounts of the HIE network.

The results of PICT Innovation Limited, a wholly owned subsidiary of Highlands and Islands Enterprise, are not consolidated within the accounts of the HIE network.

No income and expenditure account is presented for Highlands and Islands Enterprise as permitted by section 230 of the Companies Act 1985 and with the approval of Scottish Ministers.

Undertakings, other than subsidiary undertakings, in which the Network has an investment representing 20 per cent, or more than 20 per cent of the voting rights and over which it exerts significant influence, are treated as associated undertakings.

The Network accounts include Highlands and Islands Enterprise's share of the results and reserves of HIE Ventures Limited, based on audited accounts to 31 March 2006.

Scottish Health Innovations Limited, Scottish Intellectual Asset Management Limited and ITI Scotland Limited are jointly owned with Scottish Enterprise. The Network accounts include Highlands and Islands Enterprise's share of the results and reserves of Scottish Health Innovations Limited and Scottish Intellectual Asset Management Limited, based on audited accounts to 31 March 2006.

The consolidated accounts do not include the results of ITI Scotland Limited. The results of this company are included in the accounts of Scottish Enterprise.

In the opinion of Highlands and Islands Enterprise, none of the other minority investments conform to the definition of associated companies contained in Financial Reporting Standard 9.

Basis of operations

Highlands and Islands Enterprise contracts with nine (2004-2005 – 10) local enterprise companies (LECs), which are companies limited by guarantee, for the creation and delivery of business development, training and environmental programmes at a local level. Careers Trust Scotland Limited, a company limited by guarantee, was formed to enable the advancement of education and training in Scotland. Highlands and Islands Community Energy Company Limited, a company limited by guarantee, was formed to promote involvement in renewable energy initiatives. HIE Ventures Limited is a venture capital company aimed at companies operating in the Highlands and Islands. Scottish Health

Innovations Limited, a company limited by guarantee, was formed to promote research and development within the National Health Service in Scotland, particularly the commercialisation of research, technology and innovations. Scottish Intellectual Asset Management Limited, a company limited by guarantee, was formed to help build Scotland's competitiveness in a modern knowledge economy by enabling Scottish businesses to exploit their intellectual assets.

Accounting for grant-in-aid

Highlands and Islands Enterprise receives grant-in-aid from Scottish Ministers to finance its capital expenditure and the excess of its revenue expenditure over attributable income. Grant-in-aid is credited to general reserves and the net expenditure set against this on the basis that grant-in-aid cannot be allocated between revenue and capital expenditure as disclosed in the accounts.

European Union funding and other grants

Claims for funding relating to investments and capital building works in respect of assets are deducted from the additions to fixed assets. This is not in strict accordance with Schedule 4 to the Companies Act, which requires assets to be shown at their purchase price or cost and hence grants and contributions would be shown as deferred income. This departure is considered necessary to give a true and fair view, as the assets involved are non-depreciating fixed assets and contributions would not be taken to the income and expenditure account. No funding relating to investment additions was received in the years ended 31 March 2005 and 31 March 2006. Additions to tangible fixed assets are reduced by £3,576,807 in the year to 31 March 2006. Additions in the year to 31 March 2005 were £3,940,000 lower than they would otherwise have been.

Grants receivable in respect of operating expenditure are credited to income in the period to which they relate.

Land and buildings

Land and buildings held for industrial and commercial use are accounted for in accordance with the principles of Statement of Standard Accounting Practice 19 (SSAP 19) 'Accounting for Investment Properties'. These are included in the balance sheet on the basis of open market value, as defined by the guidance notes issued by the Royal Institution of Chartered Surveyors. Professional, external valuations are carried out annually.

Deficits arising on revaluation, which are considered to be of a permanent nature, are charged to the income and expenditure account under the commercial property revaluation adjustment (note 10). Surpluses on revaluation are credited to a revaluation reserve after eliminating any accumulated deficit originally charged to the income and expenditure account in accordance with SSAP 19 (revised).

The implications of Financial Reporting Standard 15 (FRS 15) 'Tangible Fixed Assets' have been considered in relation to the HIE network. However, due to the nature of the tangible fixed assets held by Highlands and Islands Enterprise and its subsidiaries, it is not considered appropriate to apply it to these accounts.

Tenants' improvements

Tenants' improvements are depreciated on a straight line basis over their useful life at rates of 4 - 25 per cent per annum.

Plant and equipment

Plant and equipment are depreciated on a straight line basis over the useful life of the asset at a rate of 25 per cent per annum.

Investments and loans

Investments are shown at cost less provision for any diminution in value. No investments are valued at more than cost even though the underlying value may have increased. Loans are shown at the amount outstanding at the balance sheet date less provision for estimated losses.

Local enterprise company assets and investments

Tangible fixed assets and investments purchased by local enterprise companies, in their own name with funds provided under the operating contract with Highlands and Islands Enterprise, are included in the accounts of the relevant local enterprise company at cost or valuation less depreciation and provisions as appropriate. Under the terms of the operating contract, all sums due from the disposal of these assets and investments and income arising from these assets fall to be repaid to Highlands and Islands Enterprise. The net book value of these assets and investments is included in the balance sheet of Highlands and Islands Enterprise under debtors.

Stocks

Stocks are stated at market value.

Irrecoverable income

Irrecoverable debts are written off at the earliest opportunity. Provision is made for debts which are considered unlikely to be recovered.

Leases

Assets acquired under finance leases are capitalised in the balance sheet and depreciated over their useful lives. The interest element of the rental obligations is charged to the income and expenditure account over the period of the lease and represents a constant proportion of the balance of capital repayments outstanding. Rentals paid under operating leases are charged to the income and expenditure account on a straight line basis over the life of the lease.

Research expenditure

All research expenditure is charged against revenue in the year it occurs.

Insurance

In line with central government policy, Highlands and Islands Enterprise and the local enterprise companies bear their own liability for all risks except for statutory obligations.

Taxation

The companies in the Network are subject to corporation tax on their annual surplus as computed for taxation purposes.

Provision is made for deferred taxation only when material liabilities are expected to arise in the foreseeable future.

Provision for corporation tax is made on gains, profits and losses, as computed for tax purposes, arising from business activities.

Pension costs

Staff are members of the Highlands and Islands Enterprise superannuation scheme or local government pension funds. The Highlands and Islands Enterprise superannuation scheme provides benefits based on final pensionable salary. The assets of the scheme are held separately from those of Highlands and Islands Enterprise and are invested with independent investment managers agreed by the scheme's trustees. The local government pension funds are defined benefit schemes, the assets of which are held in independently administered funds.

On the advice of independent qualified actuaries, contribution payments are made to the plans to ensure that the plans' assets are sufficient to cover future liabilities. Pension plan assets are measured using market values. Pension plan liabilities are measured using the projected unit method and discounted by the yield available on long-dated, high quality corporate bonds. Any increase in the present value of the liabilities of the defined benefit pension plans expected to arise from employee service in the period is charged against operating surplus. The expected return on the plans' assets and the increase during the period in the present value of the plans' liabilities arising from the passage of time are included in investment income. Actuarial gains and losses are recognised in the statement of total recognised gains and losses.

2. Income from operating activities

Income, which is shown net of Value Added Tax (VAT), is made up of receipts from various bodies as detailed below:

	Network	
	2006 £000	2005 £000
European Regional Development Fund	185	1,567
European Social Fund	57	99
Other European contributions	5,152	6,412
Scottish Executive receipts	376	77
Property income (note 9)	5,298	6,068
Other external income	5,786	2,970
	16,854	17,193

All income shown relates to continuing activities.

3. Expenditure on operating activities

Expenditure is shown net of Value Added Tax (VAT) except where the VAT is irrecoverable.

	Growing businesses £000	Making global connections £000	Developing skills £000	Strengthening communities £000	Total £000	2005 £000
Highlands and Islands Enterprise	13,425	14,839	3,552	6,447	38,263	24,047
Argyll and the Islands Enterprise	1,759	1,945	2,330	1,561	7,595	8,697
Caithness and Sutherland Enterprise	1,043	1,153	984	786	3,966	6,477
HIE Inverness and East Highland	1,061	1,172	1,169	581	3,983	4,929
Lochaber Enterprise	624	689	686	405	2,404	3,250
HIE Moray	864	955	1,779	340	3,938	10,907
Orkney Enterprise	555	614	677	339	2,185	2,447
Ross and Cromarty Enterprise	844	932	2,077	835	4,688	5,881
Shetland Enterprise	596	658	938	315	2,507	2,915
HIE Skye and Wester Ross	380	421	628	259	1,688	2,827
Western Isles Enterprise	1,029	1,137	1,230	1,046	4,442	4,744
Highlands and Islands Community Energy Company	-	-	-	1,414	1,414	-
Network	22,180	24,515	16,050	14,328	77,073	77,121
2005	16,596	30,481	16,775	13,269	77,121	

Expenditure on growing businesses and making global connections is split in the proportion of 47.50 per cent to 52.50 per cent (2005 – 35.25 per cent to 64.75 per cent). This allocation of expenditure between operating groups is an estimate based on formula share and the split of budgets across the Network that is calculated at the beginning of the financial year.

Property revaluation and management costs of £13,772,000 (2005 - £5,905,000) are included within growing businesses and making global connections expenditure above (note 9).

Under the provision of Section 2(4) of the Enterprise and New Towns (Scotland) Act 1990, Highlands and Islands Enterprise bears the cost of allowances paid to participants on youth and adult training schemes administered by local enterprise companies.

The adult training allowance is paid by the Department for Work and Pensions acting in their capacity as agents of Highlands and Islands Enterprise. The allowance is currently equivalent to an individual's benefit entitlement plus £10 per week training supplement. The total cost of adult training allowance, paid by the Employment Service on this basis for the year ended 31 March 2006, is £187,928 (2005 - £366,623) which is included in developing skills expenditure above.

4a. Administration and management charges – by organisation

	Network	
	2006 £000	2005 £000
Highlands and Islands Enterprise	15,064	13,860
Argyll and the Islands Enterprise	1,217	1,596
Caithness and Sutherland Enterprise	471	1,783
HIE Inverness and East Highland	1,301	1,146
Lochaber Enterprise	761	705
HIE Moray	1,067	969
Orkney Enterprise	609	555
Ross and Cromarty Enterprise	1,015	910
Shetland Enterprise	576	509
HIE Skye and Wester Ross	537	628
Western Isles Enterprise	1,708	2,822
Highlands and Islands Community Energy Company	203	-
Other	-	3
Network	24,529	25,486

4b. Administration and management charges

	Network		HIE	
	2006 £000	2005 £000	2006 £000	2005 £000
Staff costs (note 8)	16,396	15,530	10,052	9,602
FRS17 adjustment in respect of service costs and curtailments	40	30	45	(14)
Travel and subsistence - board members	66	65	31	28
Travel and subsistence - staff	1,317	1,096	865	707
Accommodation	2,326	1,889	1,317	1,161
Hospitality - board members	24	10	14	10
Hospitality - staff	60	73	52	44
Audit fees	192	187	129	128
Non-audit fees paid to auditors	7	7	-	-
Operating lease rentals - equipment	525	623	489	591
Depreciation of fixed assets	281	453	95	251
Equipment and furnishings	79	160	73	157
Provision for irrecoverable debts and losses	(53)	2,671	(333)	(564)
Other administration costs	3,269	2,692	2,235	1,759
	24,529	25,486	15,064	13,860

5. Notional charges

In accordance with HM Treasury paper 'Executive Non-Departmental Public Bodies: Annual Reports and Accounts Guidance' issued in March 1996, the Network is required to account for the full cost of its activities.

The following notional charge has been included in the accounts:

	Network	
	2006 £000	2005 £000
Interest charge	1,718	1,609

The notional interest charge is shown separately on the face of the income and expenditure account and the corresponding credit is shown at the bottom of the same account. The charge is calculated on the basis of 3.5 per cent (2005 – 3.5 per cent) on the average capital employed in the year.

6. Investment income

	Network	
	2006 £000	2005 £000
Dividends received	6	-
Loan interest receivable	232	181
Bank interest receivable	341	299
Surplus on disposal of investments	31	-
	610	480
Expected return on pension plan assets	3,178	2,685
Interest on pension plan liabilities	(3,756)	(3,297)
	32	(132)

7. Interest payable

	Network	
	2006 £000	2005 £000
Other	-	10
	-	10

8. Staff costs

	Network	
	2006 £000	2005 £000
Wages and salaries	13,412	12,874
Voluntary redundancy packages	-	42
Social security costs	1,004	974
Other pension costs	2,810	2,384
Staff on inward secondment	-	32
Contract/temporary staff	169	185
	17,395	16,491
Board members' remuneration	382	368
	17,777	16,859

Of the total above, £16,395,699 (2005 - £15,529,512) relates to complement staff and board members. The balance relates to project staff charged to expenditure on operating activities.

During the year ended 31 March 2006, no staff were awarded voluntary redundancy packages (2005 - 3).

The average number of employees was as follows:

	Network 2006		Network 2005	
	Complement staff	Total staff	Complement staff	Total staff
Senior management	55	59	51	57
Operational staff	321	363	310	342
Administration and support staff	135	135	143	151
	511	557	504	550

The totals include project staff who work on fixed short-term contracts in support of a number of special initiatives.

9. Commercial property

	Notes	Network	
		2006 £000	2005 £000
Income			
Rents receivable - operating leases		4,632	4,305
Profit on sales		666	1,763
	2	5,298	6,068
Expenditure			
Maintenance and factoring		2,249	2,423
Provision for bad debts		23	(58)
Revaluation adjustment - properties added during the year		11,803	3,229
Revaluation adjustment - properties held throughout the year		(433)	205
Share of operating and management costs		130	106
	3	13,772	5,905
(Deficit)/Surplus		(8,474)	163

Reconciliation of profit on sales:

	Network	
	2006 £000	2005 £000
Sales value of disposals	2,855	4,874
Net book value of disposals	2,189	3,111
Profit on sales	666	1,763

10. Taxation

	Network	
	2006 £000	2005 £000
Corporation tax	24	15
Corporation tax under-provided in previous years	-	-
Share of taxation of associated undertaking	3	33
	27	48

Corporation tax is charged at 30 per cent on the taxable surplus of Highlands and Islands Enterprise and charged at rates between 10 and 20 per cent on the taxable income of its subsidiaries.

Where liabilities for earlier years have not been finally agreed with HM Revenue and Customs, provision has been made for material estimated liabilities outstanding.

11. Tangible fixed assets

At 31 March 2006, industrial and commercial properties were valued on an open market value basis, in accordance with the guidance notes on the valuation of assets issued by the Royal Institution of Chartered Surveyors, at £36,975,425 (2005 - £38,486,320). The valuations were carried out by Graham and Sibbald, chartered surveyors.

Network

	Industrial and commercial property £000	Tenants' improvements £000	Vehicles and equipment £000	Total £000	2005 £000
Cost or market value					
At 1 April 2005	38,486	731	3,347	42,564	39,878
Additions	15,687	79	132	15,898	13,216
Disposals	(2,189)	(16)	(115)	(2,320)	(3,185)
European Regional Development Fund	(3,577)	-	-	(3,577)	(3,940)
Revaluations	(11,432)	-	-	(11,432)	(3,405)
At 31 March 2006	36,975	794	3,364	41,133	42,564
Depreciation					
At 1 April 2005	-	153	2,975	3,128	2,744
Charge for the year	-	65	216	281	453
Disposals	-	(2)	(96)	(98)	(69)
At 31 March 2006	-	216	3,095	3,311	3,128
Net book value					
At 31 March 2006	36,975	578	269	37,822	39,436
At 1 April 2005	38,486	578	372	39,436	37,134

Of the total net book value of £36,975,000 (2005 - £38,486,000) relating to industrial and commercial property as at 31 March 2006, £373,400 (2005 - £434,825) relates to leasehold sites.

HIE

	Industrial and commercial property £000	Tenants' improvements £000	Vehicles and equipment £000	Total £000	2005 £000
Cost or market value					
At 1 April 2005	38,486	255	1,143	39,884	37,495
Additions	15,687	56	-	15,743	12,845
Disposals	(2,189)	-	(28)	(2,217)	(3,111)
European Regional Development Fund	(3,577)	-	-	(3,577)	(3,940)
Revaluations	(11,432)	-	-	(11,432)	(3,405)
At 31 March 2006	36,975	311	1,115	38,401	39,884
Depreciation					
At 1 April 2005	-	46	1,013	1,059	808
Charge for the year	-	31	64	95	251
Disposals	-	-	(28)	(28)	-
At 31 March 2006	-	77	1,049	1,126	1,059
Net book value					
At 31 March 2006	36,975	234	66	37,275	38,825
At 1 April 2005	38,486	209	130	38,825	36,687

Of the total net book value of £36,975,000 (2005 - £38,486,000) relating to industrial and commercial property as at 31 March 2006, £373,400 (2005 - £434,825) relates to leasehold sites.

The deficit arising on revaluation at 31 March 2006 consisted of:

	Network		HIE	
	2006 £000	2005 £000	2006 £000	2005 £000
Deficit on properties added during the year	11,803	3,229	11,803	3,229
(Increase)/decrease in valuation of property held throughout the year	(371)	176	(371)	176
	11,432	3,405	11,432	3,405

The deficit on properties added during the year is directly affected by the level of properties under construction at the year end. The valuation of such properties is made in accordance with standard Royal Institution of Chartered Surveyors statements of asset valuation and practice, whereby each property is valued at an open market value on completion with an abatement for estimated costs to completion.

12. Investments

Network

	Shares £000	Loans £000	Total £000	2005 £000
Cost				
At 1 April 2005	9,239	5,371	14,610	9,790
Additions	1,323	1,907	3,230	6,280
Repayments	-	(848)	(848)	(506)
Disposals	(82)	-	(82)	(245)
Written off	(120)	(716)	(836)	(709)
At 31 March 2006	10,360	5,714	16,074	14,610
Diminution in value				
At 1 April 2005	5,220	4,132	9,352	7,515
Additions	643	(707)	(64)	2,724
Disposals	-	-	-	(178)
Written off	(120)	(716)	(836)	(709)
At 31 March 2006	5,743	2,709	8,452	9,352
Net book value				
At 31 March 2006	4,617	3,005	7,622	5,258
At 1 April 2005	4,019	1,239	5,258	2,275

At 31 March 2006, share investments of £4,617,000 (2005 - £4,019,000) consisted of ordinary shares of £2,210,000 (2005 - £2,007,000) and preference shares of £2,407,000 (2005 - £2,012,000).

At 31 March 2006, loan instalments due for repayment within one year amounted to £4,463,000 (2005 - £836,000).

HIE

	Shares £000	Loans £000	Total £000	2005 £000
Cost				
At 1 April 2005	601	1,193	1,794	2,108
Additions	550	875	1,425	80
Repayments	-	(185)	(185)	(197)
Disposals	(110)	-	(110)	(175)
Written off	(60)	(402)	(462)	(22)
At 31 March 2006	981	1,481	2,462	1,794
Diminution in value				
At 1 April 2005	275	816	1,091	1,688
Additions	-	(344)	(344)	(510)
Disposals	-	-	-	(65)
Written off	(60)	(402)	(462)	(22)
At 31 March 2006	215	70	285	1,091
Net book value				
At 31 March 2006	766	1,411	2,177	703
At 1 April 2005	326	377	703	420

At 31 March 2005, share investments of £766,000 (2005 - £326,000) consisted of ordinary shares of £151,000 (2005 - £151,000) and preference shares of £615,000 (2005 - £175,000).

At 31 March 2006, loan instalments due for repayment within one year amounted to £1,017,000 (2005 - £180,000).

Details of subsidiary undertakings: all held by Highlands and Islands Enterprise unless indicated.

Name of company	Country of incorporation	Holding	Proportion of voting rights and shares held	Nature of business
Argyll and the Islands Enterprise Company	Scotland	n/a	n/a	Local enterprise company
Caithness and Sutherland Enterprise Company Limited	Scotland	n/a	n/a	Local enterprise company
HIE Inverness and East Highland (formerly Inverness, Nairn, Badenoch and Strathspey Local Enterprise Company)	Scotland	n/a	n/a	Local enterprise company
Lochaber Enterprise	Scotland	n/a	n/a	Local enterprise company
HIE Moray	Scotland	n/a	n/a	Local enterprise company
Orkney Enterprise Limited	Scotland	n/a	n/a	Local enterprise company
Ross and Cromarty Enterprise Limited	Scotland	n/a	n/a	Local enterprise company
Shetland Enterprise Company Limited	Scotland	n/a	n/a	Local enterprise company
HIE Skye and Wester Ross (formerly Skye and Lochalsh Local Enterprise Company Limited)	Scotland	n/a	n/a	Local enterprise company
Western Isles Enterprise Company Limited	Scotland	n/a	n/a	Local enterprise company
Hi-Wide Limited	Scotland	n/a	n/a	Develop and deliver broadband and other online services and facilitate the development of the knowledge economy in the Highlands and Islands.
Highlands and Islands Community Energy Company Limited	Scotland	n/a	n/a	Promote community involvement in renewable energy initiatives.
PICT Innovation Limited	Scotland	n/a	n/a	Promote and commercialise information and communication technology research and development, within the Highlands and Islands area of Scotland.
Careers Trust Scotland Limited	Scotland	n/a	n/a	Enable the advancement of education and training in Scotland.

Highlands and Islands Enterprise is a joint member, along with Scottish Enterprise, of Careers Trust Scotland Limited.

The results of PICT Innovation Limited and Hi-Wide Limited are not consolidated within the accounts of the HIE network, on the basis that they are not considered significant, nor are the companies' operations integral to those of the Network.

Details of associated undertakings: all held by Highlands and Islands Enterprise unless indicated.

Name of company	Country of incorporation	Holding	Proportion of shares held	Nature of business
HIE Ventures Limited	Scotland	Ordinary shares 'A' Ordinary Shares (non voting)	30% 80%	Venture capitalist
Scottish Health Innovations Limited	Scotland	n/a	n/a	Promote research and development within the National Health Service in Scotland particularly the commercialisation of research, technology and innovations.
Scottish Intellectual Asset Management Limited	Scotland	n/a	n/a	Help build Scotland's competitiveness in a modern knowledge economy by enabling Scottish businesses to exploit their intellectual assets.
ITI Scotland Limited	Scotland	n/a	n/a	Develop strategic market opportunities within and across the areas of energy, life sciences and techmedia that represent commercial potential for existing or new companies in Scotland.

Highlands and Islands Enterprise is a joint member, along with Scottish Enterprise, of Scottish Health Innovations Limited, Scottish Intellectual Asset Management Limited and ITI Scotland Limited.

The results of Scottish Health Innovations Limited and Scottish Intellectual Asset Management Limited are included in the HIE network accounts. The results of ITI Scotland Limited are not consolidated within the accounts of the HIE network on the basis that, although HIE is a joint member, they are consolidated in full in the accounts of Scottish Enterprise.

Details of investments in companies in which the Network's total investment in shares and loans:

(a) equals 20 per cent, or more than 20 per cent, of the voting rights and exceeds £100,000 or;

(b) the total investment exceeds £1,000,000:

Name of company – activity	% of voting rights	Holding as at 31 March 2006	Shares value paid £000	Loan outstanding £000	Outstanding commitment £000
HIE Ventures Limited - venture capitalist	30%	60,000 ordinary shares	60	*	-
	-	40,000 'A' non voting ordinary shares	40	-	-
Aviemore Highland Resort Limited – provider of accommodation in Aviemore	-	1,000,000 preference shares	1,000	-	-
	-	1,400,000 preferred ordinary shares	1,400	-	-
					950
Camcal Limited – steel fabricator	13.3%	7,161 'A' ordinary shares	48	-	-
	-	1,551,664 'A' preference shares	1,552	-	-
	-	44,996 'B' preference shares	-	-	-
	-	440,000 'C' preference shares	440	-	1,064
Investment in 59 other businesses			5,820	5,714	
			10,360	5,714	

*Loans of £1,000,000 netted off by ERDF received.

The outstanding commitment in respect of Aviemore Highland Resort Limited relates to grants of £950,000.

The outstanding commitment in respect of Camcal Limited relates to shares of £559,400 and grants of £504,600.

13. Stocks

Stocks comprise sheep and animal feedstuffs which are held on Orbost Estate.

14. Debtors

	Network		HIE	
	2006 £000	2005 £000	2006 £000	2005 £000
Assets and investments held by local enterprise companies (see below)	-	-	6,092	5,746
Other debtors	8,587	6,659	8,151	6,288
Provision for bad debts	(753)	(1,159)	(747)	(1,144)
	7,834	5,500	7,404	5,144
Taxation recoverable	1,116	776	1,007	937
Accrued income and prepayments	1,108	689	712	585
Owed by subsidiary undertakings	-	-	3,479	1,628
	10,058	6,965	18,694	14,040

Local enterprise companies purchase, in their own name, tangible fixed assets and investments with funds provided under the operating contract with Highlands and Islands Enterprise. Under the terms of the operating contract their value falls to be repaid to Highlands and Islands Enterprise on the disposal of such assets and investments. The sums due from these assets are attributable to the following:

	Network	
	2006 £000	2005 £000
Investments	5,545	5,135
Equipment	202	241
Tenants' improvements	345	370
	6,092	5,746

15. Cash at bank and in hand

	Network		HIE	
	2006 £000	2005 £000	2006 £000	2005 £000
Network and HIE funds	1,383	2,150	128	936
Other scheme funds held	1,081	951	1,081	951
	2,464	3,101	1,209	1,887

The balance sheet includes funds held by Highlands and Islands Enterprise relating to the following schemes:

	Network		HIE	
	2006 £000	2005 £000	2006 £000	2005 £000
SME	9	9	9	9
Scottish Land Fund	212	106	212	106
CED	572	538	572	538
LEADER +	288	298	288	298
	1,081	951	1,081	951

Highlands and Islands Enterprise has been appointed by the Scottish Executive to act as the implementing authority for the SME scheme in the Highlands and Islands.

Highlands and Islands Enterprise has been contracted by The Big Lottery Fund to promote and administer the Scottish Land Fund in Scotland.

The HIE network is an applicant under the Community Economic Development (CED) and LEADER + schemes. The balance on these accounts represents advances from the Scottish Executive.

16. Creditors: amounts falling due within one year

	Network		HIE	
	2006 £000	2005 £000	2006 £000	2005 £000
Other creditors	6,164	4,325	5,744	3,550
Accruals	1,479	1,328	763	795
Corporation tax	24	14	-	-
Prepaid rental income	466	389	466	388
Owed to subsidiary undertakings	-	-	4,754	3,594
	8,133	6,056	11,727	8,327

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

	Network		HIE	
	2006 £000	2005 £000	2006 £000	2005 £000
Deferred income - other schemes	1,081	951	1,081	951
	1,081	951	1,081	951

18. Pension schemes

Staff are members of the Highlands and Islands Enterprise superannuation scheme or local government pension funds. The Highlands and Islands Enterprise superannuation scheme provides benefits based on final pensionable salary. The assets of the scheme are held separately from those of Highlands and Islands Enterprise and are invested with independent investment managers agreed by the scheme's trustees. The local government pension funds are defined benefit schemes, the assets of which are held in independently administered funds.

Contributions are made to the following local government pension funds by the HIE network:

- Highland Council Pension Fund
- Orkney Islands Council Pension Fund
- Shetland Islands Council Pension Fund
- Strathclyde Pension Fund

Pension disclosure under FRS17

Highlands and Islands Enterprise superannuation scheme

Highlands and Islands Enterprise operates a defined benefit scheme in the UK. A full actuarial valuation was carried out at 5 April 2003 and updated to 31 March 2006 by a qualified independent actuary.

The service cost has been calculated using the projected unit method.

The major assumptions used by the actuary were (in nominal terms):

	31 March 2006	31 March 2005	31 March 2004	31 March 2003
Rate of salary increases (% per annum)	4.90	4.90	4.90	4.60
Rate of pension increase (% per annum)	2.90	2.90	2.90	2.60
Discount rate (% per annum)	5.80	5.40	5.50	5.40
Inflation rate (% per annum)	2.90	2.90	2.90	2.60

During the year, Highlands and Islands Enterprise paid contributions equivalent to 20.4 per cent of pensionable salaries. The company has agreed to maintain this level of contributions, although this rate is subject to review.

The assets in the scheme and expected rate of return were:

	Long-term rate of return expected at 31 March 2006 %	Value at 31 March 2006 £000	Long-term rate of return expected at 31 March 2005 %	Value at 31 March 2005 £000	Long-term rate of return expected at 31 March 2004 %	Value at 31 March 2004 £000	Long-term rate of return expected at 31 March 2003 %	Value at 31 March 2003 £000
Equities	6.50	34,542	6.90	27,280	6.90	23,576	6.50	17,998
Gilts/corporate bonds	3.70	14,359	4.10	11,435	4.10	10,664	3.75	8,882
Cash	3.70	408	3.95	430	3.15	450	2.75	211
Total market value of assets		49,309		39,145		34,690		27,091
Actuarial value of liability		(53,122)		(52,909)		(48,317)		(42,921)
Deficit in the scheme		(3,813)		(13,764)		(13,627)		(15,830)
Related deferred tax asset/ (liability)		-		-		-		-
Net pension liability		(3,813)		(13,764)		(13,627)		(15,830)

The actuarial valuation at 31 March 2006 showed a decrease in the deficit to £3,813m from £13.764m at 31 March 2005.

Local government pension funds

The valuation for the local government pension funds used for FRS 17 disclosures has been based on the most recent actuarial valuations at 31 March 2002 and updated by a qualified actuary to take account of the requirements of FRS 17 in order to assess the liabilities of the funds at 31 March 2006. Fund assets are stated at their market value at 31 March 2006:

	31 March 2006	31 March 2005	31 March 2004	31 March 2003
Main assumptions:				
Rate of salary increases (% per annum)	4.60	4.40	4.40	4.00
Rate of pension increase (% per annum)	3.10	2.90	2.90	2.50
Discount rate (% per annum)	6.00	5.40	5.50	5.40
Inflation rate (% per annum)	3.10	2.90	2.90	2.50

The share of the assets in the funds and the expected rate of return were:

	Long-term rate of return expected at 31 March 2006 %	Value at 31 March 2006 £000	Long-term rate of return expected at 31 March 2005 %	Value at 31 March 2005 £000	Long-term rate of return expected at 31 March 2004 %	Value at 31 March 2004 £000	Long-term rate of return expected at 31 March 2003 %	Value at 31 March 2003 £000
Equities	7.40	10,224	7.70	6,960	7.70	5,927	8.00	4,400
Bonds	4.90	2,091	4.80	1,649	5.10	1,445	4.80	1,031
Property	5.50	1,299	5.70	757	6.50	358	6.00	203
Cash	4.60	330	4.80	244	4.00	219	4.00	217
Estimated employer assets		13,944		9,610		7,949		5,851
Present value of scheme liabilities		(15,343)		(12,403)		(10,786)		(8,792)
Present value of unfunded liabilities		(97)		(88)		(93)		-
Deficit in the scheme		(1,496)		(2,881)		(2,930)		(2,941)
Related deferred tax liability		-		-		-		-
Net pension liability		(1,496)		(2,881)		(2,930)		(2,941)

The pension contributions with effect from 1 April 2006 for the local government pension funds are:

	2006	2005
Highland Council Pension Fund - LECs	16.2%	14.7%
Highland Council - Careers Scotland	16.8%	15.0%
Orkney Islands Council Pension Fund	17.7%	17.7%
Shetland Islands Council Pension Fund	17.0%	16.8%
Strathclyde Pension Fund	15.6%	15.0%

Network

	HIE superannuation scheme 2006 £000	LGPF 2006 £000	Total 2006 £000	HIE superannuation scheme 2005 £000	LGPF 2005 £000	Total 2005 £000
Analysis of the amount charged to operating profit						
Current service cost	2,033	529	2,562	1,745	544	2,289
Contributions	(2,204)	(470)	(2,674)	(1,786)	(469)	(2,255)
Past service cost	-	-	-	-	-	-
Contributions in respect of unfunded benefits	-	(16)	(16)	-	(4)	(4)
Curtailments and settlements	-	168	168	-	-	-
Total operating charge	(171)	211	40	(41)	71	30
Analysis of net return on pension scheme						
Expected return on pension scheme assets	2,404	774	3,178	2,103	582	2,685
Interest on pension scheme liabilities	(2,885)	(871)	(3,756)	(2,679)	(618)	(3,297)
Net return	(481)	(97)	(578)	(576)	(36)	(612)
Analysis of amount recognised in statement of total recognised gains and losses						
Actual return less expected return on scheme assets	6,544	1,978	8,522	1,521	465	1,986
Experience gains and losses on scheme liabilities	(150)	1,306	1,156	(138)	4	(134)
Changes in assumptions underlying the present value of scheme liabilities	3,867	(1,591)	2,276	(985)	(313)	(1,298)
Actuarial gain/(loss) recognised in statement of total recognised gains and losses	10,261	1,693	11,954	398	156	554
Movement in surplus during the year						
Deficit in scheme at beginning of year	(13,764)	(2,881)	(16,645)	(13,627)	(2,930)	(16,557)
Movement in year:						
Current service cost	(2,033)	(529)	(2,562)	(1,745)	(544)	(2,289)
Contributions	2,204	470	2,674	1,786	469	2,255
Past service costs	-	16	16	-	-	-
Curtailments and settlements	-	(168)	(168)	-	4	4
Net return on assets/(interest cost)	(481)	(97)	(578)	(576)	(36)	(612)
Actuarial gain/(loss)	10,261	1,693	11,954	398	156	554
Deficit in scheme at end of year	(3,813)	(1,496)	(5,309)	(13,764)	(2,881)	(16,645)

	HIE superannuation scheme 2006 £000	Careers Scotland LGPF 2006 £000	Total 2006 £000	HIE superannuation scheme 2005 £000	Careers Scotland LGPF 2005 £000	Total 2005 £000																																																																																																													
Analysis of the amount charged to operating profit																																																																																																																			
Current service cost	2,033	271	2,304	1,745	249	1,994																																																																																																													
Contributions	(2,204)	(211)	(2,415)	(1,786)	(222)	(2,008)																																																																																																													
Past service cost	-	-	-	-	-	-																																																																																																													
Contributions in respect of unfunded benefits	-	(12)	(12)	-	-	-																																																																																																													
Curtailments and settlements	-	168	168	-	-	-																																																																																																													
Total operating charge	(171)	216	45	(41)	27	(14)																																																																																																													
Analysis of net return on pension scheme																																																																																																																			
Expected return on pension scheme assets	2,404	425	2,829	2,103	254	2,357																																																																																																													
Interest on pension scheme liabilities	(2,885)	(410)	(3,295)	(2,679)	(271)	(2,950)																																																																																																													
Net return	(481)	15	(466)	(576)	(17)	(593)																																																																																																													
Analysis of amount recognised in statement of total recognised gains and losses																																																																																																																			
Actual return less expected return on scheme assets	6,544	1,090	7,634	1,521	225	1,746																																																																																																													
Experience gains and losses on scheme liabilities	(150)	128	(22)	(138)	1	(137)																																																																																																													
Changes in assumptions underlying the present value of scheme liabilities	3,867	(1,259)	2,608	(985)	(134)	(1,119)																																																																																																													
Actuarial gain recognised in statement of total recognised gains and losses	10,261	(41)	10,220	398	92	490																																																																																																													
Movement in surplus during the year																																																																																																																			
Deficit in scheme at beginning of year	(13,764)	(1,254)	(15,018)	(13,627)	(1,302)	(14,929)																																																																																																													
Movement in year:																																																																																																																			
Current service cost	(2,033)	(271)	(2,304)	(1,745)	(249)	(1,994)																																																																																																													
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Curtailments and settlements	-	(168)	(168)	-	-	-																																																																																																													
Net return on assets/(interest cost)	(481)	15	(466)	(576)	(17)	(593)																																																																																																													
Actuarial gain/(loss)	10,261	(41)	10,220	398	92	490																																																																																																													
Deficit in scheme at end of year	(3,813)	(1,496)	(5,309)	(13,764)	(1,254)	(15,018)																																																																																																													
<table border="1"> <thead> <tr> <th></th> <th colspan="4">HIE superannuation scheme</th> <th colspan="4">Local government pension funds</th> </tr> <tr> <th></th> <th>2006 £000</th> <th>2005 £000</th> <th>2004 £000</th> <th>2003 £000</th> <th>2006 £000</th> <th>2005 £000</th> <th>2004 £000</th> <th>2003 £000</th> </tr> </thead> <tbody> <tr> <td colspan="9">History of experience gains and losses</td> </tr> <tr> <td>Difference between expected and actual return on scheme assets</td> <td>6,544</td> <td>1,521</td> <td>4,436</td> <td>(8,593)</td> <td>1,978</td> <td>465</td> <td>1,033</td> <td>(2,082)</td> </tr> <tr> <td>Value of assets</td> <td>49,309</td> <td>39,145</td> <td>34,690</td> <td>27,091</td> <td>13,944</td> <td>9,610</td> <td>7,949</td> <td>5,851</td> </tr> <tr> <td>Percentage of scheme assets</td> <td>13.0</td> <td>3.9</td> <td>12.8</td> <td>-31.7</td> <td>14.2</td> <td>4.8</td> <td>13.0</td> <td>-35.6</td> </tr> <tr> <td>Experience gains and losses on scheme liabilities</td> <td>(150)</td> <td>(138)</td> <td>983</td> <td>(217)</td> <td>1,409</td> <td>4</td> <td>(12)</td> <td>(162)</td> </tr> <tr> <td>Present value of liabilities</td> <td>53,122</td> <td>52,909</td> <td>48,317</td> <td>42,921</td> <td>15,410</td> <td>12,491</td> <td>10,879</td> <td>8,792</td> </tr> <tr> <td>Percentage of scheme liabilities</td> <td>-</td> <td>-0.3</td> <td>2.0</td> <td>-0.5</td> <td>9.1</td> <td>-</td> <td>-0.1</td> <td>-1.8</td> </tr> <tr> <td>Total amount recognised in statement of total recognised gains and losses</td> <td>10,261</td> <td>398</td> <td>2,661</td> <td>(12,023)</td> <td>1,693</td> <td>156</td> <td>220</td> <td>(2,658)</td> </tr> <tr> <td>Present value of liabilities</td> <td>53,122</td> <td>52,909</td> <td>48,317</td> <td>42,921</td> <td>15,440</td> <td>12,491</td> <td>10,879</td> <td>8,792</td> </tr> <tr> <td>Percentage of scheme liabilities</td> <td>19.0</td> <td>0.8</td> <td>5.5</td> <td>-28.0</td> <td>11.0</td> <td>1.2</td> <td>2.0</td> <td>-30.2</td> </tr> </tbody> </table>									HIE superannuation scheme				Local government pension funds					2006 £000	2005 £000	2004 £000	2003 £000	2006 £000	2005 £000	2004 £000	2003 £000	History of experience gains and losses									Difference between expected and actual return on scheme assets	6,544	1,521	4,436	(8,593)	1,978	465	1,033	(2,082)	Value of assets	49,309	39,145	34,690	27,091	13,944	9,610	7,949	5,851	Percentage of scheme assets	13.0	3.9	12.8	-31.7	14.2	4.8	13.0	-35.6	Experience gains and losses on scheme liabilities	(150)	(138)	983	(217)	1,409	4	(12)	(162)	Present value of liabilities	53,122	52,909	48,317	42,921	15,410	12,491	10,879	8,792	Percentage of scheme liabilities	-	-0.3	2.0	-0.5	9.1	-	-0.1	-1.8	Total amount recognised in statement of total recognised gains and losses	10,261	398	2,661	(12,023)	1,693	156	220	(2,658)	Present value of liabilities	53,122	52,909	48,317	42,921	15,440	12,491	10,879	8,792	Percentage of scheme liabilities	19.0	0.8	5.5	-28.0	11.0	1.2	2.0	-30.2
	HIE superannuation scheme				Local government pension funds																																																																																																														
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19. Provisions for loss

Network

	Investments £000	Loan capital £000	Revenue debts £000	Total £000	2005 £000
At 1 April 2005	5,220	4,132	1,159	10,511	8,854
Written off	(120)	(716)	(440)	(1,276)	(956)
	5,100	3,416	719	9,235	7,898
Provisions for year:					
General	643	(707)	11	(53)	2,671
Commercial property	-	-	23	23	(58)
At 31 March 2006	5,743	2,709	753	9,205	10,511

HIE

	Investments £000	Loan capital £000	Revenue debts £000	Total £000	2005 £000
At 1 April 2005	275	816	1,143	2,234	3,001
Written off	(60)	(402)	(430)	(892)	(145)
	215	414	713	1,342	2,856
Provisions for year:					
General	-	(344)	11	(333)	(564)
Commercial property	-	-	23	23	(58)
At 31 March 2006	215	70	747	1,032	2,234

20. Losses statement

	NETWORK		HIE	
	No of cases	£000	No of cases	£000
Claims waived (amounts written off) during the year ended 31 March 2006	46	1,579	26	1,022

These write-offs relate to Scottish Executive approved balances and Highlands and Islands Enterprise delegated authority.

Detail of individual cases exceeding £100,000:

Lewis Offshore Limited	£606,344
Sargasso Limited	£120,391
Eolas Media Limited	£174,986
Heather Isle Meats Limited	£138,334

The Highlands and Islands Enterprise network continues to pursue all outstanding debts.

21. Reserves

Network

	Revaluation reserve £000	Other reserve £000	Pension reserve £000	General reserve £000	Total £000
At 1 April 2005	219	320	(16,645)	48,233	32,127
Grant-in-aid received during the year	-	-	-	85,020	85,020
	219	320	(16,645)	133,253	117,147
Transfer from income and expenditure account	-	-	(618)	(84,314)	(84,932)
Actuarial gain	-	-	11,954	-	11,954
Other movements	(62)	80	-	(80)	(62)
At 31 March 2006	157	400	(5,309)	48,859	44,107

Since the incorporation of Highlands and Islands Enterprise in 1991, the accumulated figure of financing provided by way of grant-in-aid totals £1,038.2 million. During the year ended 31 March 2006, the HIE network offset £3 million of grant-in-aid in lieu of a payment made by the Scottish Executive on the Network's behalf.

HIE

	Revaluation reserve £000	Other reserve £000	Pension reserve £000	General reserve £000	Total £000
At 1 April 2005	219	-	(15,018)	45,958	31,159
Grant-in-aid received during the year	-	-	-	85,020	85,020
	219	-	(15,018)	130,978	116,179
Transfer from income and expenditure account	-	-	(511)	(84,588)	(85,099)
Actuarial gain	-	-	10,220	-	10,220
Other movements	(62)	-	-	-	(62)
At 31 March 2006	157	-	(5,309)	46,390	41,238

22. Net cash flow from operating activities

	Network	
	2006 £000	2005 £000
Excess of expenditure over income on operating activities	(84,748)	(85,414)
FRS 17 pension adjustments	40	30
	(84,708)	(85,384)
Adjustment for items not involving movement of cash:		
(Decrease)/increase in debtors	(2,384)	555
Increase in creditors	2,357	1,619
Decrease in stocks	-	23
Depreciation	281	453
Provisions and write-offs	(470)	2,544
Profits on disposal of fixed assets	(662)	(1,761)
Revaluation of property	11,370	3,434
Net cash outflow from operating activities	(74,216)	(78,517)

23. Analysis of cash flows for headings in the cash flow statement

	2006 £000	2005 £000
Returns on investments and servicing of finance		
Interest received	869	449
Dividends received	89	-
Interest paid	-	(10)
Net cash flow from returns on investments and servicing of finance	958	439
Taxation		
Corporation tax paid	(14)	(9)
	(14)	(9)
Capital expenditure and financial investment		
Loans advanced	(1,907)	(1,200)
Loans repaid	848	506
Payments to acquire shares	(1,323)	(5,080)
Receipts from the disposal of shares	193	147
Payments for the construction of property	(15,950)	(13,221)
Payments to acquire vehicles, equipment and tenants' improvements	(238)	(510)
Receipts from the disposal of tangible fixed assets	2,884	4,877
Net cash flow from capital expenditure and financial investment	(15,493)	(14,481)
Financing		
Deferred income movement	130	(1,314)
Grant-in-aid received	85,020	90,248
European Regional Development Fund	2,978	4,120
Net cash flow from financing	88,128	93,054

24. Analysis of net funds

Network

	At 31 March 2005 £000	Cash flow £000	Other changes £000	At 31 March 2006 £000
Cash at bank and in hand	3,101	(637)	-	2,464
	3,101	(637)	-	2,464

25. Commitments and contingent liabilities

	Network		HIE	
	2006 £000	2005 £000	2006 £000	2005 £000
Commitments				
Local enterprise companies	-	-	See note (1) below	See note (1) below
Property	20,145	7,462	20,145	7,462
Grants and loans	48,327	34,338	15,436	9,398

(1) Contracts with all nine (2005-2006 - ten) local enterprise companies were renewed. The budgets offered for 2006-2007 totalled £55.20m (2005-2006 - £62.60m). Payments in respect of these budgets will be made partly by Highlands and Islands Enterprise on behalf of the local enterprise companies.

(2) Commitments to capital and business investment projects often extend over more than one financial year. Major projects and initiatives are undertaken by Highlands and Islands Enterprise with the support of Scottish Ministers.

(3) As noted in the financial commentary of the management commentary, a potential contingent liability remains unresolved in relation to the European audit on the Highlands and Islands Objective One programme. The HIE network has responded in full to all requests for further information and supporting documentation. The EU report has still to be finalised.

26. Financial commitments

Payments due under non-cancellable operating leases:

Network	Property £000	Equipment £000	Total £000	2005 £000
Operating and similar leases which expire:				
Within one year	110	574	684	735
Within two to five years	184	134	318	95
In over five years	1,813	66	1,879	1,543
	2,107	774	2,881	2,373
<hr/>				
HIE	Property £000	Equipment £000	Total £000	2005 £000
Operating and similar leases which expire:				
Within one year	76	567	643	717
Within two to five years	29	122	151	38
In over five years	1,600	66	1,666	1,205
	1,705	755	2,460	1,960

27. Transactions involving board members' registered interests

During the year the following transactions were made by the Highlands and Islands Enterprise network with businesses in which Highlands and Islands Enterprise board members had an interest:

Business	Approvals brought forward (£)	Amount approved/ (withdrawn) in year (£)	Amount paid in year (£)	Nature of transaction	Board member and interest
Mysterian Ltd	88,000	(88,000)	-	Development grant	W Roe – Director, Mysterian Ltd (resigned 2 September 2004)
Rocket Science UK Ltd	12	53,967	53,979	Fees	W Roe – Director, Rocket Science UK Ltd
Western Isles Sea Fisheries Training Association	32,948	(12,742)	20,206	Project grants	Duncan MacInnes – Secretary, Western Isles Sea Fisheries Training Association
Gael Force Marine Equipment Ltd	16,250	(16,250)	-	Development grant	Stewart Graham – Director, Gael Force Marine Equipment Ltd
Spoff (Scotland) Ltd	4,317	-	-	Business Learning Account	Angus Mackenzie – Joint Managing Director, Spoff (Scotland) Ltd
Spoff (Scotland) Ltd	-	822	822	Project grant	Angus Mackenzie – Joint Managing Director, Spoff (Scotland) Ltd
BSW Sawmills Ltd	-	3,000,000	-	Development grants	Andrew Rogers – Mill Manager, BSW Sawmills
BSW Sawmills Ltd	-	80,000	49,340	Development grants	Andrew Rogers – Mill Manager, BSW Sawmills
BSW Sawmills Ltd	-	26,375	20,186	Project grant	Andrew Rogers – Mill Manager, BSW Sawmills
BSW Sawmills Ltd	-	457	457	Training grants	Andrew Rogers – Mill Manager, BSW Sawmills
Calman Housing Trust Association	-	2,625	2,625	Training grants	George Campbell – Chairman, Calman Housing Trust Association
Highland Housing Alliance	-	75,000	33,175	Project grant	Susan Torrance – Chief Executive, Highland Housing Alliance
Western Isles Fishermen's Association	12,000	11,000	16,386	Project grants	Duncan MacInnes – Secretary, Western Isles Fishermen's Association

Transactions also took place with the following bodies from which HIE board members received a remuneration:

Name of body	Board member and interest
Royal Society for the Protection of Birds	G Campbell, Regional Director (North Scotland)
Crofters Commission	D Ratter, Commissioner
Shetland Islands Council	D Ratter, Member

Organisations which received funding in the year and in which the board members, key managerial staff or other related parties had a non-financial interest include:

Argyll College	Nevis Range Development Company
Black Isle Farmers Society	Nevisprint Limited
Commun na Gaidhlig	Quality Scotland
Eden Court Theatre	Shetland College
The European Marine Energy Centre Limited	The Highland Council
Fusion Scotland	Tulloch Construction Group
Highlands and Islands (Scotland) Structural Funds Partnership Ltd	UHI Millennium Institute

28. Related party transactions

Highlands and Islands Enterprise is a non-departmental public body sponsored by the Scottish Executive.

The Scottish Executive is regarded as a related party. During the year, Highlands and Islands Enterprise has had various material transactions with the Scottish Executive and with other entities for which the Scottish Executive is regarded as the parent body.

In addition, Highlands and Islands Enterprise has had a small number of material transactions with other Government departments, central government bodies, local government, non-departmental public bodies and similar organisations.

Material transactions have taken place with:

Aberdeenshire Council	The Moray Council
Argyll and Bute Council	Orkney Islands Council
Caledonian MacBrayne	Scottish Enterprise
Communities Scotland	Scottish Natural Heritage
Comhairle nan Eilean Siar	Shetland Islands Council
Crofters Commission	Scottish University for Industry
Forestry Commission	UHI Millennium Institute
Highlands and Islands Airports Limited	Visit Scotland
The Highland Council	

None of the board members, key managerial staff or other related parties have undertaken any material transactions with Highlands and Islands Enterprise other than those disclosed in note 28.

29. Rural Petrol Stations Grant Scheme

The HIE network is involved in providing assistance under the Rural Petrol Stations Grant Scheme. Transactions relating to this scheme are as follows:

Network	2006 £000	2005 £000
Funds brought forward at 1 April 2005	159	236
Funds received in the year	238	-
Monies paid out in the year	(376)	(77)
Funds carried forward at 31 March 2006	21	159

Direction by the Scottish Ministers to Highlands and Islands Enterprise: accounts direction

1. The Scottish Ministers, in pursuance of section 30(1) of the Enterprise and New Towns (Scotland) Act 1990, hereby give the following direction.

2. The statement of accounts for the financial year ended 31 March 2006, and subsequent years, shall comply with the accounting principles and disclosure requirements of the edition of the Government Financial Reporting Manual (FReM) which is in force for the year for which the statement of accounts are prepared.

3. The accounts shall be prepared so as to give a true and fair view of the income and expenditure and cash flows for the financial year, and of the state of affairs as at the end of the financial year.

4. Clarification of the application of the accounting and disclosure requirements of the Companies Act and accounting standards is given in Schedule 1 attached. Additional disclosure requirements are set out in Schedule 2 attached.

5. The income and expenditure account and balance sheet shall be prepared under the historical cost convention modified by the inclusion of:

5.1 fixed assets at their value to the business by reference to current costs; and

5.2 stocks valued at the lower of net current replacement cost (or historical cost if this is not materially different) and net realisable value.

6. This direction shall be reproduced as an appendix to the statement of accounts. The direction given on 18th June 2002 is hereby revoked.

Jane Morgan

Signed by the authority of the
Scottish Ministers

Dated 14 December 2005

Schedule 1

Application of the accounting and disclosure requirements of the Companies Act and accounting standards

Companies Act

1. The disclosure exemptions permitted by the Companies Act shall not apply with the exception of section 230 of the Companies Act 1985.
2. The operating and financial review shall contain a schedule analysing and summarising the cash outturn by Scottish Executive funding block.
3. Highlands and Islands Enterprise is not required to provide the additional information required by paragraph 33(3) of Schedule 4 to the Companies Act, nor to comply fully with the disclosure requirements re investments of section 231 of the Companies Act 1985 (specifically those specified in Schedule 5, Part 11, paragraphs 23 to 28).

Accounting policies

4 The accounting policies adopted by Highlands and Islands Enterprise shall include the following:

4.1 Grant-in-aid received by Highlands and Islands Enterprise shall be credited to a general reserve on the basis that grant-in-aid cannot be allocated between revenue and capital expenditure as disclosed in the accounts.

4.2 Land and buildings held for industrial or commercial use shall be accounted for in accordance with the principles of Statement of Standard Accounting Practice 19, 'Accounting for Investment Properties', being included in the balance sheet at open market value on the basis of annual revaluations, which should be conducted by an independent firm of professional valuers at least every five years.

Schedule 2

Additional disclosure requirements

1. The notes to the accounts shall include:

1.1 Disclosure of the income, expenditure, and net surplus or deficit of commercial property activities;

1.2 An analysis of other income;

1.3 An analysis of operating costs, including training allowances costs, in categories consistent with 'A Smart Successful Scotland';

1.4 An analysis of management costs;

1.5 An analysis of bad and doubtful debts and miscellaneous losses;

1.6 The accumulated figure of financing provided by grant-in-aid since the incorporation of Highlands and Islands Enterprise;

1.7 Details of the property valuation in appropriate categories together with the revaluation adjustment required to bring the original cost to market value. The basis of the valuation should be clearly stated and any comments, including those of the valuers, on the basis and limitations of the valuation which will assist the reader of the accounts in assessing the value of the portfolios should be provided;

1.8 An analysis of property related items in the income and expenditure account to show surpluses/deficits on sales of property by reference to the net book amount at the beginning of the year of sale; adjustments in respect of land purchased or held and property developments contracted or in progress during the year; and adjustments in respect of changes in the value of investment property held throughout the year;

1.9 An analysis of the movements on all reserves;

1.10 The insurance arrangements of the Highlands and Islands Enterprise network;

1.11 An analysis of expenditure on travel and subsistence and entertaining, separately disclosing expenditure in respect of board members and staff;

1.12 The average, full-time equivalent number of employees, whether permanent or temporary, employed in the Highlands and Islands Enterprise network, analysed in appropriate categories to disclose at least the following:

- Senior management (that is, the holders of those posts identified in paragraph 2.7.8 of the Management Statement of Highlands and Islands Enterprise);
- Operations;
- Administration and support functions;

1.13 The total sum paid to each local enterprise company analysed by strategic theme (alternatively, this disclosure may be provided in the Operating Financial Review);

1.14 The guarantees and contingent liabilities provided by the Highlands and Islands Enterprise network in the following categories:

- Joint ventures or property investments underwritten;
- Liability arising from legal action;
- Guaranteed loan and bank overdrafts of companies in which the Highlands and Islands Enterprise network has invested;
- Guarantees to banks in respect of property sales;
- Any other guarantees or liabilities;

1.15 A schedule of all investments showing:

I) In respect of companies in which the Highlands and Islands Enterprise network holds 20 per cent or more than 20 per cent of the voting rights and where the total investment (including loans) is in excess of £100,000:

- Name of company;
- Nature of its business;
- Percentage of voting rights held;
- Amount invested in shares (distinguishing between ordinary and preference shares);
- Amount of loan given to each company;
- Any other commitments in respect of each company;

II) In respect of companies in which Highlands and Islands Enterprise Network holds less than 20 per cent of the voting rights but where the total investment (including loans) is in excess of £1,000,000:

- Name of company;
- Nature of its business;
- Percentage of voting rights held;
- Amount invested in shares (distinguishing between ordinary and preference shares);
- Amount of loan given to each company;
- Any other commitments in respect of each company;

III) In respect of all other investments by the Highlands and Islands Enterprise network:

- Total number of companies involved;
- Total amount invested;
- Total amount of loans given;
- Total amount of any other commitments.