HIGHLANDS AND ISLANDS AIRPORTS LIMITED

ANNUAL REPORT AND GROUP ACCOUNTS

2005/2006

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DIRECTORS

Alex Matheson OBE, Chairman

Inglis E Lyon, Managing Director

Grenville S Johnston OBE TD JP CA

Shona C MacLennan

Charles Alexander Goodlad

Linn Phipps

COMPANY SECRETARY

Jane Thornton CA

REGISTERED OFFICE

Inverness Airport
Inverness
IV2 7JB

Registered in Scotland Number 97647

AUDITORS

Ernst and Young LLP
Barony House
Stoneyfield Business Park
Stoneyfield
Inverness
IV2 7PA

COMPANY OPERATING LOSS AND CAPITAL EXPENDITURE BY AIRPORT

2005/2006

AIRPORTS	Traffic Operations and Other Income	Revenue Operating Costs	Operating (Loss) before Subsidies	Capital Expenditure	Operating (Loss) before Subsidies plus Capital Expenditure per Airport
	£000	£000	£000	£000	£000
BARRA	162	(695)	(533)	(1)	(534)
BENBECULA	526	(2,094)	(1,568)	(234)	(1,802)
CAMPBELTOWN	262	(958)	(696)	(6)	(702)
INVERNESS	5,226	(8,375)	(3,149)	(39,785)	(42,934)
ISLAY	330	(1,109)	(779)	(11)	(790)
KIRKWALL	1,210	(3,370)	(2,160)	(185)	(2,345)
STORNOWAY	1,493	(3,269)	(1,776)	(28)	(1,804)
SUMBURGH	1,894	(5,320)	(3,426)	(6,726)	(10,152)
TIREE	138	(753)	(615)		(615)
WICK	525	(2,733)	(2,208)	(180)	(2,388)
	11,766	(28,676)	(16,910)	(47,156)	(64,066)
WORKING CAPITAL MOVEMENT					2,978
DEPRECIATION					384
TOTAL SUBSIDIES RECEIVABLE					60,704

DIRECTORS' REPORT

The Directors submit their Report and the Group Accounts for the year ended 31 March 2006

RESULTS AND DIVIDENDS

The trading loss for the period, after taking account of taxation, amounted to £969,000 The directors recommend that no dividend be paid, leaving the full amount to be set against reserves

PRINCIPAL ACTIVITY

The group's principal activity is to operate airports safely and efficiently through best business practice so that they contribute to the economic and social wellbeing of the Highlands and Islands

REVIEW OF THE BUSINESS AND FUTURE DEVELOPMENTS

Subsidies from the Scottish Ministers received for the year ended 31 March 2006 totalled £58,902,000 made up of revenue subsidy of £14,747,000 and capital subsidy of £44,155,000 The capital subsidy figure includes £28,333,000 which was used to purchase the entire share capital of Inverness Air Terminal Limited on 20 January 2006 and £6,624,000 which was used to repay a long term loan that existed at that date To improve efficiency of operations, the Directors propose to restructure the group so that the trade, assets and liabilities (excluding inter company loans) of Inverness Air Terminal Limited are hived up into Highlands and Islands Airports Limited This transfer agreement is likely to be signed early in the new financial year

Passenger numbers, freight tonnage and aircraft movements increased by 14%, 3% and 13% respectively in the year

CAPITAL EXPENDITURE

Investment in new fixed assets amounted to £9,560,000 Expenditure was incurred on major items as follows

a) At Benbecula, work commenced on an improvement to the terminal building to meet increased security and operational requirements at a cost of £217,000

b) At Inverness, environmental measures continued at a cost of £806,000 to satisfy water quality standards imposed by SEPA A project to extend the South Apron to facilitate continued growth commenced during the year at a cost of £1,271,000

c) At Sumburgh, the 09/27 runway extension project continued with works costing £6,643,000
This project has been developed by the Sumburgh Airport Strategic Partnership, which comprises Shetland Islands Council, Shetland Enterprise, Sumburgh Airport Consultative Committee and Highlands and Islands Airports Limited The project attracted the following levels of funding during the year, £2,500,000 from the Scottish Executive, £1,548,000 from the European Regional Development Fund and £48,000 from Shetland Islands Council

d) At Wick, improvements to the terminal building required to meet increased security and operational requirements were completed at a cost of £161,000

AIRPORT CONSULTATIVE COMMITTEES

Airport Consultative Committees are maintained at each airport These provide a forum for the discussion of all matters concerning the development or operation of the airport, which have an impact on the users of the airport and on people living and working in the surrounding area Consultative Committees are a means of keeping all interested parties informed of matters affecting them, of providing an opportunity to reconcile differences of view and resolve difficulties

SAFETY

The group is committed to ensuring, as far as is reasonably practicable, a high standard of health, safety and welfare for members of the public, all employees and others affected by its undertakings

CREDITOR PAYMENT POLICY AND PRACTICE

It is company policy that payments to suppliers are made in accordance with terms and conditions agreed between the company and its suppliers, provided that all trading terms and conditions have been complied with

At 31 March 2006 the company had an average of 11 days' purchases outstanding in trade creditors

HUMAN RESOURCES

At the year end the total staff headcount stood at 304, showing a decrease of 7 on the total staffing levels for the previous year Over the course of the year we recruited to fill 21 permanent posts plus a number of temporary fixed term, part time and relief employees to cover air traffic control and other temporary shortages, while 28 left the company including medical retirements and resignations

Promotions, re grading and transfers resulted in a further 19 staff changes

TRAINING AND DEVELOPMENT

Staff are recognised as a valuable Company resource with a wealth of expertise and experience who excel in providing services to the Company's customers We will ensure that we maintain this quality by investing in recognised standards of management systems and employee development

Where practical and possible, the Company encourages internal promotion to support and promote a career structure Considerable effort is spent in ensuring that staff have the necessary skills to undertake their job efficiently and effectively Career development and training are encouraged, and Staff Development Reviews feed into the Company training plan to encourage staff to build on skills and grow within the organisation The staff turnover associated with our Company is correspondingly low, and therefore appropriate training and development is essential to not only maintain this level but to ensure people have the skills necessary to carry out tasks required of them

Training courses undertaken as a result of regulatory requirements, include phased training of fire service personnel, air traffic services, engineering or specific aviation security courses, which are undertaken internally or sourced through external providers In addition to these aspects, the Company continues to implement its programme which involves recruitment, learning and development in support of its Investors In People accreditation

EMPLOYMENT POLICIES

As a company HIAL promotes equality of opportunity This includes equality of opportunity for people with disabilities within the workplace from the initial recruitment stage through to development and career progression within the company In line with legislation HIAL offers flexible working and family friendly policies and supports these requests whenever this is operationally possible HIAL also has employment policies, which meet statutory requirements and in the case of maternity, paternity and adoptive leave go beyond the statutory minimum

Communication to staff flows through the management structure of the company on a regular basis either through line management or through the functional grouping (AFS, ATC, Engineering etc) The company recognises three Trades Unions (PCS, Prospect, and T&G) and encourages all staff to be a member of the appropriate trade union Joint management/Trades Union meetings are held at least quarterly

POLITICAL AND CHARITABLE CONTRIBUTIONS

No political contributions were made during the year The company made a charitable contribution of £300 to the charity Sunshine Holiday fund during the year

GOING CONCERN

The company sets an annual budget which aims to balance income, expenditure and subsidy provisions set by government Future operational and legislative requirements are addressed in a ten year corporate plan which includes provision for revenue and capital items such as major repairs to runways or new or replacement equipment The subsidy provisions for the year to March 2006 were originally set at £22 1 million and were increased during the year to £23 9 million £21 1 million was drawn down during the year The company has applied to carry forward £1 6 million to meet future expenditure on completion of Benbecula terminal building, 09/27 runway overlay at Sumburgh and contributions to a hangar at Kirkwall The balance of £1 2 million was not drawn down from the Scottish Executive The subsidy provisions have been set at £22 7 million for the year ending March 2007 This is considered by the directors to be adequate to sustain the company as a going concern

AUDITORS

Ernst & Young LLP were reappointed as auditors at the Annual General Meeting on 29 July 2005 A resolution to reappoint Ernst & Young LLP will be laid before the Annual General Meeting on 4 August 2006

DIRECTORS AND THEIR INTERESTS

The directors who served during the year to 31 March 2006 and subsequently are

Alex Matheson, Chairman	
Robert M Macleod, Managing Director	(retired 8 June 2005)
Inglis E Lyon, Managing Director	(appointed 3 May 2005)
William Brackenridge, Director	(retired 30 November 2005)
Stuart Edmond, Director	(retired 31 March 2006)
Charles Alexanderr Goodlad, Director	(appointed 1 March 2006)
Grenville S Johnston, Director	
Shona C MacLennan, Director	
Linn Phipps, Director	(appointed 1 March 2006)

None of the directors had an interest in the share capital of the Company The Register of Directors' interests may be examined by prior arrangement with the Company Secretary during normal office hours at the Registered Office of the company

DIRECTORS' INDEMNITY INSURANCE

During the year the company purchased and maintained liability insurance for its directors as permitted by section 309C of The Companies Act 1985

DIRECTORS' STATEMENT AS TO DISCLOSURE OF INFORMATION TO AUDITORS

The directors who were members of the board at the time of approving the directors' report are listed on page 1 Having made enquiries of fellow directors and of the company's auditors, each of these directors confirms that

- to the best of each director's knowledge and belief, there is no information relevant to the preparation of their report of which the company's auditors are unaware, and
- each director has taken all the steps a director might reasonably be expected to have taken to be aware of relevant audit information and to establish that the company's auditors are aware of that information

By order of the board

Jane Thornton CA
Company Secretary
8 June 2006

STATEMENT ON INTERNAL CONTROL

As Accountable Officer I have responsibility for maintaining a sound system of internal control that supports the achievement of the company's policies, aims and objectives agreed between the Board and the Scottish Ministers, whilst safeguarding the public funds and assets for which I am personally responsible, in accordance with the responsibilities assigned to me

The system of internal control is designed to manage rather than eliminate the risk of failure to achieve the company's policies, aims and objectives It can therefore only provide reasonable and not absolute assurance of effectiveness

The system of internal control is based on an ongoing process designed to identify the principal risks to the achievement of the company's policies, aims and objectives, to evaluate the nature and extent of those risks and to manage them efficiently, effectively and economically This process, which has been fully in place since 14 March 2003, accords with the Scottish Public Finance Manual (SPFM) guidance and has continued up to the date of approval of the annual report and accounts

All bodies subject to the requirements of the SPFM must operate a risk management strategy in accordance with relevant guidance issued by the Scottish Ministers The general principles for a successful risk management strategy are set out in the SPFM

Risk Management

The managing director, senior managers and appropriate line managers are responsible for the effective management of risk within the Company and ensure that appropriate procedures, resources and skills are introduced and maintained to achieve this

Policy aims and objectives adopted by the Board in relation to risk are

- Minimisation of the risks of injury, damage, loss of facilities and inconvenience to the travelling public other service users, staff and service providers arising from the provision of company facilities and services,
- Business continuity,
- Raising awareness of the need for Risk Management throughout the company,
- Enabling the Board of Directors and management of the company to anticipate and respond to changing social, environmental and legislative conditions,
- Application of a documented robust framework and procedures for identification, analysis, assessment and management of risk,
- Minimisation of the cost of risk,
- Ongoing maintenance and review of the Risk Register for the company

Formal reporting lines on risk follow existing management structures Strategic risk is managed and reviewed at Board level The company is also in the process of working with Safety Regulation Group within the Civil Aviation Authority to develop a Safety Management System covering our Air Navigation Service Provision to meet the EU Common Requirements Regulation due to come into effect in 2006 Clear responsibilities, roles and reporting lines have been established across all departments and services provided including a framework that addresses the following issues

- Assessment of the different types of risk – strategic and operational,
- How these risks will be managed and evaluated

- Board and Departmental roles and accountabilities,
- Prompt reporting of accidents, near misses and losses
- Provision for risk assessment in all decision making processes of the Company,
- Measurement of performance in risk management activities against the aims and objectives,
- Ensuring all relevant external agencies contracted to provide services to the Company are aware of the Company's expectations on risk,
- Investigation into incidents and revisiting and adjusting control measures as appropriate,
- Tasking managers with bringing forward for assessment hazards not previously dealt with,
- Revisiting Risk assessments annually Significant changes in hazards will be considered at the time of the change,
- Laying the Risk Register before the Audit Committee and Board annually,

The Board reviews the risk management policy statement annually to ensure its continued relevance to the Company

Control Environment

Capable, competent personnel are viewed as an essential part of the control environment High standards of behaviour are supported by high recruitment standards and ongoing staff training and development

The systems of internal financial control include

- an annual budget approved by the Board
- regular consideration by the Board of budget and actual results
- delegated financial authorities
- clearly defined procurement and evaluation procedures

More generally, the organisation is committed to a process of continuous development and improvement, developing systems in response to any relevant reviews and developments in best practice in this area

As Accountable Officer I have responsibility for reviewing the effectiveness of the system of internal control My review is informed by

- the senior managers within the company who have responsibility for the development and maintenance of the internal control framework,
- the work of the internal auditors, who submit to the company's Audit Committee regular reports which include their objective opinion on the adequacy and effectiveness of the system of internal control, together with recommendations for improvement,
- Comments made by the external auditors in their management letters and other reports

The following processes are established

The Board

The Board is responsible for determining the business strategy of the company, taking into account the Scottish Ministers' expressed policy to encourage economic and social development in the Highlands and Islands

The Board is composed of six members appointed by the Scottish Ministers The six members are the non executive chairman, the executive managing director and four non executive directors The Board meets on a six weekly cycle and has adopted a policy of requiring all significant matters to be referred to the Board for decision unless these are specifically within delegated limits given to the managing director

Monitoring systems used by the Board

The Board at its regular meetings deals with issues of risk and internal control on an ongoing basis In particular, it reviews safety, financial performance including variances from budget, commercial and marketing information and objectives, acquisitions and disposals as necessary, environmental and regulatory issues, business planning and strategies

The management team led by the Managing Director monitors financial performance by a system of monthly financial reporting and review together with forward projections

Board Committees

During the year the Audit Committee was composed of three non executive directors Mr G S Johnston, Mr S Edmond and Ms S MacLennan The Committee, chaired by Mr G S Johnston, works to terms of reference agreed by the Board and meets on a regular basis The managing director and the company secretary are normally invited to attend meetings The Committee receives regular reports from both the internal and external auditors and makes periodic reports concerning internal control to the Board The Committee reviews and comments to the Board as to corporate governance compliance and the adequacy of risk management arrangements

Internal Audit

The internal audit concentrates on areas determined by analysis of the degree of risk and in accordance with the internal audit plan considered by the Audit Committee and approved by the Board The Audit Committee enhances the independence and value of internal audit and provides a forum for senior management to discuss internal control including issues raised by internal audit

Operational Control

Each of the airports under the company's control is subject to regular operational inspections by the Civil Aviation Authority as regulator

The Assessor

An Assessor appointed by the Scottish Ministers is entitled to attend but not vote at any meeting of the company or its directors

Appropriate action is in place to address any weaknesses identified and to ensure the continuous improvement of the system

I E Lyon
Managing Director
8 June 2006

STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE ACCOUNTS

The directors are responsible for preparing the Annual Report and the financial statements in accordance with the applicable law and United Kingdom Generally Accepted Accounting Practice Company law requires the directors to prepare accounts for each financial year which give a true and fair view of the state of affairs of the company and of the group and of the profit or loss of the group for that period In preparing those accounts, the directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgements and estimates that are reasonable and prudent,
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts,
- prepare the accounts on the going concern basis unless it is inappropriate to presume that the company will continue in business

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the group and to enable them to ensure that the accounts comply with the Companies Act 1985 They are also responsible for safeguarding the assets of the group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities

GROUP PROFIT AND LOSS ACCOUNT

FOR THE YEAR 1 APRIL 2005 TO 31 MARCH 2006

	Note	2006	2005
			As restated
		£000	£000
TURNOVER			
Continuing operations			
Ongoing		11,766	10,826
Acquisitions – Inverness Air Terminal Limited		147	—
GROUP TURNOVER		11,913	10,826
Total subsidies receivable		60,704	21,505
Less Capital subsidies carried to deferred income		45,941	4,101
Revenue subsidies from Scottish Ministers and others	(2)	14,763	17,404
		26,676	28,230
DIRECT OPERATING COSTS		(24,834)	(25,947)
GROSS PROFIT		1,842	2,283
ADMINISTRATIVE EXPENSES		(3,821)	(3,608)
OPERATING (LOSS)			
Continuing operations			
Ongoing		(2,203)	(1,325)
Acquisitions – Inverness Air Terminal Limited		224	
GROUP OPERATING (LOSS)	(3)(4)	(1,979)	(1,325)
Share of operating (loss) in joint venture		(37)	—
TOTAL OPERATING (LOSS) GROUP AND SHARE OF JOINT VENTURE		(2,016)	(1,325)
PROFIT (LOSS) ON DISPOSAL OF TANGIBLE FIXED ASSETS		1,155	(22)
		(861)	(1,347)
INTEREST RECEIVABLE AND SIMILAR INCOME	(7)	437	407
INTEREST PAYABLE AND SIMILAR CHARGES	(8)	(266)	—
(LOSS) ON ORDINARY ACTIVITIES BEFORE TAX		(690)	(940)
TAX ON ORDINARY ACTIVITIES	(9)	(279)	—
(LOSS) FOR THE FINANCIAL YEAR		(969)	(940)

Notes 1 to 22 form part of these accounts

GROUP STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES
FOR THE YEAR ENDED 31 MARCH 2006

	2006 £000	2005 £000
(Loss) for the financial year excluding share of losses of joint venture	**(933)**	(940)
Share of joint venture's (loss) for the year	**(36)**	
(Loss) for the financial year attributable to members of the parent company	**(969)**	(940)
Actuarial gain on pension scheme	**1,300**	3,200
Total recognised gain relating to the financial year	**331**	2,260
Prior year adjustment		(2,300)
Total gain (loss) recognised since last annual report	**331**	(40)

Notes 1 to 22 form part of these accounts

GROUP BALANCE SHEET
AS AT 31 MARCH 2006

	Note	£000	2006 £000	£000	2005 £000
FIXED ASSETS					
Intangible assets	(10)		3,188		
Tangible assets	(11)		55,303		39,093
Investments	(12)				
Investment in joint venture					
Share of gross assets		1,472			
Share of gross liabilities		(1,190)			
Element redeemable to company		1,823		—	
			2,105		
Other investments			103		
			60,699		39,093
CURRENT ASSETS					
Debtors	(13)	3,171		2,229	
Cash in hand		3,192		1,507	
		6,363		3,736	
CREDITORS Amounts falling due within one year	(14)	(3,164)		(1,872)	
NET CURRENT ASSETS			3,199		1,864
TOTAL ASSETS LESS CURRENT LIABILITIES			63,898		40,957
PROVISION FOR LIABILITIES AND CHARGES	(15)		(579)		
ACCRUALS AND DEFERRED INCOME					
Deferred Government subsidies	(16)		(58,128)		(35,797)
NET ASSETS EXCLUDING RETIREMENT BENEFITS			5,191		5,160
Retirement benefits asset	(19)		400		100
NET ASSETS INCLUDING RETIREMENT BENEFITS			5,591		5,260
CAPITAL AND RESERVES					
Share capital	(17)		50		50
Profit and loss account	(18)		5,541		5,210
TOTAL SHAREHOLDER'S EQUITY	(18)		5,591		5,260

Alex Matheson

Alex Matheson, **Chairman**

Inglis Lyon, **Managing Director**

8 June 2006

Notes 1 to ~~21~~ 22 form part of these accounts

COMPANY BALANCE SHEET

AS AT 31 MARCH 2006

	Note	2006 £000	2005 £000
FIXED ASSETS			
Tangible assets	(11)	44,230	39,093
Investments	(12)	30,921	—
		75,151	39,093
CURRENT ASSETS			
Debtors	(13)	9,273	2,229
Cash in hand		1,552	1,507
		10,825	3,736
CREDITORS Amounts falling due within one year	(14)	(2,896)	(1,872)
NET CURRENT ASSETS		7,929	1,864
TOTAL ASSETS LESS CURRENT LIABILITIES		83,080	40,957
PROVISION FOR LIABILITIES AND CHARGES	(15)	(21,738)	
ACCRUALS AND DEFERRED INCOME			
Deferred Government subsidies	(16)	(56,022)	(35,797)
NET ASSETS EXCLUDING RETIREMENT BENEFITS		5,320	5,160
Retirement benefits asset	(19)	400	100
NET ASSETS INCLUDING RETIREMENT BENEFITS		5,720	5,260
CAPITAL AND RESERVES			
Share capital	(17)	50	50
Profit and loss account	(18)	5,670	5,210
TOTAL SHAREHOLDER'S EQUITY	(18)	5,720	5,260

Alex Matheson Alex Matheson, **Chairman**

Inglis Lyon, **Managing Director**
8 June 2006

Notes 1 to ~~21~~ 22 form part of these accounts

GROUP CASH FLOW STATEMENT

FOR THE YEAR 1 APRIL 2005 TO 31 MARCH 2006

	Note		2006		2005
		£000	**£000**	£000	£000
NET CASH INFLOW FROM OPERATING ACTIVITIES	(4 2)		**350**		16
RETURNS ON INVESTMENTS AND SERVICING OF FINANCE					
Interest received			**136**		104
CAPITAL EXPENDITURE AND FINANCIAL INVESTMENT					
Purchase of tangible fixed assets		**(9,779)**		(4,409)	
Purchase of investments		**(2,588)**			
Receipt of capital subsidy Scottish Ministers		**44,156**		4,105	
European Regional Development Fund		**1,548**		184	
Other		**237**		14	
Sale of tangible fixed assets		**1,214**		94	
			34,788		(12)
ACQUISITIONS AND DISPOSALS					
Purchase of subsidiary undertaking		**(28,333)**			
Net cash acquired with subsidiary undertaking		**1,309**			
			(27,024)		
FINANCING					
Repayment of long term loans			**(6,565)**		
INCREASE IN CASH			**1,685**		108

RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET FUNDS

	£000	£000
Increase in cash in the period	**1,685**	108
Net funds at 1 April	**1,507**	1,399
Net funds at 31 March	**3,192**	1,507

Notes 1 to 22 form part of these accounts

NOTES TO THE FINANCIAL STATEMENTS

BASIS OF PREPARATION

1 ACCOUNTING POLICIES

1 1 Basis of preparation

The accounts are prepared in accordance with the historical cost convention and in accordance with applicable accounting and financial reporting standards The company receives subsidies from the Scottish Ministers on an annual basis The annual accounts are prepared on the assumption that the company will continue to receive such subsidies for the foreseeable future

1 2 Basis of Consolidation

The group accounts consolidate the results of Highlands and Islands Airports Limited and its subsidiary undertakings drawn up to 31 March each year No individual profit and loss account is presented for Highlands and Islands Airports Limited as permitted in section 230 of the Companies Act 1985 The Company loss for the year was £840,000

Inverness Air Terminal Limited has been included in the group accounts using the acquisition method of accounting Accordingly, the group profit and loss account and statement of cash flows include the results and cash flows of Inverness Air Terminal Limited for the period from its acquisition on 20 January 2006 The purchase consideration has been allocated to the assets and liabilities on the basis of fair value at the date of acquisition

Entities in which the group holds an interest on a long term basis and are jointly controlled by the group and one or more other venturers under a contractual arrangement are treated as joint ventures In the group accounts, joint ventures are accounted for using the gross equity method

1 3 Goodwill

Positive goodwill arising on acquisitions is capitalised, classified as an asset on the balance sheet and amortised on a straight line basis over its useful economic life up to a presumed maximum of 10 years It is reviewed for impairment at the end of the first full financial year following the acquisition and in other periods if events or changes in circumstances indicate that the carrying value may not be recoverable

1 4 Intangible Assets

Intangible asses acquired separately from a business are capitalised at cost Intangible assets acquired as part of an acquisition of a business are capitalised separately from goodwill if the fair value can be measured reliably on initial recognition, subject to the constraint that, unless the asset has a readily ascertainable market value, the fair value is limited to an amount that does not create or increase any negative goodwill on the acquisition Intangible assets, excluding development costs, created within the business are not capitalised and expenditure is charged against profits in the year in which it is incurred

Intangible assets are amortised on a straight line basis over their estimated useful lives up to a maximum of 10 years The carrying value of intangible assets is reviewed for impairment at the end of the first full year following acquisition and in other periods if events or changes in circumstances indicate that the carrying value may not be recoverable

1 5 Tangible Assets

Tangible fixed assets are stated at cost Interest and other directly attributable finance costs in respect of loans for the purposes of constructing assets, are capitalised as part of the cost of constructing the buildings up to the date of practical completion Subsequent interest is charged to the profit and loss account

Depreciation is provided on tangible fixed assets to spread the cost by equal annual instalments over their estimated useful lives, as follows

Freehold buildings	20 25 years
Leasehold land and buildings	over the remaining life of the lease to a maximum of 20 years

Navigation aids	7 years
Plant and other equipment	3 10 years
Vehicles	5 years
Runways, aprons and main services	7 25 years
Runway bases	100 years

The following categories of tangible fixed assets are not depreciated

Freehold land

Furniture, fixtures and fittings

Initial purchases of furniture, fixtures and fittings are treated as tangible fixed assets, replacement expenditure is charged to the profit and loss account Items that are disposed of and not replaced are eliminated from tangible fixed assets

Net Depreciation (as disclosed in Note 3) includes depreciation charge for the year and release of deferred government subsidies

1 6 Investments

Investments are shown at cost less provision for impairment

1 7 Subsidies

Subsidies in respect of capital expenditure are credited to a deferred income account and released to the profit and loss account over the estimated useful lives of the relevant assets

Subsidies for revenue expenditure are separately disclosed within turnover in the period to which they relate

1 8 Deferred Taxation

Deferred taxation is provided in full on timing differences that result in an obligation at the balance sheet date to pay more tax, or a right to pay less tax, at a future date, at rates expected to apply when they crystallise based on current tax rates and law Timing differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in financial statements Deferred tax assets and liabilities are not discounted

1 9 Leases

The rentals on operating leases are charged to the profit and loss account as incurred

1 10 Pension Costs

The company operates the Highlands and Islands Airports Pension Scheme, a defined benefit scheme Contributions are charged to the profit and loss account in accordance with actuarial recommendations, so as to spread the cost over the employees' remaining working lives with the company

On the advice of an independent qualified actuary, contributions are made to the plan to ensure that the plan's 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 at the current rate of return on a high quality corporate bond of equivalent term and currency to the liability Any increase in the present value of the liabilities of the defined benefit pension plan expected to arise from employee service in the period is charged against operating profit The expected return on the plan's assets and the increase during the period in the present value of the plan's liabilities arising from the passage of time are included in interest receivable and similar income Actuarial gains and losses are recognised in the Statement of Total Recognised Gains and Losses

1 11 Capital instruments

In accordance with FRS4 "capital instruments", the costs associated with the issue of capital instruments, other than shares, are charged to the profit and loss account over the life of the instrument, at a constant rate based on the carrying amount

2 TURNOVER

Turnover represents amounts received and receivable (stated net of value added tax) in respect of airport services provided in the UK

Revenue subsidies from Scottish Ministers and others represent a revenue subsidy of £14,467,000 received from the Scottish Ministers in accordance with Section 34 of the Civil Aviation Act 1982 and a total of £16,000 received from Highlands & Islands Enterprise and Inverness, Nairn, Badenoch & Strathspey Enterprise towards various studies A further £260,000 was utilised from the Route Development Fund, which provides support for new cross border routes from the Highlands and Islands, up to 31 March 2006

The results of Inverness Air Terminal Limited, which was acquired on 20 January 2006, all relate to the operation of the Terminal building at Inverness Airport Its turnover, both by source and destination, all relates to the United Kingdom

3 OPERATING RESULTS – YEAR TO 31 MARCH 2006

	Total Activities		Consolidation Inter group trading		Subsidy received from Scottish Ministers		Barra		Benbecula		Campbeltown		Inverness	
	2006	2005	**2006**	2005	**2006**	2005	**2006**	2005	**2006**	2005	**2006**	2005	**2006**	2005
		As restated		As restated		As restated		As restated		As restated		As restated		As restated
	£000	£000	**£000**	£000	**£000**	£000	**£000**	£000	**£000**	£000	**£000**	£000	**£000**	£000
Turnover														
Traffic operations	10 552	9,488	-	-	-	-	152	119	473	435	191	142	4 802	4 233
Other income	1 361	1 338	(397)	-	-	-	10	8	53	66	71	12	424	638
Subsidies receivable	14 763	17 404	-	-	14 487	17 333	-	-	1	-	-	-	167	67
	26 676	28 230	(397)	-	14 487	17 333	162	127	527	501	262	154	5,393	4 938
Operating costs														
Staff costs	14 737	14,258	-	-	-	-	391	400	1 363	1 219	581	548	3 123	3 374
Property rates	860	805	-	-	-	-	8	7	44	38	16	15	313	276
Security utilities materials	6,989	6 505	(397)	-	-	-	95	87	244	227	147	103	3 678	3 170
Repairs and maintenance	2 252	4 051	-	-	-	-	60	83	163	314	148	220	423	900
Net depreciation	505	466	56	-	-	-	13	14	25	24	(1)	(1)	176	231
Other operating costs	3,312	3 470	-	-	-	-	128	115	255	220	67	84	662	921
	28 655	29 555	(341)	-	-	-	695	706	2 094	2 042	958	969	8 375	8 872
Operating (loss) profit	(1 979)	(1 325)	(56)	0	14 487	17,333	(533)	(579)	(1 567)	(1 541)	(696)	(815)	(2 982)	(3,934)

3 OPERATING RESULTS – YEAR TO 31 MARCH 2006 (continued)

	Inverness Air Terminal Limited		Islay		Kirkwall		Stornoway		Sumburgh		Tiree		Wick	
	2006	2005 As restated	**2006**	2005 As restated	**2006**	2005 As restated	**2006**	2005 As restated	**2006**	2005 As restated	**2006**	2005 As restated	**2006**	2005 As restated
	£000	£000	**£000**	£000	**£000**	£000	**£000**	£000	**£000**	£000	**£000**	£000	**£000**	£000
Turnover														
Traffic operations	-	-	301	249	1,105	1 019	1 278	1 190	1 652	1,563	113	84	485	454
Other income	544	-	29	23	105	87	215	225	242	232	25	18	40	29
Subsidies receivable	-	-	-	-	1	-	5	-	6	4	-	-	96	-
	544	-	330	272	1 211	1 106	1 498	1 415	1 900	1 799	138	102	621	483
Operating costs														
Staff costs	-	-	667	599	2 054	2 086	1,907	1 930	2 465	2 347	424	395	1,762	1,360
Property rates	-	-	25	23	136	119	105	107	163	174	11	12	39	34
Security utilities materials	212	-	193	196	639	667	684	683	1 051	1 019	107	91	336	262
Repairs and maintenance	4	-	119	183	329	496	288	743	364	601	111	194	243	317
Net depreciation	65	-	15	32	(18)	18	23	(36)	60	54	42	76	49	54
Other operating costs	39	-	90	97	230	287	262	296	1 217	1 190	58	80	304	180
	320	-	1,109	1 130	3 370	3,673	3 269	3 723	5,320	5,385	753	848	2 733	2 207
Operating (loss) profit	224	-	(779)	(858)	(2 159)	(2 567)	(1,771)	(2,308)	(3 420)	(3 586)	(615)	(746)	(2 112)	(1 724)

		2006 £000	2005 £000
4	OPERATING LOSS		
4 1	*This is stated after charging*		
	Depreciation	**4,325**	3,802
	Auditors' remuneration – audit services	**14**	10
	Auditors' remuneration – non audit services	**7**	
	Goodwill impairment	**21,738**	
	Amortisation of other intangible assets	**56**	
	And after crediting		
	Subsidies released	**25,612**	3,336

		2006 £000	2005 As restated £000
4 2	Reconciliation of operating loss to net cash inflow from operating activities		
	Operating (loss)	**(1,979)**	(1,325)
	Depreciation	**4,325**	3,802
	Deferred subsidies released	**(25,612)**	(3,336)
	Increase in debtors	**(477)**	(181)
	Increase (decrease) in creditors	**999**	(44)
	Other non cash movements		
	Current service costs	**1,000**	800
	Past service costs	**300**	300
	Amortisation of other intangible assets	**56**	
	Impairment of goodwill	**21,738**	
	Net cash inflow from operating activities	**350**	16

		2006 £000	2005 £000
5	STAFF COSTS		
	Wages and salaries	**9,997**	9,651
	Social security costs	**848**	820
	Pension costs	**3,442**	3,162
	Other staff costs	**450**	625
		14,737	14,258

The average number of employees during the period was 308 (2005 309)

		2006 £000	2005 £000
6	DIRECTORS' EMOLUMENTS		
	Emoluments	**148**	136
	Pension contributions	**19**	17

Directors' emoluments, including pension contributions, fell within the following ranges

		2006 No.	2005 No
£1	£5,000	**3**	
£5,001	£10,000	**3**	4
£20,001	£25,000	**2**	1
£95,001	£100,000	**1**	
£105,001	£110,000		1

The emoluments of the Chairman were £20,911 (2005 £20,568) including pension contributions of £Nil (2005 £Nil) and of the highest paid director, Inglis Edward Lyon, were £82,020 (2005 £Nil) including pension contributions of £16,039 (2005 £Nil)

Mr I Lyon and Mr R M Macleod were the only directors for whom the company made contributions during the year who were members of the Highlands and Islands Airports Pension Scheme

Directors' emoluments include £1,094 that was paid to Johnston Carmichael for the services of Grenville Johnston as a director during the period while he was a consultant for that firm

Directors' emoluments include £6,685 that was paid to Solas Business Services Limited for the services of Shona MacLennan as a director during the year

NOTES TO THE FINANCIAL STATEMENTS

		2006 £000	2005 £000
7	INTEREST RECEIVABLE AND SIMILAR INCOME		
	Interest received	130	107
	Expected return on pension plan assets	2,200	2,000
	Interest on retirement benefits liabilities	(1,900)	(1,700)
		430	407

		2006 £000	2005 £000
8	INTEREST PAYABLE AND SIMILAR CHARGES		
	Finance advisory fees	266	—

9 TAX ON ORDINARY ACTIVITIES

	2006 £000	2005 £000
Current tax		
UK corporation tax	284	—
Deferred tax		
Originating and reversal of timing differences	(5)	—
Tax on profit on ordinary activities	279	—

9 1 Factors affecting current tax charge

The tax assessed for the period is different from the standard rate of corporation tax in the UK of 30% (2005 30%) The differences are explained below

	2006 £000	2005 As restated £000
(Loss) on ordinary activities before tax	(690)	(940)
Tax at 30% thereon	(207)	(282)
Effects of		
Expenses not deductible for tax purposes	(174)	67
Other timing differences	8	
Capital allowances in excess of net depreciation	20	52
Pension provisions not deductible for tax purposes	300	239
Utilisation of tax losses	(1)	(96)
Adjustments relating to the sale of fixed assets	338	20
Current tax charge for period	284	—

10 INTANGIBLE FIXED ASSETS

	Goodwill £000	Other £000	Total £000
Cost			
At 1 April 2005			
Acquisition of subsidiary undertaking	21,738		21,738
Other intangible assets		2,900	2,900
Share of joint venture	344		344
At 31 March 2006	**22,082**	**2,900**	**24,982**
Amounts provided			
At 1 April 2005			
Provided during the year	21,738	56	21,794
31 March 2006	**21,738**	**56**	**21,794**
Net book value at 31 March 2006	**344**	**2,844**	**3,188**
Net book value at 31 March 2005			

The goodwill has been immediately impaired as it has no useful life due to Inverness Air Terminal Limited only carrying out a single contract, with the company being the other party and there is no external income to the group

Other intangible assets relates to concession income separately identifiable as part of the acquisition of Inverness Air Terminal Limited This is being amortised over its useful economic life of 10 years

11 TANGIBLE FIXED ASSETS

Group

	Land and Buildings Freehold £000	Navaids £000	Plant and Other Equipment Vehicles Furniture £000	Runways Aprons and Main Services £000	Assets in Course of Construction and Installation £000	Total £000
Cost or valuation						
At 1 April 2005	22,172	8,285	15,696	20,670	2,946	**69,769**
Additions during year	295		166	18	9,081	**9,560**
Acquisition of subsidiary undertaking	11,130		31			**11,161**
Disposals during year	(21)	(58)	(686)	(4)	(74)	**(843)**
Transfers during year	876		872		(1,748)	
At 31 March 2006	**34,452**	**8,227**	**16,079**	**20,684**	**10,205**	**89,647**
Depreciation						
At 1 April 2005	(7,621)	(2,938)	(11,515)	(8,602)		**(30,676)**
Provided during year	(1,202)	(953)	(924)	(1,246)		**(4,325)**
Disposals during year	18	58	577	4		**657**
At 31 March 2006	**(8,805)**	**(3,833)**	**(11,862)**	**(9,844)**		**(34,344)**
Net book value **at 31 March 2006**	**25,647**	**4,394**	**4,217**	**10,840**	**10,205**	**55,303**
Net book value at 31 March 2005	14,551	5,347	4,181	12,068	2,946	39,093

Company

	Land and Buildings Freehold £000	Navaids £000	Plant and Other Equipment Vehicles Furniture £000	Runways Aprons and Main Services £000	Assets in Course of Construction And Installation £000	Total £000
Cost						
At 1 April 2005	22,172	8,285	15,696	20,670	2,946	**69,769**
Additions during year	295		166	18	9,081	**9,560**
Disposals during year	(21)	(58)	(686)	(4)	(74)	**(843)**
Transfers during year	876		872		(1,748)	
At 31 March 2006	**23,322**	**8,227**	**16,048**	**20,684**	**10,205**	**78,486**
Depreciation						
At 1 April 2005	(7,621)	(2,938)	(11,515)	(8,602)		**(30,676)**
Provided during year	(1,116)	(953)	(922)	(1,246)		**(4,237)**
Disposals during year	18	58	577	4		**657**
At 31 March 2006	**(8,719)**	**(3,833)**	**(11,860)**	**(9,844)**		**(34,256)**
Net book value **at 31 March 2006**	**14,603**	**4,394**	**4,188**	**10,840**	**10,205**	**44,230**
Net book value at 31 March 2005	14,551	5,347	4,181	12,068	2,946	39,093

The net book value of freehold land and buildings includes £311,752 in respect of land (2005 £304,217)

12 INVESTMENTS

Group

	2006 £000	2005 £000
Joint venture (a)	2,105	
Other fixed asset investments (b)	103	
	2,208	

(a) Joint venture

	£000
At 1 April 2005	
Share of loss retained by joint venture	(36)
At 31 March 2006	(36)

Additional disclosures are given in respect of Inverness Airport Business Park Limited, which exceeds certain thresholds under FRS 9 "Associates and Joint Ventures", as follows

	2006 £000	2005 £000
Fixed assets	1,440	
Current assets	32	
Share of gross assets	1,472	
Liabilities due within one year	104	
Liabilities due after more than one year	1,086	
Share of gross liabilities	1,190	
Share of net assets	282	-
Redeemable shares of £1 each held by the company	1,823	
Investment in joint venture	2,105	

The summarised results of the joint venture company are as follows

	2006 £000	2005 £000
Turnover		
Loss before tax	(105)	
Taxation		
Loss after tax	(105)	

(b) Other fixed asset investments

	£000
At 1 April 2005	
Additions	103
At 31 March 2006	103

Company

	Subsidiary undertakings £000	Joint ventures £000	Other investments £000	Total £000
Cost				
At 1 April 2005	50			50
Additions	28,333	2,485	103	30,921
At 31 March 2006	**28,383**	**2,485**	**103**	**30,971**
Amounts provided				
At 1 April 2005 and 31 March 2006	**50**			**50**
Net book value at 31 March 2006	**28,333**	**2,485**	**103**	**30,921**
Net book value at 31 March 2005				

Details of the investments in which the company holds 20% or more of the nominal value of any class of share capital are as follows

Name of company	Holding	Proportion of shares held	Nature of Business
Subsidiary undertakings			
Airport Management Services Limited	Ordinary shares	100%	Dormant
Inverness Air Terminal Limited	Ordinary shares	100%	Terminal building operations
Joint venture			
Inverness Airport Business Park Limited	Ordinary shares	34%	Property investment
	Redeemable shares	87%	

On 20 January 2006 the group acquired Inverness Air Terminal Limited for a consideration of £28,333,000 The investment in Inverness Air Terminal Limited has been included in the company's balance sheet at its fair value at the date of acquisition

Analysis of the acquisition of Inverness Air Terminal Limited

Net assets at date of acquisition

	Book value £000	Adjustments Revaluation £000		Other £000	Fair value to Group £000
Tangible fixed assets	7,900	3,260	(a)		11,160
Other intangible fixed assets		2,900	(b)		2,900
Debtors	476				476
Cash	1,309				1,309
Creditors due within one year	(239)				(239)
Creditors due after one year	(8,427)				(8,427)
Deferred taxation	(584)				(584)
Net assets	435	6,160			6,595
Goodwill arising on acquisition					21,738
					28,333

Adjustments

(a) Increase in the value of land and buildings as a result of a revaluation carried out on acquisition

(b) Other intangible fixed assets relates to concession income separately identifiable as part of the acquisition of Inverness Air Terminal Limited This is being amortised over its useful economic life of 10 years

Inverness Air Terminal Limited contributed an outflow of £143,000 to the group's net operating cash inflow, received £6,000 in respect of net returns on investments and servicing of finance and paid £6,565,000 in respect of financing

Inverness Air Terminal Limited earned a profit after tax of £620,000 in the year ended 31 March 2006 (2005 £538,000), of which £657,000 arose in the period from 1 April 2005 to 20 January 2006 The summarised profit and loss account for the period from 1 April 2005 to the effective date of acquisition is as follows

	£000
Turnover	**2,653**
Operating profit	**1,464**
Interest receivable	**24**
Interest payable	**(411)**
Profit before tax	**1,077**
Taxation	**(420)**
Profit for the period ended 20 January 2006	**657**

There were no recognised gains and losses in the period ended 20 January 2006 other than the profit of £657,000 above

		Group 2006 £000	Company 2006 £000	Group 2005 £000	Company 2005 £000
13	DEBTORS				
	Trade debtors	1,514	1,117	1,073	1,073
	Prepayments and accrued income	384	247	293	293
	Amounts owed by subsidiary undertaking		6,636		
	Amounts owed by joint venture	133	133		
	Other debtors	1,140	1,140	863	863
		3,171	9,273	2,229	2,229

		Group 2006 £000	Company 2006 £000	Group 2005 £000	Company 2005 £000
14	CREDITORS				
	Amounts falling due within one year				
	Trade creditors	825	781	529	529
	Other creditors	544	518	36	36
	Corporation tax	283	278		
	Other taxes and social security costs	375	277	279	279
	Accruals and deferred income	1,137	1,042	1,028	1,028
		3,164	2,896	1,872	1,872

		Group 2006 £000	Company 2006 £000	Group 2005 £000	Company 2005 £000
15	PROVISION FOR LIABILITIES AND CHARGES				
	Deferred tax	579			
	Onerous contract provision		21,738		
		579	21,738		
	Analysis of deferred tax balances				
	capital allowances in advance of depreciation	579		15	15
	trading losses			(15)	(15)
		579			

A deferred tax asset has not been recognised in respect of timing differences related to,

1 Historical trading losses incurred by the company amounting to £6 3 million, which will be recovered only if the company begins to make significant taxable profits

2 Pension provisions made in the accounts amounting to £1 0 million (net), which are not tax deductible in the current year and will be tax deductible only when paid

There is insufficient evidence that this asset will be recovered to allow it's recognition in these accounts

The estimated value of the deferred tax asset not recognised, measured at a standard rate of 30% is £2,211,000

Onerous contract provision

HIAL purchased Inverness Air Terminal Limited on 20 January 2006 The consideration was £28,333,000 An evaluation was carried out on the basis of future cash flows and this purchase price was demonstrated to represent value for money compared with the PFI contract running its full term to 2024 An onerous contract provision of £21,738,000 has been made in the company's accounts

		Group	**Company**	Group As restated	Company As restated
		2006	**2006**	2005	2005
		£000	**£000**	£000	£000
16	DEFERRED SUBSIDIES				
	Balance at 1 April	**35,797**	**35,797**	35,079	35,079
	Subsidies Receivable	**45,941**	**45,941**	4,101	4,101
	Deferred grants acquired with subsidiary undertaking	**2,129**			
	Released to profit and loss account	**(25,612)**	**(25,589)**	(3,336)	(3,336)
	Released against asset disposals	**(127)**	**(127)**	(47)	(47)
	Balance at 31 March	**58,128**	**56,022**	35,797	35,797

17 SHARE CAPITAL

	Company			
	Authorised		Issued and fully paid	
	2006	2005	**2006**	2005
	Number	Number	**£000**	£000
Ordinary shares of £1 each	**50,000**	50,000	**50**	50

18 SHARE CAPITAL, MOVEMENT ON RESERVES AND RECONCILIATION OF MOVEMENT IN SHAREHOLDER'S FUNDS

Group

	Share Capital £000	Profit and Loss account £000	Total £000
At 1 April 2005	50	5,210	5,260
Retained loss for the year		**(969)**	**(969)**
Actuarial gain on pension scheme		**1,300**	**1,300**
At 31 March 2006	50	5,541	5,591

The cumulative amount of goodwill written off at 31 March 2006 is £21,738,000 (2005 £Nil)

Company

	Share Capital £000	Profit and Loss account £000	Total £000
At 1 April 2005	50	5,210	5,260
Retained loss for the year		**(840)**	**(840)**
Actuarial gain on pension scheme		**1,300**	**1,300**
At 31 March 2006	50	5,670	5,720

19 PENSION COSTS

The information below is disclosed in accordance with the provisions of FRS17

This note excludes assets and liabilities in respect of money purchase AVCs and insured pensions

	2006 £000	2005 £000	2004 £000	2003 £000
Total market value of assets	**43,100**	32,700	26,300	21,100
Present value of the scheme's liabilities	**42,700**	32,600	28,600	27,600
Surplus in the scheme	**400**	100	(2,300)	(6,500)

As a deferred tax asset has not been recognised, see note 13, the related deferred tax liability of £120,000 on the above surplus in the scheme has not been recognised

The Company operates a defined benefit scheme in the UK The values of the scheme's liabilities have been determined by a qualified actuary based on the results of an actuarial valuation as at 31 December 2004, updated to the balance sheet date, and using the following assumptions

	2006 %pa	2005 %pa	2004 %pa	2003 %pa
Discount rate	**5.0**	5 4	5 5	5 4
Rate of increase in salaries	**4.3**	4 3	4 3	4 1
Rate of increase in pensions in payment	**2.9**	2 9	2 9	2 7
Rate of increase in pensions deferment	**2.9**	2 9	2 9	2 7
Rate of inflation	**2 9**	2 9	2 9	2 6
Mortality table	**PA92C2020**	PA92C2020	PA92C2020	PA80 5

The company's share of the assets in the Highlands and Islands Airports Pension Scheme and the expected rate of return were

	Expected long term return %	**Value at 2006 £000**	Expected long term return %	Value at 2005 £000	Expected long term return %	Value at 2004 £000	Expected long term return %	Value at 2003 £000
Equities	**7 5**	**28,100**	7 50	20,000	7 5	25,600	7 5	17 300
Bonds	**5 0**	**14,700**	5 00	12,400				
Other	**4 5**	**300**	4 75	300	4 0	700	6 0	3,800
Total market value of assets		**43,100**		32,700		26 300		21,100

	2006 £000	2005 £000	2004 £000
Analysis of amount charged to operating profit			
Current service cost (excluding employee contributions)	**3,200**	2,900	2,500
Past service cost	**300**	300	
Total operating charge	**3,500**	3,200	2,500
Analysis of amount credited to other finance income			
Expected return on pension scheme assets	**2,200**	2,000	1,500
Interest on pension scheme liabilities	**(1,900)**	(1,700)	(1,500)
Net return	**300**	300	

	2006 £000	2005 £000	2004 £000
Analysis of amount recognised in STRGL			
Actual less expected return on assets	**5,500**	1,900	3,600
Experience gains on liabilities	**300**	1,800	1,900
Effect of change in assumptions on liabilities	**(4,500)**	(500)	(1,300)
Actuarial gain recognised in STRGL	**1,300**	3,200	4,200

The Company has agreed to contribute at a rate of 22 0% of pensionable salaries for the next accounting year

	2006 £000	**2005 £000**	**2004 £000**
Movement in surplus (deficit) during the year			
Surplus (deficit) in scheme at start of the year	**100**	(2,300)	(6,500)
Current service cost (excluding employee contributions)	**(3,200)**	(2,900)	(2,500)
Cash contribution (excluding employee contributions)	**2,200**	2,100	2,500
Past service cost	**(300)**	(300)	
Other finance income	**300**	300	
Actuarial gain	**1,300**	3,200	4,200
Surplus (deficit) in scheme at end of the year	**400**	100	(2,300)

History of experience gains and losses	**2006**	2005	2004	2003
Difference between expected and actual returns on scheme assets				
amount	**5,500**	1,900	3,600	8,400
% of assets at year end	**13%**	6%	14%	40%
Experience gains (losses) on scheme liabilities				
amount	**300**	1,800	1,800	(300)
% of liabilities at year end	**1%**	6%	6%	(1%)
Total gain recognised in STRGL				
amount	**1,300**	3,200	4,100	11,600
% of liabilities at year end	**3%**	10%	14%	42%

20 POST BALANCE SHEET EVENT

The dırectors agreed ın prıncıple, prıor to the year end, to restructure the group by hıvıng up the trade, assets and lıabılıtıes of IATL ınto the parent company HIAL The net assets wıll be transferred at theır net book value (excludıng inter company loans) of £10,293,534 Due to the tıme requıred to prepare the transfer documentatıon, the transfer agreement was not sıgned at the year end, but the dırectors ıntend the transfer to be effectıve from 1 Aprıl 2006 It ıs lıkely that the transfer agreement wıll be sıgned early ın the new financıal year but after the date these accounts are sıgned

	Group 2006 £000	**Company 2006 £000**	Group 2005 £000	Company 2005 £000
21 CAPITAL COMMITMENTS				
Contracted	2,749	2,749	9,446	9,446

22 RELATED PARTIES

(a) Durıng the year the company receıved subsıdıes totallıng £58,902,000 from the Scottısh Mınısters At the balance sheet date there was a balance of £490,000 due to Scottısh Mınısters

(b) Durıng the year the company paıd £1,559 to Johnston Carmıchael, for the servıces of Grenvılle Johnston, for professıonal advıce and guıdance provıded ın settıng up the new Hıghlands and Islands Aırports Pensıon Scheme The company also paıd £2,245 to Johnston Carmıchael ın respect of taxatıon advıce Grenvılle Johnston, a dırector of the company, also acted as a consultant to that firm durıng the year

(c) Durıng the year the company provıded on call servıces to the Scottısh Ambulance Servıce at a cost of £316,825 At the balance sheet date there was a balance of £97,016 due from the Scottısh Ambulance Servıce Wıllıam Brackenrıdge, a dırector of the company durıng the year, was also the chaırman of Scottısh Ambulance Servıce durıng the year

(d) Durıng the year the company transferred land ınto Inverness Aırport Busıness Park Lımıted, a joınt venture company The value of the land transferred was £1,162,000 for whıch the company receıved redeemable shares The company also contrıbuted £1,322,000 towards the constructıon of the new Inverness aırport access road for whıch redeemable shares of £661,000 were receıved, the balance beıng a capıtal contrıbutıon

These transactıons were entered ınto on an arm's length basıs

ECONOMIC REGULATION STATEMENT

FOR THE YEAR 1 APRIL 2005 TO 31 MARCH 2006

Highlands and Islands Airports Limited is subject to economic regulation under the Airports Act 1986 which requires the company to hold permissions from the Civil Aviation Authority to levy airport charges

Operational activities are required to be allocated between airport charges levied in connection with the landing, parking and taking off of aircraft (including passenger related charges) and other operational income

All revenue and costs from non operational activities, such as items where the income is not primarily from airport users, is required to be shown in a separate category

Costs have been apportioned on a basis obtained by the analysis of 1994/95 actual expenditure

	£000	£000
AIRPORT OPERATIONAL ACTIVITIES		
Airport Income		
Airport charges	10,552	
Subsidies	14,763	
	25,315	
Costs	27,188	(1,873)
Other Income		
Revenue	1,361	
Costs	1,467	(106)
NON OPERATIONAL ACTIVITIES		
The Group has no such activities under the Act		
Group operating loss for the period		(1,979)

Unless specified elsewhere in these accounts, the Group received no preferential treatment or financial support from any associated person or organisation during the period of these accounts

GROUP FIVE YEAR SUMMARY

RESULTS TO 31 MARCH

	2006	2005	2004	2003	2002
		(As restated)	(As restated)		
	£000	£000	£000	£000	£000
PROFIT AND LOSS ACCOUNT					
Traffic operations and other income	**11,913**	10,826	9,806	9,229	9,063
Total subsidies received	**60,704**	21,505	24,545	25,149	21,963
less Capital subsidies	**45,941**	4,101	7,159	9,203	9,664
Revenue subsidies	**14,763**	17,404	17,386	15,946	12,299
less net operating costs	**28,655**	29,555	27,905	26,543	22,823
Operating (loss)	**(1,979)**	(1,325)	(713)	(1,368)	(1,461)
Share of joint venture	**(37)**				
Profit/(loss) on disposal of fixed assets	**1,155**	(22)	+	+	+
Interest receivable	**437**	407	70	64	54
Interest payable and similar charges	**(266)**				
Tax on ordinary activities	**(279)**				
(Loss) for the financial year	**(969)**	(940)	(643)	(1,304)	(1,407)

BALANCE SHEET					
Fixed assets	**60,699**	39,093	38,863	34,826	28,689
Net current assets	**3,199**	1,864	1,516	1,503	1,910
Provision for liabilities and charges	**(579)**				
Accruals and deferred income	**(58,128)**	(35,797)	(35,079)	(30,386)	(23,352)
Retirement benefits – asset (liability)	**400**	100	(2,300)	*	*
	5,591	5,260	3,000	5,943	7,247
Share capital	**50**	50	50	50	50
Reserves	**5,541**	5,210	2,950	5,893	7,197
Total shareholder's equity	**5,591**	5,260	3,000	5,943	7,247

\+ The profits/(losses) on disposal of fixed assets for 2002, 2003 and 2004 are disclosed within net operating costs

* The results for 2002 and 2003 have not been adjusted for FRS 17

	2006	2005	2004	2003	2002
STATISTICS					
Total passengers	**1,152,895**	1,015,657	933,779	864,301	832,140
Total aircraft movements	**93,234**	82,764	81,064	76,119	74,978

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF HIGHLANDS AND ISLANDS AIRPORTS LIMITED

We have audited the group and parent company financial statements (the "financial statements") of Highlands & Islands Airports Limited for the year ended 31 March 2006 which comprise the Group Profit and Loss Account, the Group and Company Balance Sheets, the Group Cash Flow Statement, the Group Statement of Total Recognised Gains and Losses and the related notes 1 to 22 These financial statements have been prepared under the accounting policies set out therein

This report is made solely to the company's members, as a body, in accordance with Section 235 of the Companies Act 1985 Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed

Respective responsibilities of directors and auditors
The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable United Kingdom law and Accounting Standards (United Kingdom Generally Accepted Accounting Practice) as set out in the Statement of Directors' Responsibilities

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland)

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985 and that the information given in the directors' report is consistent with the financial statements

We also report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed

We read other information contained in the Annual Report, and consider whether it is consistent with the audited financial statements This other information comprises only the Chairman's Statement, the Statement of Internal Control, the Economic Regulation Statement and the Group Five Year Summary We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements Our responsibilities do not extend to any other information

We review whether the statement on page 7 complies with Scottish Executive guidance on statements of system of internal control We report if it does not comply with the guidance, or if the statement is misleading or inconsistent with other information we are aware of from our audit

Basis of audit opinion
We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the group's and company's circumstances, consistently applied and adequately disclosed

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

Opinion
In our opinion

- the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the group's and the parent company's affairs as at 31 March 2006 and of the group's loss for the year then ended,
- the financial statements have been properly prepared in accordance with the Companies Act 1985,
- the information given in the directors' report is consistent with the financial statements, and
- in all material aspects, the income and expenditure presented in the financial statements have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them

Other opinion

In our opinion the Economic Regulation Statement presents fairly the information set forth therein and is in accordance with the requirements of the accounts' conditions issued by the Civil Aviation Authority under section 41(1) of the Airports Act 1986

Ernst & Young LLP

Ernst & Young LLP
Registered auditor
Inverness

12 June 2006