

Stanford University

Annual Financial Report

For the years ended August 31, 2011 and 2010

STANFORD UNIVERSITY 2011 FINANCIAL REVIEW

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DISCUSSION OF FINANCIAL RESULTS

Stanford experienced strong financial results in fiscal year 2011 (FY11), a sign of a healthy recovery from the 2008-09 financial downturn. Consolidated net assets increased \$3.7 billion to end the year at \$25.1 billion, the highest level in Stanford's history. Consolidated operating revenues exceeded expenses by \$515 million, compared to \$362 million in FY10. Stanford's FY11 financial results benefited from excellent investment returns, increases in other revenue sources, and cost-saving measures implemented in response to the recent economic downturn.

These consolidated results reflect the combined results of the University and the Hospitals. Below are additional details about the University's and Hospitals' operations and financial results.

University

During FY11, the University's financial position continued to recover from the 2008-09 financial downturn. FY11 net assets increased over \$3.1 billion to \$22.6 billion compared to \$19.4 billion in the prior year. The University's endowment rose in value by 19% over the prior year to \$16.5 billion at August 31, 2011. Donor support and investment returns were the major factors contributing to these results. Despite these positive results, the University's endowment remains 4% lower than at year-end 2008.

FY11 FINANCIAL HIGHLIGHTS

Generous support from donors. The University continues to benefit from the generous and loyal support of its donors. FY11 gifts as reported by the University Office of Development totaled \$709 million in cash or property, 18% above the prior year. These results, along with a record number of donors, are evidence of the breadth and depth of our donor support. (Gifts and pledges of \$516 million are reported in the financial statements on an accrual basis.)

As in recent years, the majority of gifts and pledges supported The Stanford Challenge, which commenced five years ago and concludes on December 31, 2011. The Stanford Challenge funds are aimed at seeking solutions to intractable global problems and educating a new generation of leaders for the complexities of today's world. Most recent fundraising efforts have been concentrated in facilities, faculty and program support, new graduate fellowships and undergraduate financial aid. With the Campaign drawing to a close, it has exceeded the original goal of \$4.3 billion.

Positive investment performance. University investment returns in FY11 were \$3.4 billion, compared to \$1.9 billion in FY10. These positive returns were achieved during another volatile year in the U.S. and international financial markets.

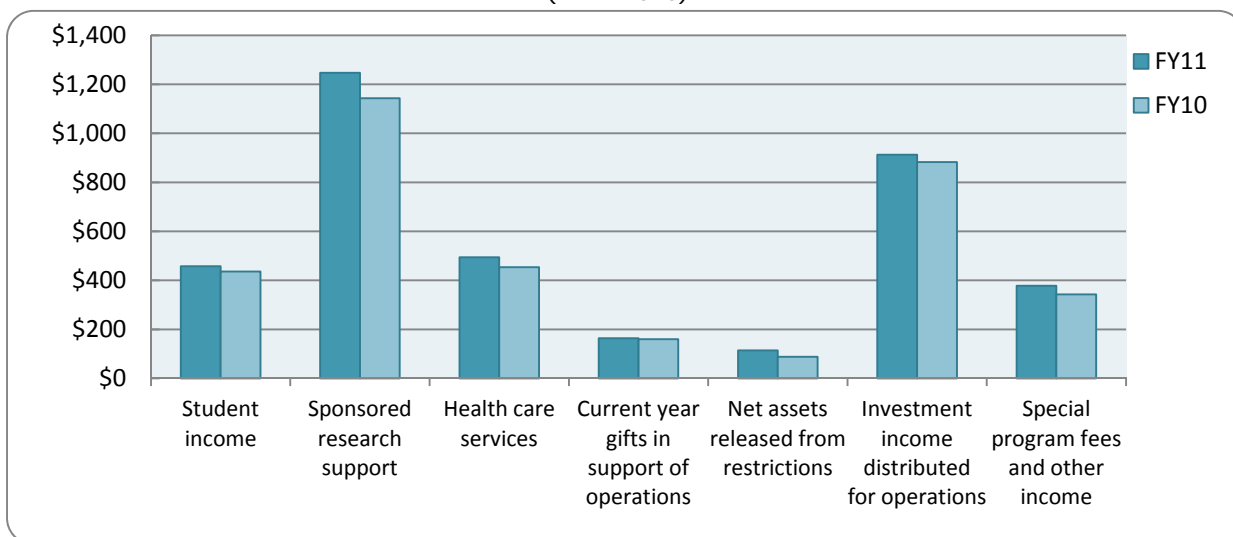
OPERATING RESULTS

The *Statements of Activities* include both results from operations and non-operating changes in the net assets of the University. Operating activities include all revenues and expenses that support current year teaching and research efforts and other University priorities.

The University ended the year with a surplus from operations of \$257 million in FY11 compared to \$210 million in FY10. FY11 operating revenues increased 7% compared to an increase in expenses of 6% during the same period.

The University's non-operating changes in net assets totaling \$2.9 billion are discussed in the *Financial Position* section of this analysis.

FIGURE 1
OPERATING REVENUES
(in millions)



OPERATING REVENUES

FY11 operating revenues were \$3.8 billion, reflecting a 7% increase over FY10. The components of the University’s operating revenues are shown above.

Student Income

Total student income, which represents 12% of University operating revenues, increased 5% to \$458 million in FY11. Total student income includes tuition and fees from undergraduate and graduate programs and room and board; this amount is offset by financial aid. Revenues from student tuition and fees increased 5% in FY11 primarily as a result of a 3.5% undergraduate and general graduate tuition increase and a slight increase in graduate student enrollment.

Financial aid increased \$9.1 million or 4% in FY11 to \$230 million, reflecting Stanford’s continued commitment to providing an affordable education for all students. Approximately 57% of undergraduate students and 81% of graduate students were awarded financial aid from Stanford, including scholarships/grants, loans and jobs in FY11.

Sponsored Research Support

Sponsored research support for the University was \$1.2 billion in FY11, increasing 9% over FY10. This category represents approximately one third of the University’s operating revenues.

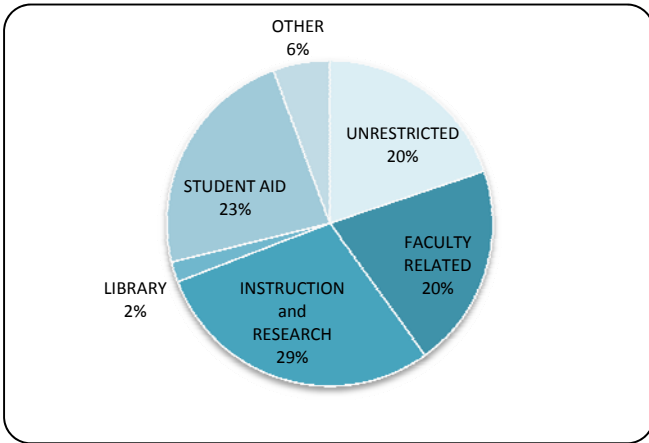
Approximately 84% of the University’s sponsored research support, including SLAC National Accelerator Laboratory (SLAC), is received directly or indirectly from the federal government. The largest federal sponsor, the Department of Health and Human Services, provided revenue of \$449 million during FY11 compared to \$401 million in the prior year. Most of these funds support research within the University’s School of Medicine.

The federal economic stimulus bill, the American Recovery and Reinvestment Act (ARRA), has been a major driver of the increase in research activity for FY11 and FY10. As of August 31, 2011, Stanford has been awarded \$308 million of ARRA funding; approximately \$131 million of this amount was spent by the University and SLAC in FY11 bringing the total amount spent to date to \$224 million.

Direct costs for SLAC increased \$34 million or 10% over FY10. This increase was largely due to increased funding for ARRA projects including infrastructure modernization and the LCLS Ultrafast Science Instrumentation (LUSI) project which will provide experimental instruments to be used with the LCLS. In addition, FY11 was the first full year of operations of the LCLS (Linac Coherent Light Source), the world’s most powerful x-ray laser.

In addition to payment for the direct costs of performing research, the University receives an amount from sponsors for facilities and administrative costs, known as indirect costs. For FY11, the federal and non-federal indirect cost recovery increased \$17 million to \$220 million as a result of higher research volume. This increase occurred despite a reduction in the indirect cost rate for new federally sponsored research from 60% in FY10 to 57% in FY11.

FIGURE 2
ENDOWMENT PAYOUT BY PURPOSE



Health Care Services

FY11 health care services revenue for the University increased \$40 million or 9% from FY10 to \$494 million and represented 13% of operating revenues.

School of Medicine faculty serve as physicians for the Hospitals. Clinical revenue is collected by the Hospitals, and a portion is remitted to the University for these physician services. In addition, the Hospitals pay the University for other essential services such as medical direction. Health care services revenues of \$472 million represent the net value of services provided by the School of Medicine to the Hospitals; these amounts are eliminated in consolidation.

THE UNIVERSITY'S ENDOWMENT

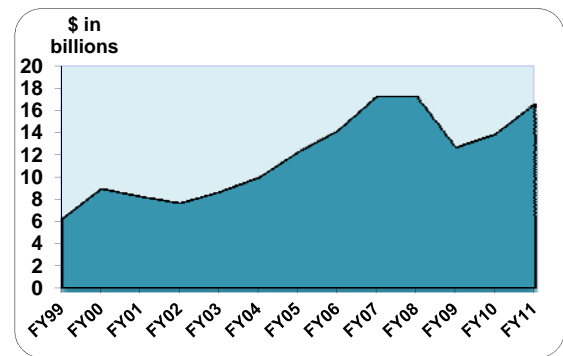
The University's endowment is a collection of gift funds and reserves which are set aside and invested to support the University's teaching and research missions. At August 31, 2011, the endowment totaled \$16.5 billion and represented approximately 73% of the University's net assets. The endowment includes pure endowment funds (which include endowed lands), term endowment funds and funds functioning as endowment.

Gifts and pledge payments, investment returns, and other invested funds increased the endowment by \$2.7 billion in FY11.

Payout to operations from the endowment continues to be a substantial source of operating revenue for the University, covering approximately 22% of expenses in FY11, down from 26% in FY10.

The University's endowment provides funding annually for a wide variety of important purposes. See Figure 2 for a distribution of endowment payout by purpose.

Approximately 29% funds instruction and research activities, 23% goes to student aid, 20% covers faculty salaries and support, 20% is unrestricted and the remainder is split between library support and other purposes.



UNIVERSITY ENDOWMENT BY YEAR

Current Year Gifts in Support of Operations and Net Assets Released from Restrictions

Current year gifts in support of operations increased 2% to \$164 million in FY11. Net assets released from restrictions increased 29% to \$114 million, due to a 34% increase in payments received on pledges and a 19% increase in prior year gifts released from restrictions for use in operations.

Total Investment Income Distributed for Operations

Total investment income distributed for operations represented 24% of University revenue, the second highest source of operating revenue for the University.

- Endowment income distributed for operations decreased to \$785 million in FY11, from \$855 million in FY10. The decrease was primarily the result of a 25% reduction in the payout from existing funds implemented following the economic downturn (10% in FY10, and an additional 15% in FY11). The endowment payout in FY11 was equal to 5.7% of the endowment value at the beginning of the fiscal year.
- Expendable funds pools and other investment income distributed for operations was \$128 million in FY11, compared to \$28 million in FY10. This category primarily includes the payout to operations from the Expendable Funds Pool (EFP) and the Endowment Income Funds Pool (EIFP), the principal investment vehicles for the University's expendable funds.
 - The EFP policy provides a variable payout to certain funds that support operations based on the prior year's investment returns. FY09 losses in the EFP significantly reduced amounts paid out to support operations in FY10. With the positive FY10 returns, payout to these funds resumed in FY11. See Note 6 to the FY11 Consolidated Financial Statements.
 - The EIFP holds endowment payout previously distributed but unexpended. These amounts are invested in highly liquid instruments in order to preserve the principal balance. Earnings on these investments are distributed to the fund holders. See Note 6 to the FY11 Consolidated Financial Statements.

OPERATING EXPENSES

Total expenses increased \$213 million, or 6%, to \$3.5 billion in FY11. Salaries and benefits comprised 62% of the University's total expenses, depreciation expense was 7% and other operating expenses represented 31%.

- Salaries and benefits increased 5% in FY11 to \$2.2 billion. Stanford implemented a modest salary program in FY11 after a salary freeze in FY 10 and the elimination of approximately 500 positions during the previous two years. Despite these cost cutting actions, FY11 headcount increased slightly to support increased sponsored research including projects funded by ARRA.
- Depreciation expense increased by 11% to \$259 million in FY11 from \$234 million in FY10. The increase in this category resulted from buildings recently placed in service, including the Knight Management Center and the William H. Neukom Building. See the **Capital Projects** section below.
- Other operating expenses increased 8% to \$1.1 billion in FY11 from \$999 million in FY10. These increases, in large part, are due to additional expenses incurred in support of higher levels of sponsored research, as described above in **Sponsored Research Support** section.

FINANCIAL POSITION

The University's *Statements of Financial Position* reflect solid investment returns and strong operating results. Total University assets increased \$3.1 billion in FY11 to end the year at \$27.7 billion. Total University liabilities were relatively unchanged at \$5.1 billion.

Cash and Cash Equivalents

The University closely monitors liquidity required to meet operating and contractual commitments. In April 2009, the University issued \$1 billion of taxable bonds, of which \$800 million in cash was set aside to ensure adequate liquidity to support University investments, capital projects and operations during the financial crisis. As economic conditions have improved, a portion of the funds has been used for other purposes, including additional capital projects and repayment of other debt. At August 31, 2011, the University's cash

position included approximately \$490 million of the April 2009 taxable bond proceeds.

Investments

Investments increased by \$3.4 billion, up 19% from FY10 due to strong investment returns and donor contributions. Alternative investments, including various types of limited partnerships, private equity funds, venture capital funds, natural resources investments, real estate and hedge funds, represent approximately 73% of total investments at August 31, 2011. The aggregate amount of unfunded commitments for alternative investments was \$3.9 billion at year-end, down significantly from approximately \$6 billion at August 31, 2008. See the Report from the Stanford Management Company for analysis of University investment strategies and performance.

Capital Projects

The University continues to invest heavily in its physical facilities to support key academic initiatives, housing and infrastructure. During FY11, the University invested \$362 million in capital projects, bringing gross plant facilities before accumulated depreciation to \$6.6 billion. Plant facilities, net of accumulated depreciation, increased \$90 million to \$3.7 billion.

Buildings completed and opened in FY11 include the Knight Management Center (the new Graduate School of Business campus) and the William H. Neukom Building in the law school. Construction began on the Bioengineering/Chemical Engineering Building, the fourth and final building in the Science and Engineering Quad 2 ("SEQ2"). Other major construction projects underway include the Bing Concert Hall and the Jill and John Freidenrich Center for Translational Research.

The University is committed to advancing sustainability in the design, construction and operation of campus facilities. University buildings use energy, water, and other natural resources efficiently and provide a safe, productive, and educational environment. Under the University's sustainability standards, new buildings include using 30% less energy and 25% less water than building codes require. The University is exploring options for a major capital utility project to reduce

overall energy consumption and use cleaner energy sources.

Debt

Total debt decreased \$89 million to \$2.7 billion as of August 31, 2011, primarily due to the maturity of \$50 million of Medium Term Notes. During FY11, Standard and Poor's, Moody's and Fitch affirmed the University's debt ratings in the highest rating categories for short and long-term debt.

The University's debt policy governs the amount and type of debt Stanford may incur and is intended to preserve debt capacity, financial flexibility and access to capital markets at competitive rates. A combination of fixed and variable rate debt, of varying maturities, is used to fund academic facilities, residential housing and dining facilities, faculty and staff mortgage loans and other infrastructure projects.

In November 2011, the University paid down \$62 million and redeemed \$50 million of tax-exempt debt with proceeds from the 2009 taxable bonds. In December 2011, the University redeemed an additional \$90 million in tax-exempt debt. See the **Cash and Cash Equivalents** section above.

Unrestricted Net Assets

In total, unrestricted net assets of the University increased \$2.1 billion to \$11.2 billion, with \$257 million resulting from operating activities. The most significant component of other changes in unrestricted net assets in FY11 was the \$1.6 billion increase in realized and unrealized investment gains. Also included in non-operating activities was \$244 million in capital and other gifts released from restrictions for assets placed in service and for operating activities.

Temporarily Restricted Net Assets

Temporarily restricted net assets increased \$716 million to \$6.2 billion in FY11. The University received \$197 million of new temporarily restricted gifts and pledges in FY11, and benefited from an \$889 million increase in realized and unrealized investment gains. Partially offsetting these increases were the \$244 million in capital and other gifts released to unrestricted net assets as described above.

Permanently Restricted Net Assets

Permanently restricted net assets increased \$300 million to \$5.1 billion during FY11. The increase was driven by \$151 million in new gifts and pledges and \$81 million of transfers from unrestricted and temporarily restricted net assets primarily due to donor redesignations and matching funds added to donor gift funds. The principal value of these assets must be invested in perpetuity to generate endowment income to be used only for the purposes designated by donors.

Hospitals

The financial results and financial position of Stanford Hospital and Clinics (SHC) and Lucile Packard Children's Hospital at Stanford (LPCH and with SHC, the Hospitals) are combined in the consolidated financial statements under the "Hospitals" column. The University is the sole member of each of the Hospitals.

In FY11, the Hospitals received local government approval to rebuild and expand their principal facilities. Based on current estimates, management expects construction of these facilities to be completed by 2017. These projects will assure that the Hospitals have adequate inpatient capacity in modern, technologically-advanced facilities, and meet State-mandated earthquake safety standards and deadlines. The total estimated cost, inclusive of owner's reserves, is approximately \$2.0 billion for SHC and \$1.2 billion for LPCH.

The following discussion summarizes the individual financial results of SHC and LPCH as shown in the Consolidated Financial Statements.

Stanford Hospital and Clinics

SHC continued to show solid operating results in FY11 generating income from operations of \$173 million compared to \$100 million for FY10. An increase in operating margin is mainly due to overall strong volume growth and partly due to expense containment measures implemented during FY11. Net assets grew by \$427 million, or 48%, to \$1.3 billion mainly due to strong operating performance, financial market performance and philanthropy.

Operating Results

Operating revenues increased by 11% to \$2.2 billion primarily due to a 12% increase in patient revenues to \$2.1 billion. Both inpatient and outpatient revenues grew significantly due to overall strong volume growth and increased commercial payer mix. Net revenues over expenses of \$8 million from the Hospital Quality Assurance Fee (QAF) Program and Hospital Fee Program—programs which provide supplemental payments to certain hospitals for Medi-Cal patients—contributed to this result as well.

Operating expenses increased 8% to \$2.0 billion in FY11. Salaries and benefits grew by 6% to \$890 million primarily in response to growth in patient volumes and to maintain SHC's position in the competitive market for health care professionals. Physicians' services and support increased by 8% to \$338 million largely due to increased outpatient activities in FY11.

Depreciation and other operating expenses were up by 10% to \$790 million primarily as a result of costs related to the increase in patient activity, QAF expenses, enhanced IT infrastructure and other SHC initiatives.

Statement of Financial Position (Balance Sheet)

SHC's *Statement of Financial Position* reflects continued investments in the facilities and systems required to remain at the forefront of medicine and to be the provider of choice for complex care in the communities it serves. Gross property and equipment increased \$80 million to \$1.7 billion during FY11. As of August 31, 2011, SHC had recorded \$149 million in construction in progress related to rebuilding its principal facilities.

In FY11, SHC completed a restructuring and reoffering of bonds in the amount of \$272 million as part of SHC's strategy to reduce risk in its debt portfolio in preparation for financing a portion of the costs of its major facilities replacement project.

Other SHC highlights

SHC recently launched the Corporate Partners Program ("CPP"). CPP is a partnership between SHC and top Silicon Valley firms which

management anticipates will provide substantial philanthropic support for the construction of new hospital facilities. SHC also engages in numerous community benefit programs and services. These services include health research, education and training and other community benefits for the larger community. Charity care and uncompensated costs including services to patients under Medi-Cal and Medicare that reimburse at amounts less than the cost of services provided to the recipients, were \$205 million in FY11.

Lucile Packard Children's Hospital at Stanford

Despite the challenges of the economy, which have resulted in lower births, and state budget issues, LPCH had a strong FY11, resulting in an excess of revenue over expenses of \$170 million, an increase of \$63 million or 59% over FY10. Net assets at August 31, 2011 were \$1.2 billion, reflecting an increase of \$155 million over FY10. Strong operating results, investment income and gains from the University's Merged Pool, and donor contributions contributed to this result.

Operating Results

Income from operations was \$92 million in FY11, an increase of \$40 million or 77% from FY10. Net revenues over expenses of \$33 million from the Hospital Quality Assurance Fee (QAF) Program and Hospital Fee Program—programs which provide supplemental payments to certain hospitals for Medi-Cal patients—contributed to this result.

Total operating revenues in FY11 were \$924 million, a 15% increase over FY10. Net patient revenues also grew 15% to \$871 million in FY11 reflecting an increase in acuity of the patients, higher commercial contract rates, significant stop-loss reimbursement and funding from the QAF Program.

Operating expenses grew by 11% in FY11. Higher labor costs (44% of total expense), services purchased from the University, and fees paid as part of the QAF drove this increase. Labor costs increased 8% in FY11 due to higher salaries commanded in the competitive market for health care professionals, an increase in

benefit costs, and an increase in needed temporary labor.

Statement of Financial Position (Balance Sheet)

LPCH's *Statement of Financial Position* reflects investment growth resulting from investment income and gains and donor contributions as well as continued investments in its facilities to expand capacity and to provide modern, technologically-advanced hospital services. Property and equipment, net of depreciation, increased \$37 million to \$460 million during FY11. As of August 31, 2011, LPCH had recorded \$98 million in construction in progress related to expanding its principal facilities.

Other LPCH Highlights

LPCH's community benefits, including services to patients under Medi-Cal and other publicly sponsored programs that reimburse at amounts less than the cost of services provided to the recipients, were \$164 million in FY11 compared with \$135 million in FY10. The increase was due to increases in Medi-Cal utilization, costs exceeding the related contract increases, and uncompensated care. In addition, LPCH also invests in improving the health of the children of San Mateo and Santa Clara counties through a range of community-based programs.

Health Care Reform

In March 2010, the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 (the "Acts") were signed into law. These Acts broadly affect the health care industry, including a significant expansion of health care coverage. Some provisions were effective immediately; others will be phased in through 2014 and later years. The impacts of these Acts will significantly affect SHC and LPCH.

LOOKING FORWARD

With the FY11 financial results, including the growth in the endowment and net assets, Stanford enters FY12 in a solid financial position. Additionally, the existing physical infrastructure, along with plans currently underway for new buildings, the rebuilding and expansion of the Hospitals, and other projects, position us well to

advance our mission of teaching, research and patient care. Our financial resources provide a strong foundation that will enable us to explore and fund strategic academic and research opportunities and to address important administrative and infrastructure needs.

Despite the very positive FY11 results, Stanford has not lost sight of the impending risks ahead: the outlook for federal research funding remains uncertain, investment markets remain volatile due to continued global economic malaise, and health

care reform is upon us. The need for financial aid is also expected to continue increasing as many of our students and their families experience additional financial pressures. We remain mindful of the recent economic events and challenges ahead. We plan to approach FY12 and beyond cautiously yet opportunistically.

The continued commitment and support of the Stanford community, including the students, alumni and friends, faculty and staff, provides the strength and resources to guide us through future challenges. For this we are grateful.



Randall S. Livingston
Vice President for Business Affairs and
Chief Financial Officer
Stanford University



M. Suzanne Calandra
Senior Associate Vice President for Finance
Stanford University



Daniel J. Morissette
Chief Financial Officer
Stanford Hospital and Clinic



Timothy W. Carmack
Chief Financial Officer
Lucile Salter Packard Children's Hospital
at Stanford

SELECTED FINANCIAL AND OTHER DATA

Fiscal Years Ended August 31

	2011	2010	2009	2008	2007
	(dollars in millions)				
CONSOLIDATED STATEMENT OF ACTIVITIES HIGHLIGHTS:					
Total Revenues	\$ 6,381	\$ 5,785	\$ 5,602	\$ 5,403	\$ 4,877
Student income (A)	458	436	401	405	394
Sponsored research support	1,247	1,143	1,031	1,076	1,058
Health care services	2,994	2,620	2,424	2,193	1,996
Total Expenses	5,866	5,423	5,093	4,957	4,467
Excess of revenues over expenses	515	362	509	446	410
Other changes in net assets	3,194	1,131	(5,450)	471	3,647
Net change in total net assets	\$ 3,709	\$ 1,493	\$ (4,941)	\$ 917	\$ 4,057
CONSOLIDATED STATEMENT OF FINANCIAL POSITION HIGHLIGHTS:					
University					
Investments at fair value	\$ 21,189	\$ 17,804	\$ 16,501	\$ 21,758	\$ 21,167
Plant facilities, net of accumulated depreciation	3,674	3,584	3,270	2,887	2,706
Notes and bonds payable	2,727	2,816	2,517	1,532	1,494
Total assets	27,698	24,553	22,672	26,704	25,888
Total liabilities	5,143	5,118	4,633	4,013	3,930
Total net assets	22,555	19,435	18,039	22,691	21,958
Hospitals					
Investments at fair value	1,796	1,359	1,257	1,712	1,952
Plant facilities, net of accumulated depreciation	1,333	1,283	1,260	1,080	766
Notes and bonds payable	983	992	999	1,007	1,015
Total assets	4,283	3,658	3,472	3,670	3,402
Total liabilities	1,722	1,686	1,597	1,506	1,422
Total net assets	2,561	1,972	1,875	2,164	1,980
OTHER UNIVERSITY FINANCIAL DATA AND METRICS:					
Total endowment at year end	\$ 16,503	\$ 13,851	\$ 12,619	\$ 17,214	\$ 17,165
Endowment payout in support of operations	785	855	957	882	609
As a % of beginning of year endowment	5.7%	6.8%	5.6%	5.1%	4.3%
As a % of total expenses	22.4%	25.9%	30.6%	27.8%	21.0%
Total gifts (B)	709	599	640	785	832
STUDENTS:					
ENROLLMENT: (C)					
Undergraduate	6,927	6,887	6,878	6,812	6,759
Graduate	8,796	8,779	8,441	8,328	8,186
DEGREES CONFERRED:					
Bachelor degrees	1,670	1,671	1,680	1,646	1,709
Advanced degrees	3,199	3,046	2,932	2,928	3,100
FACULTY:					
Total Professoriate	1,903	1,910	1,876	1,829	1,807
ANNUAL UNDERGRADUATE TUITION RATE (IN DOLLARS)	\$ 38,700	\$ 37,380	\$ 36,030	\$ 34,800	\$ 32,994

(A) Financial aid is reported as a reduction of student income in the Statement of Activities.

(B) As reported by the Office of Development (See Note 14). Beginning in 2009, reported amounts include SHC gifts.

(C) Enrollment for fall quarter immediately following fiscal year end.

MANAGEMENT RESPONSIBILITY FOR FINANCIAL STATEMENTS

The University is the sole member of Stanford Hospital and Clinics and Lucile Packard Children's Hospital at Stanford; however, each of the Hospitals has its own separate management with responsibility for its own financial reporting.

Management of the University and the Hospitals is responsible for the integrity and objectivity of their respective portions of these financial statements. The University oversees the process of consolidating the Hospitals' information into the consolidated financial statements. Management of each entity represents that, with respect to its financial information, the consolidated financial statements in this annual report have been prepared in conformity with generally accepted accounting principles in the United States.

In accumulating and controlling financial data, management of the University and the Hospitals maintains separate systems of internal accounting controls. Management of the respective entities believes that effective internal controls are maintained and communication of accounting and business policies, by selection and training of qualified personnel and by programs of internal audits, give reasonable assurance, at reasonable cost, that assets are protected and that transactions and events are recorded properly.

The accompanying consolidated financial statements have been audited by the University's and Hospitals' independent auditors, PricewaterhouseCoopers LLP. Their report expresses an informed judgment as to whether the consolidated financial statements, considered in their entirety, present fairly, in conformity with generally accepted accounting principles in the United States, the consolidated financial position and changes in net assets and cash flows. The independent auditors' opinion is based on audit procedures described in their report, which include obtaining an understanding of systems, procedures and internal accounting controls, and performing tests and other audit procedures to provide reasonable assurance that the financial statements are neither materially misleading nor contain material errors. While the independent auditors test procedures and controls, it is neither practical nor necessary for them to scrutinize a large portion of transactions.

The Board of Trustees of the University and the separate Boards of Directors of the Hospitals, through their respective Audit Committees, comprised of trustees and directors not employed by the University or the Hospitals, are responsible for engaging the independent auditors and meeting with management, internal auditors and the independent auditors to independently assess whether each is carrying out its responsibility and to discuss auditing, internal control and financial reporting matters. Both the internal auditors and the independent auditors have full and free access to the respective Audit Committees. Both meet with the respective Audit Committees at least annually, with and without each other, and without the presence of management representatives.



Randall S. Livingston
Vice President for Business Affairs
and Chief Financial Officer
Stanford University



M. Suzanne Calandra
Senior Associate Vice President for Finance
Stanford University



Daniel J. Morissette
Chief Financial Officer
Stanford Hospital and Clinics



Timothy W. Carmack
Chief Financial Officer
Lucile Salter Packard Children's Hospital
at Stanford



Report of Independent Auditors

To the Board of Trustees
Stanford University

In our opinion, the accompanying consolidated statements of financial position and the related consolidated statements of activities and cash flows present fairly, in all material respects, the financial position of Stanford University (the "University") at August 31, 2011 and 2010, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

December 14, 2011

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

At August 31, 2011 and 2010 (in thousands of dollars)

	2011			2010
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
ASSETS				
Cash and cash equivalents	\$ 1,186,257	\$ 507,958	\$ 1,694,215	\$ 2,020,803
Accounts receivable, net	253,321	449,688	703,009	626,974
Receivables (payables) from SHC and LPCH, net	60,566	(60,566)	-	-
Prepaid expenses and other assets	63,194	92,569	155,763	147,513
Pledges receivable, net	729,253	165,441	894,694	869,169
Student loans receivable, net	75,722	-	75,722	74,997
Faculty and staff mortgages and other loans receivable, net	465,344	-	465,344	442,764
Investments at fair value, including securities pledged or on loan of \$125,033 and \$118,053 for 2011 and 2010, respectively	21,189,487	1,795,710	22,985,197	19,162,619
Plant facilities, net of accumulated depreciation	3,674,383	1,332,724	5,007,107	4,866,662
Works of art and special collections	-	-	-	-
TOTAL ASSETS	\$ 27,697,527	\$ 4,283,524	\$ 31,981,051	\$ 28,211,501
LIABILITIES AND NET ASSETS				
LIABILITIES:				
Accounts payable and accrued expenses	\$ 512,841	\$ 597,804	\$ 1,110,645	\$ 1,063,010
Accrued pension and post retirement benefit cost	521,507	141,439	662,946	721,695
Pending trades of securities	209,683	-	209,683	135,345
Liabilities under security lending agreements	182,027	-	182,027	160,024
Deferred rental and other income	548,363	-	548,363	526,237
Income beneficiary share of split interest agreements	387,947	-	387,947	335,975
Notes and bonds payable	2,726,607	983,178	3,709,785	3,808,347
U.S. government refundable loan funds	53,760	-	53,760	53,485
TOTAL LIABILITIES	5,142,735	1,722,421	6,865,156	6,804,118
NET ASSETS:				
Unrestricted	11,235,457	2,000,964	13,236,421	10,677,519
Temporarily restricted	6,243,177	354,789	6,597,966	5,722,099
Permanently restricted	5,076,158	205,350	5,281,508	5,007,765
TOTAL NET ASSETS	22,554,792	2,561,103	25,115,895	21,407,383
TOTAL LIABILITIES AND NET ASSETS	\$ 27,697,527	\$ 4,283,524	\$ 31,981,051	\$ 28,211,501

The accompanying notes are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENTS OF ACTIVITIES

For the years ended August 31, 2011 and 2010 (in thousands of dollars)

	2011			2010
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
UNRESTRICTED NET ASSETS				
REVENUES:				
Student income:				
Undergraduate programs	\$ 285,582	\$ -	\$ 285,582	\$ 274,943
Graduate programs	274,784	-	274,784	260,302
Room and board	127,785	-	127,785	122,469
Student financial aid	(230,307)	-	(230,307)	(221,236)
TOTAL STUDENT INCOME	457,844	-	457,844	436,478
Sponsored research support:				
Direct costs - University	660,684	-	660,684	606,921
Direct costs - SLAC National Accelerator Laboratory	366,435	-	366,435	332,767
Indirect costs	220,248	-	220,248	202,974
TOTAL SPONSORED RESEARCH SUPPORT	1,247,367	-	1,247,367	1,142,662
Health care services:				
Patient care, net	-	2,972,208	2,972,208	2,603,046
Physicians' services and support - SHC and LPCH, net	471,779	(471,779)	-	-
Physicians' services and support - other facilities, net	22,033	-	22,033	17,245
TOTAL HEALTH CARE SERVICES	493,812	2,500,429	2,994,241	2,620,291
CURRENT YEAR GIFTS IN SUPPORT OF OPERATIONS	163,692	6,959	170,651	165,417
Net assets released from restrictions:				
Payments received on pledges	83,487	1,640	85,127	62,678
Prior year gifts released from donor restrictions	30,190	865	31,055	29,462
TOTAL NET ASSETS RELEASED FROM RESTRICTIONS	113,677	2,505	116,182	92,140
Investment income distributed for operations:				
Endowment	785,081	13,977	799,058	871,431
Expendable funds pools and other investment income	127,626	830	128,456	28,342
TOTAL INVESTMENT INCOME DISTRIBUTED FOR OPERATIONS	912,707	14,807	927,514	899,773
SPECIAL PROGRAM FEES AND OTHER INCOME	377,738	90,029	467,767	428,178
TOTAL REVENUES	3,766,837	2,614,729	6,381,566	5,784,939
EXPENSES:				
Salaries and benefits	2,173,649	1,274,962	3,448,611	3,241,407
Depreciation	258,889	135,516	394,405	368,019
Other operating expenses	1,077,541	945,749	2,023,290	1,813,662
TOTAL EXPENSES	3,510,079	2,356,227	5,866,306	5,423,088
EXCESS OF REVENUES OVER EXPENSES	\$ 256,758	\$ 258,502	\$ 515,260	\$ 361,851

The accompanying notes are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENTS OF ACTIVITIES

For the years ended August 31, 2011 and 2010 (in thousands of dollars)

	2011			2010
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
UNRESTRICTED NET ASSETS (continued)				
EXCESS OF REVENUES OVER EXPENSES	\$ 256,758	\$ 258,502	\$ 515,260	\$ 361,851
Other changes in unrestricted net assets:				
Increase in reinvested gains	1,559,542	202,816	1,762,358	741,106
Donor advised funds, net	1,057	-	1,057	35,444
Current year gifts not included in operations	4,237	-	4,237	1,238
Equity and fund transfers from Hospitals, net	31,053	(31,053)	-	-
Capital and other gifts released from restrictions	243,798	5,123	248,921	156,164
Pension and other post employment benefit related changes				
other than net periodic benefit expense	82,555	14,826	97,381	(131,235)
Transfer to permanently restricted net assets, net	(56,247)	-	(56,247)	(18,620)
Transfer to temporarily restricted net assets, net	(16,121)	-	(16,121)	(13,165)
Swap interest and unrealized gains (losses)	(1,947)	672	(1,275)	(102,544)
Loss on extinguishment of debt	-	-	-	(12,994)
Other	(1,072)	4,403	3,331	784
NET CHANGE IN UNRESTRICTED NET ASSETS	2,103,613	455,289	2,558,902	1,018,029
TEMPORARILY RESTRICTED NET ASSETS				
Gifts and pledges, net	196,615	147,144	343,759	227,313
Increase in reinvested gains	889,161	43,182	932,343	469,723
Change in value of split interest agreements, net	132	(372)	(240)	11,907
Net assets released to operations	(113,677)	(24,271)	(137,948)	(114,642)
Capital and other gifts released to unrestricted net assets	(243,798)	(5,123)	(248,921)	(156,164)
Gift transfers to Hospitals, net	(1,233)	1,233	-	-
Transfer from unrestricted net assets, net	16,121	-	16,121	13,165
Transfer from (to) permanently restricted net assets, net	(24,810)	510	(24,300)	(11,503)
Other	(2,169)	(2,778)	(4,947)	(24,865)
NET CHANGE IN TEMPORARILY RESTRICTED NET ASSETS	716,342	159,525	875,867	414,934
PERMANENTLY RESTRICTED NET ASSETS				
Gifts and pledges, net	150,813	34	150,847	107,497
Increase (decrease) in reinvested gains	15,150	-	15,150	(101,249)
Change in value of split interest agreements, net	25,862	929	26,791	23,944
Fund transfers from Hospitals, net	27,293	(27,293)	-	-
Transfer from unrestricted net assets, net	56,247	-	56,247	18,620
Transfer from (to) temporarily restricted net assets, net	24,810	(510)	24,300	11,503
Other	(259)	667	408	-
NET CHANGE IN PERMANENTLY RESTRICTED NET ASSETS	299,916	(26,173)	273,743	60,315
NET CHANGE IN TOTAL NET ASSETS	3,119,871	588,641	3,708,512	1,493,278
Total net assets, beginning of year	19,434,921	1,972,462	21,407,383	19,914,105
TOTAL NET ASSETS, END OF YEAR	\$ 22,554,792	\$ 2,561,103	\$ 25,115,895	\$ 21,407,383

The accompanying notes are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the years ended August 31, 2011 and 2010 (in thousands of dollars)

	2011			2010
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
CASH FLOW FROM OPERATING ACTIVITIES				
Change in net assets	\$ 3,119,871	\$ 588,641	\$ 3,708,512	\$ 1,493,278
Adjustments to reconcile change in net assets to net cash provided by (used for) operating activities:				
Depreciation	258,889	135,516	394,405	368,019
Amortization, loss on disposal of fixed assets and other adjustments	19,347	(321)	19,026	17,338
Net gains on investments and security agreements	(3,230,140)	(190,255)	(3,420,395)	(1,779,897)
Net (gains) losses on derivatives	(3,645)	-	(3,645)	96,819
Changes in split interest agreements	46,312	(557)	45,755	(82,581)
Investment income for restricted purposes	(10,625)	(27,173)	(37,798)	(12,573)
Gifts restricted for long-term investments	(160,700)	(131,445)	(292,145)	(184,112)
Equity and fund transfers from Hospitals	(57,113)	57,113	-	-
Gifts of securities and properties	(51,904)	-	(51,904)	(106,257)
Loss on extinguishment of debt	-	-	-	12,994
Premiums received from bond issuance	-	1,534	1,534	50,492
Changes in operating assets and liabilities:				
Accounts receivable, pledges receivable and receivables from SHC and LPCH, net	(26,759)	(77,245)	(104,004)	3,955
Prepaid expenses and other assets	18,833	(23,685)	(4,852)	(46,094)
Accounts payable and accrued expenses	14,097	60,438	74,535	29,531
Accrued pension and post retirement benefit costs	(32,861)	(25,888)	(58,749)	160,643
Deferred rental and other income	22,126	-	22,126	(7,923)
Other	-	(10,649)	(10,649)	4,306
NET CASH PROVIDED BY (USED FOR) OPERATING ACTIVITIES	(74,272)	356,024	281,752	17,938
CASH FLOW FROM INVESTING ACTIVITIES				
Land, building and equipment purchases	(396,370)	(170,931)	(567,301)	(702,562)
Student, faculty and other loans:				
New loans made	(76,749)	-	(76,749)	(66,751)
Principal collected	48,996	-	48,996	38,635
Purchases of investments	(17,816,631)	(241,206)	(18,057,837)	(8,927,979)
Sales and maturities of investments	17,891,599	22,174	17,913,773	9,645,968
NET CASH USED FOR INVESTING ACTIVITIES	(349,155)	(389,963)	(739,118)	(12,689)
CASH FLOW FROM FINANCING ACTIVITIES				
Gifts and reinvested income for restricted purposes	152,527	50,988	203,515	157,707
Equity and fund transfers from Hospitals	22,861	(22,861)	-	-
Proceeds from borrowing	250	272,365	272,615	604,165
Bond issuance costs and interest rate swaps	(11)	(1,802)	(1,813)	(5,414)
Repayment of notes and bonds payable	(82,452)	(283,410)	(365,862)	(430,130)
Increase (decrease) in liabilities under security lending agreements	22,003	-	22,003	(88,024)
Other	275	45	320	(4,024)
NET CASH PROVIDED BY FINANCING ACTIVITIES	115,453	15,325	130,778	234,280
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(307,974)	(18,614)	(326,588)	239,529
Cash and cash equivalents, beginning of year	1,494,231	526,572	2,020,803	1,781,274
CASH AND CASH EQUIVALENTS, END OF YEAR	\$ 1,186,257	\$ 507,958	\$ 1,694,215	\$ 2,020,803
SUPPLEMENTAL DATA:				
Interest paid during the year	\$ 108,767	\$ 49,243	\$ 158,010	\$ 145,315
Cash collateral received under security lending agreements	\$ 142,963	\$ -	\$ 142,963	\$ 122,566
Increase in payables for plant facilities	\$ 34,643	\$ 14,732	\$ 49,375	\$ (10,122)

The accompanying notes are an integral part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation and Significant Accounting Policies

BASIS OF PRESENTATION

The consolidated financial statements include the accounts of Stanford University (the “University”), Stanford Hospital and Clinics (SHC), Lucile Salter Packard Children’s Hospital at Stanford (LPCH) and other majority-owned or controlled entities. All significant inter-entity transactions and balances have been eliminated upon consolidation. Certain prior year amounts have been reclassified to conform to the current year’s presentation. These reclassifications had no impact on the change in net assets or total net assets.

University

The University is a private, not-for-profit educational institution, founded in 1885 by Senator Leland and Mrs. Jane Stanford in memory of their son, Leland Stanford Jr. A Board of Trustees (the “Board”) governs the University. The “University” category presented in the consolidated financial statements comprises all of the accounts of the University, including the Hoover Institution and other institutes and research centers, and the Stanford Management Company.

SLAC National Accelerator Laboratory (SLAC) is a federally funded research and development center owned by the Department of Energy (DOE). The University manages and operates SLAC for the DOE under a management and operating contract; accordingly, the revenues and expenditures of SLAC are included in the University’s *Statements of Activities*, but SLAC’s assets and liabilities are not included in the University’s *Statements of Financial Position*. SLAC employees are University employees and participate in the University’s employee benefit programs. The University holds some receivables from the DOE substantially related to reimbursement for employee compensation and benefits.

Hospitals

The health care activities of SHC and LPCH (the “Hospitals”), including revenues, expenses, assets and liabilities, are consolidated into these financial statements. Each of the Hospitals is a California not-for-profit public benefit corporation. The University is the sole member of each of the Hospitals. The Hospitals support the mission of medical education and clinical research of the University’s School of Medicine. They operate two licensed acute care and specialty hospitals on the Stanford campus and numerous physician clinics on the campus, in community settings and in association with regional hospitals in the San Francisco Bay Area and elsewhere in California. The Hospitals jointly control a captive insurance company.

Each of the Hospitals prepares separate, stand-alone financial statements. For purposes of presentation of the Hospitals’ balance sheets, statements of operations and changes in net assets and statements of cash flows in these consolidated financial statements, conforming reclassifications have been made to the Hospitals’ revenues, expenses, investment income and inter-entity receivables and payables consistent with categories in these consolidated financial statements.

TAX STATUS

The University and the Hospitals are exempt from federal and state income taxes to the extent provided by Section 501(c)(3) of the Internal Revenue Code and equivalent state provisions.

BASIS OF ACCOUNTING

The consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States ("U.S. GAAP"). These principles require management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

For financial reporting purposes, net assets and revenues, expenses, gains and losses are classified into one of three categories - unrestricted, temporarily restricted or permanently restricted.

Unrestricted Net Assets

Unrestricted net assets are expendable resources used to support the University's core activities of teaching and research or the Hospitals' patient care, teaching and research missions. Unrestricted net assets include funds designated for operations, net investment in plant facilities, certain investment and endowment gains and funds functioning as endowment. These net assets may be designated by the University or the Hospitals for specific purposes under internal operating and administrative arrangements or be subject to contractual agreements with external parties. Donor-restricted contributions that relate to the University's or the Hospitals' core activities and are received and expended or deemed expended based on the nature of donors' restrictions are classified as unrestricted. All expenses are recorded as a reduction of unrestricted net assets.

Management considers all revenues and expenses to be related to operations. Increases or decreases in reinvested gains, swap interest and unrealized gains or losses, donor advised funds, capital and other gifts released from restrictions, equity and fund transfers from the Hospitals, amounts transferred to other net asset categories, pension and other post employment benefit related changes other than net periodic benefit expense and certain other non-operating changes are reported in the *Statements of Activities* as "other changes in unrestricted net assets".

Transfers from unrestricted net assets to temporarily restricted net assets and permanently restricted net assets are primarily the result of donor redesignations or matching funds that are added to donor gift funds and then take on the same restrictions as the donor gift.

Temporarily Restricted Net Assets

Temporarily restricted net assets include gifts and pledges that are subject to donor-imposed restrictions that expire with the passage of time, payment of pledges or specific actions to be undertaken by the University or the Hospitals, which are then released and reclassified to unrestricted net assets. In addition, appreciation and income on certain donor-restricted endowment funds are classified as temporarily restricted net assets until authorized for spending (see *Notes 12 and 13*). Donor-restricted resources intended for capital projects are initially recorded as temporarily restricted and released from their temporary restrictions and reclassified as unrestricted net assets when the asset is placed in service. Also included in this category is the University's net equity in split interest agreements that are expendable at maturity.

Permanently Restricted Net Assets

Permanently restricted net assets consist primarily of endowment, annuity and life income funds which are subject to donor-imposed restrictions requiring that the principal be invested in perpetuity.

Permanently restricted net assets may also include funds reclassified from other classes of net assets as a result of donor-imposed stipulations, the University's net equity in split interest agreements that are not expendable at maturity and net assets which by donor stipulation must be made available in perpetuity for specific purposes.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents included in the *Statements of Financial Position* consist of U.S. Treasury bills, commercial paper, certificates of deposit, money market funds and all other short-term investments with original maturities of 90 days or less at the time of purchase. These amounts are carried at cost, which approximates fair value. Cash and cash equivalents that are held for investment purposes are classified as investments (see *Note 5*).

ACCOUNTS AND LOANS RECEIVABLE

Accounts and loans receivable are carried at cost, less an allowance for doubtful accounts.

PLEDGES RECEIVABLE

Unconditional promises to give are included in the consolidated financial statements as pledges receivable and are classified as temporarily restricted or permanently restricted, depending upon donor stipulations. Pledges recognized on or after September 1, 2008 are recorded at an applicable risk-adjusted discount rate commensurate with the duration of the donor's payment plan. Pledges recognized in periods prior to September 1, 2008 were recorded at a discount based on the U.S. Treasury rate. Conditional promises, which depend on the occurrence of a specified future and uncertain event, such as matching gifts from other donors, are recognized when the conditions are substantially met.

INVESTMENTS

Investments are recorded at fair value. Gains and losses (realized and unrealized) on investments are recognized in the *Statements of Activities* (see *Note 5*).

The investment portfolio may be exposed to various risks, including, but not limited to, interest rate, market, sovereign, concentration, counterparty, liquidity and credit risk. Fair value reporting requires management to make estimates and assumptions about the effects of matters that are inherently uncertain. Estimates developed using methods such as discounted cash flow are subjective, requiring significant judgments such as the amount and timing of future cash flows and the selection of appropriate discount rates that reflects market and credit risks. The University and the Hospitals regularly assess these risks through established policies and procedures. Actual results could differ from these estimates and such differences could have a material impact on the consolidated financial statements.

PLANT FACILITIES

Plant facilities are recorded at cost or, for donated assets, at fair value at the date of donation. Interest expense for construction financing, net of income earned on unspent proceeds, is capitalized as a cost of construction. Depreciation is computed using the straight-line method over the estimated useful lives of the assets.

The useful lives used in calculating depreciation for the years ended August 31, 2011 and 2010 are as follows:

	UNIVERSITY	HOSPITALS
Land improvements	10-25 years	10-25 years
Buildings and building improvements	4-50 years	7-40 years
Furniture, fixtures and equipment	3-10 years	3-20 years

WORKS OF ART AND SPECIAL COLLECTIONS

Works of art, historical treasures, literary works and artifacts, which are preserved and protected for educational, research and public exhibition purposes, are not capitalized. Donations of such collections are not recorded for financial statement purposes; however, purchases of such collections are recorded as operating expenses in the period in which they are acquired.

DONATED ASSETS

Donated assets, other than works of art and special collections as discussed above, are recorded at fair value at the date of donation. Undeveloped land, including land acquired under the original endowment from Senator Leland and Mrs. Jane Stanford, is reported at fair value at the date of acquisition. Under the terms of the original founding grant, a significant portion of University land may not be sold.

DONOR ADVISED FUNDS

The University receives gifts from donors under donor advised fund (DAF) agreements. These funds are owned and controlled by the University and are separately identified by donor. A substantial portion of the gift must be designated to the University. The balance may be used to support other approved charities. The donors have advisory privileges with respect to the distribution of certain amounts in the funds. Current year gifts under the DAF agreements are included in the *Statements of Activities* as "other changes in unrestricted net assets" at the full amount of the gift. Transfers of funds to other charitable organizations are included in the *Statements of Activities* as a reduction to "other changes in unrestricted net assets" at the time the transfer is made. At August 31, 2011 and 2010, approximately \$207.3 million and \$178.5 million, respectively, of DAFs are not designated to the University.

SPLIT INTEREST AGREEMENTS

Split interest agreements consist of arrangements with donors where the University and the Hospitals have an interest in assets held by the trustee and receive benefits that are shared with other beneficiaries. Split interest agreements where the University and the Hospitals are not the trustee are recorded in the "assets held by other trustees" category of "investments" in the *Statements of Financial Position* as described in *Note 5*.

The assets held under split interest agreements where the University is the trustee were \$628.7 million and \$571.2 million, respectively, at August 31, 2011 and 2010 and were recorded in various categories in "investments" and the discounted present value of any income beneficiary interest is reported as "income beneficiary share of split interest agreements" in the *Statements of Financial Position*. The discount rates used, which range from 3% to 6%, are established in the year the gift was received and are based on tables established by the Internal Revenue Service.

During fiscal years 2011 and 2010, the discounted present value of new gifts subject to split interest agreements where the University is the trustee, net of the income beneficiary share, were \$18.1 million and \$8.7 million, respectively, and were included in "gifts and pledges, net" in the *Statements of Activities*. Actuarial gains or losses are included in "change in value of split interest agreements, net" in the *Statements of Activities*.

Funds subject to donor-imposed restrictions requiring that the principal be invested in perpetuity are classified as "permanently restricted net assets" in the *Statements of Financial Position*; all others are classified as "temporarily restricted net assets" until the expiration of the donor-imposed restrictions, at which point they will be classified as "unrestricted net assets."

SELF-INSURANCE

The University self-insures at varying levels for unemployment, disability, workers' compensation, property losses, certain health care plans and general and professional liability losses. The Hospitals self-insure at varying levels for health care plans, workers' compensation and, through their captive insurance company, for professional liability losses. Third-party insurance is purchased to cover liabilities above the self-insurance limits. Estimates of retained exposures are accrued.

INTEREST RATE EXCHANGE AGREEMENTS

The University and the Hospitals have entered into several interest rate exchange agreements to reduce the effect of interest rate fluctuation on their variable rate revenue notes and bonds (VRDBs). Current accounting guidance for derivatives and hedges requires entities to recognize all derivative instruments at fair value. The University and the Hospitals do not designate and qualify their derivatives for hedge accounting; accordingly, any changes in the fair value (i.e. gains or losses) flow directly to the *Statements of Activities* in "swap interest and unrealized gains (losses)". The settlements (net cash payments less receipts) under the interest rate exchange agreements are recorded in the *Statements of Activities* in "swap interest and unrealized gains (losses)" for the University and in "other operating expenses" for the Hospitals.

STUDENT INCOME

Financial assistance in the form of scholarship and fellowship grants that cover a portion of tuition, living and other costs is reflected as a reduction of student income.

PATIENT CARE AND OTHER SERVICES

Health Care Services

The Hospitals derive a majority of patient care revenues from contractual agreements with third-party payers including Medicare, Medi-Cal and other payers. Payments under these agreements and programs are based on a variety of payment models such as per diem, per discharge, per service, a fee schedule, cost reimbursement or negotiated rates. "Patient care, net" is reported in the *Statements of Activities* at the estimated net realizable amounts from patients, third-party payers, and others for services rendered, including estimated retroactive audit adjustments under reimbursement agreements with third-party payers. Retroactive adjustments are estimated and recorded in the period the related services are rendered and adjusted in future periods, as final settlements are determined. Contracts, laws and regulations governing the Medicare and Medi-Cal programs are complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates may change by a material amount in the near term.

The University has entered into various operating agreements with the Hospitals for the professional services of faculty members from the School of Medicine, telecommunications services and other services and facilities charges.

Charity Care

The Hospitals provide care to patients who meet certain criteria under their charity care policies without charge or at amounts less than their established rates. The Hospitals do not record revenue for amounts determined to qualify as charity care. The amount of charity care services, quantified at established rates, was \$88.7 million and \$76.5 million for the years ended August 31, 2011 and 2010, respectively. The Hospitals also provide services to other patients under Medi-Cal and other publicly sponsored programs, which reimburse at amounts less than the cost of the services provided to the recipients. Estimated costs in excess of reimbursements for Medi-Cal and county services for the years ended August 31, 2011 and 2010 were \$251.4 million and \$219.4 million, respectively.

Provider Fee

The State of California enacted legislation in 2009 which established a Hospital Quality Assurance Fee (QAF) Program and a Hospital Fee Program. These programs imposed a provider fee on certain California general acute care hospitals that, combined with federal matching funds, would be used to provide supplemental payments to certain hospitals and support the State's effort to maintain health care coverage for children. For the year ended August 31, 2011, the Hospitals recognized \$88.6 million in "patient care, net" revenue under these programs and paid \$47.8 million in QAF to the California Department of Health Care Services.

The effective period of the Hospital Fee Program was April 1, 2009 through December 31, 2010. The State received final approval from the Centers for Medicare & Medicaid Services (CMS) in December of 2010 on the rates. Subsequent legislation extended the QAF and Hospital Fee programs, pending approval by CMS.

RECENT ACCOUNTING PRONOUNCEMENTS

In May 2011, the Financial Accounting Standards Board (FASB) issued an update to the Accounting Standards Codification (ASC) to ensure a consistent definition of fair value, fair value measurements and disclosure requirements under both U.S. GAAP and International Financial Reporting Standards. This guidance is effective for annual periods beginning after December 15, 2011. Key provisions include (1) additional information about Level 3 fair value measurements, including quantitative information about unobservable inputs, a description of the valuation process used, and a description of the sensitivity of fair value measurement to changes in inputs, and (2) for public entities, disclosure of all transfers between investments classified in the Level 1 and Level 2 fair value hierarchy. The University and the Hospitals are currently evaluating the impact that this guidance will have on its consolidated financial statement disclosures.

In July 2010, the FASB issued an update to the ASC which expanded disclosures about the credit quality of its financing receivables and allowances for credit losses. The disclosures are intended to provide additional information to assist financial statement users in assessing an entity's credit risk exposures and evaluating the adequacy of its allowance for credit losses. The University adopted this guidance for the year ended August 31, 2011.

In January 2010, the FASB issued an update to the ASC which expanded the required disclosures about fair value measurements. In particular, this guidance requires: (1) separate disclosure of the amounts of significant transfers in and out of Level 1 and Level 2 fair value hierarchy along with the reasons for such transfers; (2) information about purchases, sales, issuances and settlements to be presented separately in the reconciliation for Level 3 fair value hierarchy; (3) fair value measurements disclosures for each class of assets and liabilities; and (4) disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements that fall in either Level 2 or Level 3. The University and the Hospitals adopted this guidance for the year ended August 31, 2011 except for (2) which is effective for the fiscal year beginning September 1, 2011.

2. Accounts Receivable

Accounts receivable, net of bad debt allowances, at August 31, 2011 and 2010, in thousands of dollars, are as follows:

	2011			2010
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
U.S. government	\$ 66,173	\$ -	\$ 66,173	\$ 61,825
Non-government sponsors	28,614	-	28,614	26,818
Pending trades of securities	109,793	-	109,793	102,469
Accrued interest on investments	7,645	-	7,645	4,542
Student	9,582	-	9,582	11,220
Patient and third-party payers	-	520,295	520,295	457,094
Other	33,695	20,950	54,645	52,541
	255,502	541,245	796,747	716,509
Less bad debt allowances	(2,181)	(91,557)	(93,738)	(89,535)
ACCOUNTS RECEIVABLE, NET	\$ 253,321	\$ 449,688	\$ 703,009	\$ 626,974

3. Pledges Receivable

Pledges are recorded at applicable risk-adjusted discount rates, ranging from 2.4% to 6.0% for the University and from 0.1% to 5.8% for the Hospitals, commensurate with the duration of the donor's payment plan. At August 31, 2011 and 2010, pledges receivable, net of discounts and allowances, in thousands of dollars, are as follows:

	2011			2010
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
One year or less	\$ 131,990	\$ 34,596	\$ 166,586	\$ 130,705
Between one year and five years	684,759	73,352	758,111	689,254
More than five years	133,963	65,884	199,847	294,427
	950,712	173,832	1,124,544	1,114,386
Less discounts and allowances	(221,459)	(8,391)	(229,850)	(245,217)
PLEDGES RECEIVABLE, NET	\$ 729,253	\$ 165,441	\$ 894,694	\$ 869,169

Conditional pledges for the University, which depend on the occurrence of a specified future and uncertain event, were \$12.9 million and \$16.8 million at August 31, 2011 and 2010, respectively. The Hospitals had conditional pledges of \$126.7 million and \$100.0 million at August 31, 2011 and 2010, respectively. Lucile Packard Foundation for Children's Health is the primary community fundraising agent for LPCH and the pediatric faculty and programs at the University's School of Medicine.

4. Loans Receivable

The University's loans receivable consist primarily of student loans receivable and faculty and staff mortgages. Management regularly assesses the adequacy of the allowance for credit losses of its loans by performing ongoing evaluations, including such factors as the differing economic risks associated with each loan category, the financial condition of specific borrowers, the economic environment in which the borrowers operate, the level of delinquent loans and the value of any collateral.

STUDENT LOANS RECEIVABLE

Student loans receivable consist of institutional and federally-sponsored loans due from both current and former students. Student loans and allowance for student loan losses at August 31, 2011 and 2010, in thousands of dollars, are as follows:

	2011	2010
Institutional loans	\$ 18,082	\$ 16,208
Federally-sponsored loans	58,580	59,635
	76,662	75,843
Less allowance for student loan losses	(940)	(846)
STUDENT LOANS RECEIVABLE, NET	\$ 75,722	\$ 74,997

Institutional loans are funded by donor funds restricted for student loan purposes and University funds made available to meet demonstrated need in excess of all other sources of student loan borrowings.

Federally-sponsored loans are funded by advances to the University primarily under the Federal Perkins Loan Program (the "Program"). Loans to students under the Program are subject to mandatory interest rates and significant restrictions, and loans issued under the Program can be assigned to the federal government in certain non-repayment situations. In these situations, the federal portion of the loan balance is guaranteed.

Amounts received under the Program are ultimately refundable to the federal government in the event the University no longer participates in the Program and accordingly, have been reported as an obligation in the *Statements of Financial Position* as "U.S. government refundable loan funds".

FACULTY AND STAFF MORTGAGES

In a program to attract and retain excellent faculty and senior staff, the University provides home mortgage financing assistance, primarily in the form of secondary loans. Notes receivable amounting to \$462.5 million and \$439.9 million at August 31, 2011 and 2010, respectively, from University faculty and staff are included in "faculty and staff mortgages and other loans receivable, net" in the *Statements of Financial Position*. These loans and mortgages are collateralized by deeds of trust on properties concentrated in the region surrounding the University.

5. Investments

Investments held by the University and the Hospitals are measured and recorded at fair value. The valuation methodology, investment categories, fair value hierarchy, certain investment activities and related commitments for fiscal years 2011 and 2010 are discussed below.

Investments held by the University and the Hospitals at August 31, 2011 and 2010, in thousands of dollars, are as follows:

	2011			2010
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
Cash and cash equivalents	\$ 349,234	\$ 76,017	\$ 425,251	\$ 664,974
Collateral held for securities loaned	142,963	-	142,963	122,566
Public equities	4,446,401	111,561	4,557,962	3,835,083
Derivatives	(13,834)	-	(13,834)	(85)
Fixed income	756,822	-	756,822	415,651
Real estate	4,500,588	-	4,500,588	3,402,206
Natural resources	1,683,569	-	1,683,569	1,532,135
Private equities	5,319,813	-	5,319,813	3,867,427
Absolute return	5,253,470	-	5,253,470	5,005,170
Assets held by other trustees	163,044	13,972	177,016	166,372
Other	181,577	-	181,577	151,120
	22,783,647	201,550	22,985,197	19,162,619
Hospital funds invested in the University's Merged Pool	(1,594,160)	1,594,160	-	-
INVESTMENTS AT FAIR VALUE	\$21,189,487	\$ 1,795,710	\$ 22,985,197	\$19,162,619

VALUATION METHODOLOGY

To the extent available, the University's investments are recorded at fair value based on quoted prices in active markets. The University's investments that are listed on any U.S. or non-U.S. recognized exchanges are valued based on readily available market quotations. When such inputs do not exist, fair value measurements are based on the best available information and usually require a degree of judgment. For alternative investments, which are principally limited partnership investments in private equity, real estate, natural resources and hedge funds, the value is primarily based on the Net Asset Value (NAV) of the underlying investments. The NAV is reported by the external investment managers, including general partners, in accordance with their policies as described in their respective financial statements and offering memoranda. The most recent NAV reported is adjusted for capital calls, distributions and significant known valuation changes, if any, of its related portfolio through August 31, 2011 and 2010, respectively. These investments are generally less liquid than other investments, and the value reported may differ from the values that would have been reported had a ready market for these investments existed.

The University exercises due diligence in assessing the policies, procedures, and controls implemented by its external investment managers and believes the University's proportionate share of the carrying amount of these alternative investments is a reasonable estimate of fair value. Such due diligence procedures include, but are not limited to, ongoing communication, on-site visits, and review of information from the external investment managers as well as review of performance. In conjunction with these procedures, estimated fair value is determined by consideration of a wide range of factors, including market conditions, redemption terms and restrictions, and risks inherent in the inputs of the external investment managers' valuation.

For alternative investments which are direct investments, the University considers various factors to estimate fair value, such as the timing of the transaction, the market in which the company operates, comparable transactions, company performance and projections as well as discounted cash flow analysis. The selection of an appropriate valuation technique may be affected by the availability and general reliability of relevant inputs. In some cases, one valuation technique may provide the best indication of fair value while in other circumstances, multiple valuation techniques may be appropriate. Furthermore, the University may review the investment's underlying portfolio as well as engage external appraisers, depending on the nature of the investment.

INVESTMENT CATEGORIES

Investments are categorized by asset class and valued as described below:

Cash and cash equivalents categorized as investments include money market funds, overnight receivables on repurchase agreements and restricted cash. Overnight receivables on repurchase agreements are valued based on cost, which approximates fair value. Money market funds are valued based on reported unit values. Restricted cash includes collateral provided to or received from counterparties related to investment-related derivative contracts (see *Note 7*).

Included in "cash and cash equivalents" for the Hospitals are assets limited as to use of \$1.0 million at both August 31, 2011 and 2010. Assets limited as to use include hospital accounts held by a trustee in accordance with indenture requirements. The indenture terms require that the trustee control the expenditure of bond proceeds for hospital capital projects. The assets are recorded at fair value.

Collateral held for securities loaned originates in the form of cash and cash equivalents and is reinvested for income in cash equivalent vehicles. These investments are recorded at cost, which approximates fair value (see *Note 9*).

Public equities are investments valued based on quoted market prices on the last trading date on or before the balance sheet date of the principal market (and exchange rates, if applicable). They include investments that are directly held as well as commingled funds which invest in publicly traded equities. These investments are reported on a trade-date basis. The fair values of public equities held through alternative investments are calculated by the respective external investment managers as described under *Valuation Methodology* above.

Derivatives are used by the University to manage its exposure to certain risks relating to ongoing business and investment operations. Derivatives such as forward currency contracts, options, interest rate swaps and credit default swaps (CDS) are valued using models based on market verifiable inputs, or by using independent broker quotes.

Fixed income investments are valued by independent pricing sources, broker dealers or pricing models that factor in, where applicable, recently executed transactions, interest rates, bond or credit default spreads and volatility. They include investments that are actively traded fixed income securities or mutual funds.

Real estate represents directly owned real estate and other real estate interests held through limited partnerships. The fair value of real estate directly owned by the University, including the Stanford Shopping Center and the Stanford Research Park, is based primarily on discounted cash flows, using estimates from the asset manager or external investment managers, corroborated by appraisals and market data, if available. The fair value of real estate held through limited partnerships is based on NAV as reported by the external investment managers and is adjusted as described under *Valuation Methodology* above.

Natural resources are mostly held in commodity and energy related investments, which are valued on the basis of a combination of models, including appraisals, discounted cash flows and commodity price factors. The fair value of these types of alternative investments is based on NAV as reported by the external investment managers and adjusted as described under *Valuation Methodology* above.

Private equities are investments that participate primarily in venture capital and leveraged buyout strategies. Distributions from these investments are received through liquidation of the underlying asset. The fair value of these types of alternative investments is based on the NAV reported by the external investment managers and is adjusted as described under *Valuation Methodology* above.

Absolute return investments are typically commingled funds that employ multiple strategies to produce positive returns, regardless of the direction of the financial markets. The fair value of these types of alternative investments is valued based on NAV as reported by the external investment managers and is adjusted as described under *Valuation Methodology* above.

Assets held by other trustees generally represent the University's and the Hospitals' residual interest in split interest agreements where the University or the Hospitals are not the trustee. The residual (or beneficial) interest represents the present value of the future distributions expected to be received over the term of the agreement, which approximates fair value, and the assets are based on estimates provided by trustees.

FAIR VALUE HIERARCHY

U.S. GAAP defines fair value as the price received upon sale of an asset or paid upon transfer of a liability in an orderly transaction between market participants. Current guidance establishes a hierarchy of valuation inputs based on the extent to which the inputs are observable in the marketplace. Inputs are used in applying the various valuation techniques and take into account the assumptions that market participants use to make valuation decisions. Inputs may include price information, credit data, liquidity statistics, and other factors specific to the financial instrument. Observable inputs reflect market data obtained from independent sources. In contrast, unobservable inputs reflect the entity's assumptions about how market participants would value the financial instrument. Valuation techniques used under U.S. GAAP must maximize the use of observable inputs to the extent available.

A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. The following describes the hierarchy of inputs used to measure fair value and the primary valuation methodologies used for financial instruments measured at fair value on a recurring basis:

Level 1 – Investments whose values are based on quoted market prices in active markets for identical assets or liabilities are classified as Level 1. Level 1 investments include active listed equities and certain short term fixed income securities. Such investments are valued based upon the closing price quoted on the last trading date on or before the reporting date on the principal market, without adjustment.

Exchange-traded derivatives such as options, futures contracts and warrants using observable inputs such as the last reportable sale price or the most recent bid price are typically classified as Level 1 (see *Note 7*).

Level 2 – Investments that trade in markets that are not actively traded, but are valued based on quoted market prices, dealer quotations, or alternative pricing sources for similar assets or liabilities are classified as Level 2. These investments include certain United States government and sovereign obligations, government agency obligations, investment grade corporate bonds and certain limited marketability securities.

Privately negotiated over-the-counter (OTC) derivatives such as forward currency contracts, CDS, total return swaps, and interest rate swaps are typically classified as Level 2 (see *Note 7*). In instances where quotations received from counterparties or valuation models are used, the value of an OTC derivative depends upon the contractual terms of the instrument as well as the availability and reliability of observable inputs. Such inputs include market prices for reference securities, yield curves, and credit curves.

Level 3 – Investments classified as Level 3 have significant unobservable inputs, as they trade infrequently or not at all. The inputs into the determination of fair value of these investments are based upon the best information in the circumstance and may require significant management judgment. These investments primarily consist of the University's alternative investments and are classified as Level 3 as the inputs are not observable. Certain alternative investments may be reclassified to Level 2 when the University has the ability to redeem them at NAV in the near term without significant restrictions on redemption.

The following table summarizes the University's investments and other assets within the fair value hierarchy and asset categories at August 31, 2011 and 2010, in thousands of dollars:

	AS OF AUGUST 31,			
	2011	LEVEL 1	LEVEL 2	LEVEL 3
UNIVERSITY*				
Cash and cash equivalents	\$ 349,234	\$ 324,675	\$ 24,559	\$ -
Collateral held for securities loaned	142,963	86,178	56,785	-
Public equities	4,446,401	2,048,108	579,456	1,818,837
Derivatives	(13,834)	4,534	(18,368)	-
Fixed income	756,822	114,427	642,395	-
Real estate	4,500,588	-	-	4,500,588
Natural resources	1,683,569	217,980	-	1,465,589
Private equities	5,319,813	15,371	-	5,304,442
Absolute return	5,253,470	-	1,863,197	3,390,273
Assets held by other trustees	163,044	-	-	163,044
Other	181,577	122	680	180,775
TOTAL	22,783,647	2,811,395	3,148,704	16,823,548
HOSPITALS				
Cash and cash equivalents	76,017	72,106	3,911	-
Public equities	111,561	65,262	46,299	-
Assets held by other trustees	13,972	-	-	13,972
TOTAL	201,550	137,368	50,210	13,972
CONSOLIDATED TOTAL	\$ 22,985,197	\$ 2,948,763	\$ 3,198,914	\$ 16,837,520

* Amounts include the Hospitals' cross investment in the University's investment pools of \$1.6 billion.

	AS OF AUGUST 31,			
	2010	LEVEL 1	LEVEL 2	LEVEL 3
UNIVERSITY*				
Cash and cash equivalents	\$ 625,207	\$ 587,689	\$ 37,518	\$ -
Collateral held for securities loaned	122,566	86,128	36,438	-
Public equities	3,788,900	1,772,259	655,839	1,360,802
Derivatives	(85)	(27)	(58)	-
Fixed income	415,651	154,633	261,018	-
Real estate	3,402,206	-	-	3,402,206
Natural resources	1,532,135	249,040	-	1,283,095
Private equities	3,867,427	7,383	-	3,860,044
Absolute return	5,005,170	-	1,607,159	3,398,011
Assets held by other trustees	152,744	-	-	152,744
Other	151,120	132	653	150,335
TOTAL	19,063,041	2,857,237	2,598,567	13,607,237
HOSPITALS				
Cash and cash equivalents	39,767	35,663	4,104	-
Public equities	46,183	-	46,183	-
Assets held by other trustees	13,628	-	-	13,628
TOTAL	99,578	35,663	50,287	13,628
CONSOLIDATED TOTAL	\$ 19,162,619	\$ 2,892,900	\$ 2,648,854	\$ 13,620,865

* Amounts include the Hospitals' cross investment in the University's investment pools of \$1.3 billion.

The University manages the majority of the Hospitals' investments, including the Hospitals' investment in the Merged Pool (MP), with a combined fair value of \$1.6 billion and \$1.3 billion at August 31, 2011 and 2010, respectively.

SUMMARY OF LEVEL 3 INVESTMENT ACTIVITIES AND TRANSFERS

The following tables present the activities for Level 3 investments for the years ended August 31, 2011 and 2010, in thousands of dollars:

FAIR VALUE MEASUREMENTS USING SIGNIFICANT UNOBSERVABLE INPUTS (LEVEL 3)	BEGINNING BALANCE AS OF SEPTEMBER 1, 2010	NET PURCHASES (SALES AND MATURITIES)	REALIZED GAINS (LOSSES)	CHANGE IN UNREALIZED GAINS (LOSSES)	NET TRANSFERS IN (OUT)	ENDING BALANCE AS OF AUGUST 31, 2011
UNIVERSITY						
Public equities	\$ 1,360,802	\$ 275,336	\$ 88,822	\$ 91,606	\$ 2,271	\$ 1,818,837
Real estate	3,402,206	232,310	(6,542)	862,792	9,822	4,500,588
Natural resources	1,283,095	(19,660)	52,052	155,238	(5,136)	1,465,589
Private equities	3,860,044	200,561	106,912	1,136,925	-	5,304,442
Absolute return	3,398,011	(290,354)	213,746	157,086	(88,216)	3,390,273
Assets held by other trustees	152,744	(4,931)	15,231	-	-	163,044
Other	150,335	17,435	9,747	18,528	(15,270)	180,775
TOTAL	13,607,237	410,697	479,968	2,422,175	(96,529)	16,823,548
HOSPITALS						
Assets held by other trustees	13,628	-	(213)	557	-	13,972
TOTAL	13,628	-	(213)	557	-	13,972
CONSOLIDATED TOTAL	\$ 13,620,865	\$ 410,697	\$ 479,755	\$ 2,422,732	\$ (96,529)	\$ 16,837,520

FAIR VALUE MEASUREMENTS USING SIGNIFICANT UNOBSERVABLE INPUTS (LEVEL 3)	BEGINNING BALANCE AS OF SEPTEMBER 1, 2009	NET PURCHASES (SALES AND MATURITIES)	REALIZED GAINS (LOSSES)	CHANGE IN UNREALIZED GAINS (LOSSES)	NET TRANSFERS IN (OUT)	ENDING BALANCE AS OF AUGUST 31, 2010
UNIVERSITY						
Public equities	\$ 1,439,891	\$ (159,608)	\$ (31,130)	\$ 313,186	\$ (201,537)	\$ 1,360,802
Fixed Income	25,994	(26,088)	2,084	(1,990)	-	-
Real estate	3,269,081	263,108	9,780	(139,763)	-	3,402,206
Natural resources	1,636,677	(141,882)	52,006	(64,377)	(199,329)	1,283,095
Private equities	3,197,431	155,157	(14,291)	521,747	-	3,860,044
Absolute return	3,492,396	(142,431)	(88,181)	694,387	(558,160)	3,398,011
Assets held by other trustees	139,474	(1,777)	15,047	-	-	152,744
Other	158,538	10,588	1,555	(20,346)	-	150,335
TOTAL	13,359,482	(42,933)	(53,130)	1,302,844	(959,026)	13,607,237
HOSPITALS						
Assets held by other trustees	13,997	-	(131)	(238)	-	13,628
TOTAL	13,997	-	(131)	(238)	-	13,628
CONSOLIDATED TOTAL	\$ 13,373,479	\$ (42,933)	\$ (53,261)	\$ 1,302,606	\$ (959,026)	\$ 13,620,865

Realized gains (losses) and the change in unrealized gains (losses) in the tables above are included in the *Statements of Activities* primarily as "increase (decrease) in reinvested gains" by level of restriction. For the years ended August 31, 2011 and 2010, the change in unrealized gains (losses) for Level 3 investments still held at August 31, 2011 and 2010 was \$2.5 billion and \$1.3 billion, respectively.

Net transfers in (out) include investments which have been reclassified to Level 2 as the University has the ability to redeem these at NAV in the near term. Net transfers in (out) also include situations where observable inputs have changed, such as when Level 3 investments make distributions from an underlying asset with a fair value based on quoted market prices. All transfer amounts are based on the fair value at the beginning of the fiscal year. There were no transfers between Level 1 and Level 2 during the year ended August 31, 2011.

INVESTMENT-RELATED COMMITMENTS

The University is obligated under some alternative investment agreements to advance additional funding up to specified levels over a period of several years. The following table presents significant terms of such agreements solely related to the alternative investments measured at fair value based on NAV at August 31, 2011, in thousands of dollars:

ASSET CLASS	FAIR VALUE	UNFUNDED COMMITMENT	REMAINING LIFE (YEARS)	REDEMPTION TERMS AND RESTRICTIONS
Public equities	\$ 2,398,152	\$ 12,754	0 to 5	Generally, lock-up provisions ranging from 0 to 6 years. After initial lock up expires, redemptions are available on a rolling basis and require 3 to 180 days prior notification.
Real estate	1,713,824	992,385	0 to 13	Not eligible for redemption
Natural resources	991,416	459,196	0 to 15	Not eligible for redemption
Private equities	5,304,169	2,024,440	0 to 16	Not eligible for redemption
Absolute return	5,200,304	251,716	0 to 7	Generally, lock-up provisions ranging from 0 to 6 years. After initial lock up expires, redemptions are available on a rolling basis and require 2 to 180 days prior notification.
TOTAL	\$ 15,607,865	\$ 3,740,491		

At August 31, 2011, the aggregate amount of unfunded commitments was \$3.9 billion. This amount includes both the unfunded commitments in the table above and other alternative investments where the fair values were not based on NAV.

INVESTMENT RETURNS

Total investment returns for the years ended August 31, 2011 and 2010, in thousands of dollars, are as follows:

	2011			2010
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
Investment income	\$ 218,727	\$ 11,222	\$ 229,949	\$ 166,084
Net realized and unrealized gains	3,218,576	235,335	3,453,911	1,896,526
TOTAL INVESTMENT RETURN	\$ 3,437,303	\$ 246,557	\$ 3,683,860	\$ 2,062,610

Investment returns are net of investment management expenses, including both external management fees and internal University investment-related salaries, benefits and operating expenses, and the portion of interest expense and amortization related to the April 2009 bond issuance held for liquidity purposes (see *Note 10*).

FUTURE MINIMUM RENTAL INCOME

As part of its investment portfolio, the University holds certain investment properties that it leases to third parties. Future minimum rental income due from the Stanford Shopping Center, the Stanford Research Park and other properties under non-cancelable leases in effect with tenants at August 31, 2011, in thousands of dollars, is as follows:

<u>YEAR ENDING AUGUST 31</u>	<u>FUTURE MINIMUM RENTAL INCOME</u>
2012	\$ 84,012
2013	87,918
2014	87,313
2015	81,679
2016	77,108
Thereafter	1,679,730
TOTAL	\$ 2,097,760

6. Investment Pools

The University's investments are held in various investment pools or in specific investments to comply with donor requirements as indicated in the following table, at August 31, 2011 and 2010, in thousands of dollars:

	2011	2010
UNIVERSITY		
Merged Pool	\$ 19,547,086	\$ 16,616,406
Expendable Funds Pool	2,648,621	2,369,236
Endowment Income Funds Pool	355,917	354,844
Other Investment Pools	392,285	369,572
Specific Investments	2,843,907	2,075,245
	25,787,816	21,785,303
Less:		
Amounts included in "cash and cash equivalents" in the <i>Statements of Financial Position</i>	(639,020)	(640,563)
Funds cross-invested in investment pools	(2,361,238)	(2,077,595)
Hospital funds invested in the University's investment pools	(1,598,071)	(1,263,784)
TOTAL	21,189,487	17,803,361
HOSPITALS		
Investments	1,795,710	1,359,258
TOTAL	1,795,710	1,359,258
INVESTMENTS AT FAIR VALUE	\$ 22,985,197	\$ 19,162,619

The MP is the primary investment pool in which endowment (see *Note 12*) and other long-term funds are invested. The MP is invested with the objective of optimizing long-term total return while maintaining an appropriate level of risk for the University. It is a unitized investment pool in which the fund holders purchase investments and withdraw funds based on a monthly share value.

The Expendable Funds Pool (EFP) and Endowment Income Funds Pool (EIFP) are the principal investment vehicles for the University's expendable funds. A substantial portion of the EFP is cross-invested in the MP; the remainder is included in "cash and cash equivalents" in the *Statements of Financial Position*. The EIFP holds income previously distributed to holders of permanently restricted endowment funds that has not yet been expended. The EIFP is invested in highly liquid instruments and is included in the *Statements of Financial Position* as "cash and cash equivalents".

The Board has established a policy for the distribution of the investment returns of the EFP. The difference between the actual return of this investment pool and the approved payout is deposited in, or withdrawn from, funds functioning as endowment (FFE) (see *Note 12*). For the years ended August 31, 2011 and 2010, the results of the EFP, in thousands of dollars, are as follows:

	2011	2010
Total investment return of the EFP	\$ 399,210	\$ 251,501
Less distributions to fund holders and operations	(83,199)	(478)
AMOUNTS ADDED TO FFE	\$ 316,011	\$ 251,023

7. Derivatives

The University utilizes various strategies to reduce investment and credit risks, to serve as a temporary surrogate for investment in stocks and bonds, to manage interest rate exposure on the University's debt, and/or to achieve specific exposure to foreign currencies. Futures, options and other derivative instruments are used to adjust elements of investment exposures to various securities, sectors, markets and currencies without actually taking a position in the underlying asset or basket of assets. Interest rate swaps are used to manage interest rate risk. With respect to foreign currencies, the University utilizes forward contracts and foreign currency options to manage exchange rate risk.

Foreign currency forward contracts, interest rate swaps, securities lending, and repurchase agreements entail counterparty credit risk. The University seeks to control this risk by entering into transactions with quality counterparties, by establishing and monitoring credit limits and by requiring collateral in certain situations.

INVESTMENT-RELATED DERIVATIVES

The following table presents amounts for investment-related derivatives, including the notional amount, the fair values at August 31, 2011 and 2010, and gains and losses for the years ended August 31, 2011 and 2010, in thousands of dollars:

	AS OF AUGUST 31, 2011			YEAR ENDED AUGUST 31, 2011
	NOTIONAL AMOUNT ¹	GROSS DERIVATIVE ASSETS ²	GROSS DERIVATIVE LIABILITIES ²	REALIZED AND UNREALIZED GAINS (LOSSES) ³
Interest-rate contracts	\$ 877,781	\$ 462	\$ 5,970	\$ (1,514)
Foreign exchange contracts	346,315	931	13,208	(17,926)
Equity contracts	95,978	4,488	-	176
Credit contracts	70,692	312	849	584
TOTAL	\$ 1,390,766	\$ 6,193	\$ 20,027	\$ (18,680)

	AS OF AUGUST 31, 2010			YEAR ENDED AUGUST 31, 2010
	NOTIONAL AMOUNT ¹	GROSS DERIVATIVE ASSETS ²	GROSS DERIVATIVE LIABILITIES ²	REALIZED AND UNREALIZED GAINS (LOSSES) ³
Interest-rate contracts	\$ 103,381	\$ 232	\$ 770	\$ 621
Foreign exchange contracts	62,570	1,104	419	125
Credit contracts	53,072	244	476	(515)
TOTAL	\$ 219,023	\$ 1,580	\$ 1,665	\$ 231

¹ The notional amount is representative of the volume and activity of the respective derivative type during the years ended August 31, 2011 and 2010.

² Gross derivative assets less gross derivative liabilities is presented as "derivatives" on the investment table in Note 5.

³ Gains (losses) on derivatives are included in the Statements of Activities as "increase in reinvested gains" in "other changes in unrestricted net assets".

Credit Default Swaps

The University's derivative activities include both the purchase and sale of CDS which are included in credit contracts in the previous table. CDS are contracts under which counterparties are provided protection against the risk of default on a set of debt obligations issued by specific companies (or group of companies combined in an index). The buyer of the CDS will make payment to the seller and in return receive payment if the underlying instrument goes into default or is triggered by some other credit event. The University's CDS transactions include both single name entities as well as index CDS. Under the index CDS, the credit events that would trigger settlement of the CDS and require the University to remit payment are generally bankruptcy and failure to pay.

The tables below summarize certain information regarding protection sold through CDS at August 31, 2011 and 2010, in thousands of dollars:

CREDIT RATINGS OF THE REFERENCE OBLIGATION ²	MAXIMUM POTENTIAL PAYOUT (NOTIONAL AMOUNT ¹) / YEARS TO MATURITY			FAIR VALUE ASSET/ (LIABILITY)
	LESS THAN 3	OVER 3	TOTAL	
2011				
Single name credit default swaps:				
A- to AA+	\$ 12,783	\$ 16,400	\$ 29,183	\$ 67
BBB- to BBB+	3,636	2,300	5,936	(444)
Total single name credit default swaps	16,419	18,700	35,119	(377)
TOTAL CREDIT DEFAULT SWAPS SOLD	\$ 16,419	\$ 18,700	\$ 35,119	\$ (377)
2010				
Single name credit default swaps:				
A- to AA+	\$ 7,600	\$ 200	\$ 7,800	\$ 29
BBB- to BBB+	4,000	800	4,800	(106)
Total single name credit default swaps	11,600	1,000	12,600	(77)
Index credit default swaps ³	-	800	800	(37)
TOTAL CREDIT DEFAULT SWAPS SOLD	\$ 11,600	\$ 1,800	\$ 13,400	\$ (114)

¹ The notional amount is representative of the volume and activity of the respective derivative type during the years ended August 31, 2011 and 2010.

² The credit rating is according to Standard & Poor's and represents the current performance risk of the swap.

³ Index credit default swaps are linked to a basket of credit derivatives that include entities that have a Standard & Poor's rating of BBB- or higher.

DEBT-RELATED DERIVATIVES

The University and SHC use interest rate exchange agreements to manage the interest rate exposure of their debt portfolios. Under the terms of the current agreements, the entities pay a fixed interest rate, determined at inception, and receive a variable rate on the underlying notional principal amount. Generally, the exchange agreements require mutual posting of collateral by the University and SHC and the counterparties if the termination values exceed a predetermined threshold dollar amount.

At August 31, 2011, the University had interest rate exchange agreements related to \$130.0 million of the outstanding balance of the CEFA Series S VRDBs (see *Note 10*). The agreements, which have an interest rate of 3.94%, expire November 1, 2039. The notional amount and the fair value of the exchange agreements are included in the table below. Collateral posted with various counterparties was \$25.0 million and \$35.6 million at August 31, 2011 and 2010, respectively, and is included in the *Statements of Financial Position*. In addition, the University posted an irrevocable standby letter of credit of \$15.0 million to support collateral requirements at August 31, 2011 (see *Note 10*).

At August 31, 2011, SHC had interest rate exchange agreements expiring through November 2045 (see *Note 11*). Certain of the agreements pay fixed interest rates to counterparties varying from 3.37% to 4.08% and a portion involves the exchange of fixed rate payments for variable rate payments based on a percentage of the One Month London Interbank Offered Rate (LIBOR). The notional amount and the fair value of the exchange agreements are included in the table below. The amount of collateral required to be posted with counterparties was \$7.1 million and \$72.6 million at August 31, 2011 and 2010, respectively, and was met by the posting of standby letters of credit in the aggregate amount of \$20.0 million and \$75.0 million at August 31, 2011 and 2010, respectively, which may only be drawn upon in the event of a default by SHC.

The following table presents amounts for debt-related derivatives including the notional amount, the fair values at August 31, 2011 and 2010, and gains and losses for the years ended August 31, 2011 and 2010, in thousands of dollars:

	AS OF AUGUST 31, 2011		YEAR ENDED AUGUST 31, 2011	AS OF AUGUST 31, 2010		YEAR ENDED AUGUST 31, 2010
	NOTIONAL AMOUNT ¹	GROSS DERIVATIVE LIABILITIES ²	REALIZED AND UNREALIZED GAINS ³	NOTIONAL AMOUNT ¹	GROSS DERIVATIVE LIABILITIES ²	REALIZED AND UNREALIZED (LOSSES) ³
Debt-related interest-rate contracts:						
University	\$ 130,000	\$ 38,968	\$ 3,645	\$ 150,000	\$ 42,613	\$ (17,765)
Hospitals	749,400	165,693	672	749,400	166,365	(79,054)
TOTAL	\$879,400	\$ 204,661	\$ 4,317	\$ 899,400	\$ 208,978	\$ (96,819)

¹ The notional amount is representative of the volume and activity of the respective derivative type during the years ended August 31, 2011 and 2010.

² Fair value is measured using Level 2 inputs as defined in Note 5. Amounts are included in the *Statements of Financial Position* in "accounts payable and accrued expenses" and discussed more fully in Notes 10 and 11.

³ Gains (losses) on derivatives are included in the *Statements of Activities* as "increase in reinvested gains" in "other changes in unrestricted net assets".

8. Plant Facilities

Plant facilities, net of accumulated depreciation, at August 31, 2011 and 2010, in thousands of dollars, are as follows:

	2011			2010
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
Land and improvements	\$ 461,486	\$ 93,667	\$ 555,153	\$ 547,687
Buildings and building improvements	4,280,731	1,165,826	5,446,557	4,950,274
Furniture, fixtures and equipment	1,708,469	815,455	2,523,924	2,410,892
Construction in progress	170,657	312,069	482,726	658,238
	6,621,343	2,387,017	9,008,360	8,567,091
Less accumulated depreciation	(2,946,960)	(1,054,293)	(4,001,253)	(3,700,429)
PLANT FACILITIES, NET OF ACCUMULATED DEPRECIATION	\$ 3,674,383	\$ 1,332,724	\$ 5,007,107	\$ 4,866,662

At August 31, 2011, \$1.2 billion and \$613.0 million of fully depreciated plant facilities were still in use by the University and the Hospitals, respectively.

9. Liabilities Under Security Lending Agreements

The University receives short-term U.S. government obligations and cash as collateral deposits for certain securities loaned temporarily to brokers. It is the University's policy to require receipt of collateral on securities lending contracts and repurchase agreements equal to a minimum of 102% of the fair market value of the security loaned. In addition, the University is party to certain forward sale and purchase agreements. At August 31, 2011 and 2010, these amounts, in thousands of dollars, are as follows:

	2011	2010
Collateral deposits for certain securities loaned temporarily to brokers ^{1, 2}	\$ 142,963	\$ 122,566
Forward sale and purchase agreements ¹	39,064	37,458
LIABILITIES UNDER SECURITY LENDING AGREEMENTS	\$ 182,027	\$ 160,024

¹ The corresponding investments are included as "investments" in the Statements of Financial Position (see Note 5).

² The estimated fair value of securities loaned to brokers at August 31, 2011 and 2010 was \$125.0 million and \$118.1 million, respectively.

10. University Notes and Bonds Payable

Notes and bonds payable for the University at August 31, 2011 and 2010, in thousands of dollars, are as follows:

	YEAR OF MATURITY	EFFECTIVE INTEREST RATE 2011/2010	OUTSTANDING PRINCIPAL	
			2011	2010
Tax-exempt:				
CEFA Fixed Rate Revenue Bonds:				
Series O	2031	5.13%	\$ 89,555	\$ 89,555
Series P	2013	5.25%	51,260	51,260
Series Q	2032	5.25%	101,860	101,860
Series R	2011-2021	4.00% - 5.00%	111,585	111,585
Series T	2014-2039	4.00% - 5.00%	361,310	361,310
Series U	2040	5.25%	215,375	215,375
CEFA VRDBs:				
Series L	2014-2022	0.12%/0.20%	83,818	83,818
Series S	2039-2050	0.22%-0.36%/0.30%-0.46%*	181,200	181,200
Commercial Paper	2011	0.10%/0.28%	92,682	113,532
Taxable:				
Fixed Rate Notes and Bonds:				
Stanford University Bonds	2024	6.88%	150,000	150,000
Medium Term Notes	2011-2026	6.16% - 7.65%	50,000	100,000
Stanford University Series 2009A	2014-2019	3.63% - 4.75%	1,000,000	1,000,000
Other	2015-2016	Various	67,799	70,225
Variable Rate Notes:				
Commercial Paper	2011	0.17%/0.34%*	108,976	119,676
University notes and bonds payable			2,665,420	2,749,396
Unamortized original issue premiums/discounts, net			61,187	66,537
TOTAL			\$ 2,726,607	\$ 2,815,933

*Exclusive of interest rate exchange agreements (see Note 7).

At August 31, 2011 and 2010, the fair value of these debt instruments was approximately \$3.0 billion on both dates.

The University borrows at tax-exempt rates through the California Educational Facilities Authority (CEFA). The CEFA debt is a general unsecured obligation of the University. Although CEFA is the issuer, the University is responsible for the repayment of the tax-exempt debt. The University's long-term ratings of AAA/Aaa/AAA were affirmed in fiscal year 2011 by Standard and Poor's, Moody's Investors Service and Fitch Ratings, respectively.

In April 2011, the 6.16% taxable Medium Term Notes Series A-3 in the amount of \$50.0 million matured.

In December 2010, the University entered into a \$50.0 million line of credit agreement to issue irrevocable standby letters of credit to support various collateral posting obligations. At August 31, 2011, irrevocable standby letters of credit of \$30.0 million were outstanding in the following amounts and for the following respective purposes: (i) \$15.0 million to support collateral requirements under certain interest rate exchange agreements discussed in Note 7 and (ii) \$15.0 million to serve as security for workers' compensation deductible insurance arrangements. No amounts have been drawn on these letters of credit at August 31, 2011.

In May 2010, CEFA Series U-1 revenue bonds (the "Bonds") in the amount of \$215.4 million plus an original issue premium of \$36.3 million were issued. The Bonds bear interest at a rate of 5.25% and mature on April 1, 2040. Proceeds were used to refund commercial paper and to fund facilities and infrastructure.

Stanford holds controlling interests in several investment entities which were consolidated in the financial statements in fiscal year 2011 and 2010. At August 31, 2011 and 2010, taxable debt included \$66.5 million and \$68.5 million, respectively, of debt where Stanford is ultimately liable for principal should the investees default.

The University's taxable and tax-exempt commercial paper facilities and related information at August 31, 2011 and 2010, in thousands of dollars, were as follows:

COMMERCIAL PAPER	POTENTIAL BORROWINGS	OUTSTANDING BALANCE AT AUGUST 31	WEIGHTED AVERAGE DAYS TO MATURITY	WEIGHTED AVERAGE EFFECTIVE INTEREST
2011				
Taxable	\$ 350,000	\$ 108,976	26.3	0.17%
Tax-exempt	\$ 300,000	\$ 92,682	32.3	0.10%
2010				
Taxable	\$ 350,000	\$ 119,676	45.6	0.34%
Tax-exempt	\$ 300,000	\$ 113,532	42.5	0.28%

The University had \$265.0 million of VRDBs outstanding in addition to commercial paper at August 31, 2011. CEFA Series L bonds bear interest at a weekly rate and CEFA Series S bonds bear interest at a commercial paper municipal rate and are outstanding for various interest periods of 270 days or less. In the event the University receives notice of any optional tender of its VRDBs, or if the bonds become subject to mandatory tender, the purchase price of the bonds will be paid from the remarketing of such bonds. However, if the remarketing proceeds are insufficient, the University will have a current obligation to purchase the bonds tendered. The University has identified several sources of funding including cash, money market funds, U.S. treasury securities and agencies' discount notes to provide for the full and timely purchase price of any bonds tendered in the event of a failed remarketing.

The University incurred interest expense of approximately \$71.3 million and \$60.2 million for the years ended August 31, 2011 and 2010, respectively, net of (1) \$782 thousand and \$790 thousand, respectively, of interest income on invested unspent proceeds, (2) \$1.6 million and \$3.9 million, respectively, in interest capitalized as a cost of construction and (3) \$29.9 million and \$33.7 million (net of interest income of \$667 thousand and \$683 thousand), respectively, of interest expense associated with the Series 2009A bonds which were recorded as an investment expense. Interest expense includes administrative expenses, amortized bond issuance costs, and amortized bond premium or discount.

The University uses interest rate exchange agreements to manage the interest rate exposure of its debt portfolio (see *Note 7*). Net payments on interest rate exchange agreements, which are included in "swap interest and unrealized gains (losses)" in the *Statements of Activities*, totaled \$5.6 million and \$5.7 million for the years ended August 31, 2011 and 2010, respectively.

At August 31, 2011, scheduled principal payments on notes and bonds, in thousands of dollars, are as follows:

YEAR ENDING AUGUST 31	PRINCIPAL PAYMENTS
2012 Commercial paper	\$ 201,658
2012 Variable debt subject to remarketing	265,018
2012 Other	63,916
2013	64,883
2014	573,720
2015	55
2016	250,000
Thereafter	1,246,170
TOTAL	\$ 2,665,420

11. Hospitals Notes and Bonds Payable

Notes, bonds and capital lease obligations for the Hospitals at August 31, 2011 and 2010, in thousands of dollars, are as follows:

	YEAR OF MATURITY	EFFECTIVE INTEREST RATE* 2011/2010	OUTSTANDING PRINCIPAL	
			2011	2010
SHC:				
CHFFA Fixed Rate Revenue Bonds:				
2003 Series A	2023	2.00%-5.00%	78,595	83,400
2008 Series A-1	2040	2.25%-5.15%	70,360	70,360
2008 Series A-2	2040	1.00%-5.25%/0.26%	104,100	104,100
2008 Series A-3	2040	1.00%-5.50%/3.45%	84,165	85,700
2010 Series A	2031	4.00%-5.75%	149,345	149,345
2010 Series B	2036	4.50%-5.75%	146,710	146,710
Promissory Note	2014	7.03%	539	704
CHFFA Variable Rate Revenue Bonds:				
2008 Series B	2045	0.17%/0.24%	168,200	168,200
LPCH:				
CHFFA Fixed Rate Revenue Bonds:				
2003 Series C	2013-2027	3.25%	55,000	55,000
CHFFA Variable Rate Revenue Bonds:				
2008 Series A	2027-2033	0.13%/0.25%	30,340	30,340
2008 Series B	2027-2033	0.16%/0.23%	30,340	30,340
2008 Series C	2015-2023	0.16%/0.23%	32,770	32,770
Capital lease obligations			13,643	15,572
Hospitals notes and bonds payable			964,107	972,541
Unamortized original issue premiums/discounts, net			19,071	19,873
TOTAL			\$ 983,178	\$ 992,414

*Exclusive of interest rate exchange agreements (see Note 7).

At August 31, 2011 and 2010, the fair value of these debt instruments was approximately \$1.0 billion on both dates.

The Hospitals borrow at tax-exempt rates through the California Health Facilities Financing Authority (CHFFA). The CHFFA debt is a general obligation of the Hospitals. Payments of principal and interest on the Hospitals' bonds are collateralized by a pledge of the revenues of the respective hospitals. Although CHFFA is the issuer, the Hospitals are responsible for the repayment of the tax-exempt debt. The University is not an obligor or guarantor with respect to any obligations of SHC or LPCH, nor are SHC or LPCH obligors or guarantors with respect to obligations of the University.

SHC and LPCH are each party to separate master trust indentures that include, among other requirements, limitations on the incurrence of additional indebtedness, liens on property, restrictions on disposition or transfer of assets and compliance with certain financial ratios. Subject to applicable no-call provisions, the Hospitals may cause the redemption of the bonds, in whole or in part, prior to the stated maturities.

SHC

In June 2011, SHC remarketed the CHFFA 2008 Series A-2, A-3 and B-2 bonds in the aggregate principal amount of \$272.4 million. SHC converted both the CHFFA 2008 Series A-2 bonds from a weekly interest rate mode and the CHFFA 2008 Series A-3 bonds from a multi-annual put mode to a long-term fixed interest rate mode and the bonds mature in 2040. The remarketing of the CHFFA 2008 Series A-3 bonds generated an original issue premium of approximately \$1.5 million that, pursuant to the requirements of the underlying documents, was used to reduce the principal amount of the bonds from \$85.7 million to \$84.2 million. SHC converted the CHFFA 2008 Series B-2 bonds from a weekly interest rate mode to a commercial paper mode.

In June 2010, CHFFA, on behalf of SHC, issued fixed rate revenue bonds in the aggregate principal amount of \$296.1 million to refund certain previously issued bonds. The CHFFA 2010 Series A and B bonds mature in 2031 and 2036, respectively. As a result of the bond refinancing, the unamortized bond issuance costs and original issue discount related to the refunded bonds were included in loss on extinguishment of debt of \$13.0 million for the year ended August 31, 2010.

In June 2010, SHC converted the CHFFA 2008 Series A-1 bonds from an annual put mode to a long-term fixed interest rate mode and the bonds mature in 2040. The remarketing of the CHFFA 2008 Series A-1 bonds generated an original issue premium of approximately \$140 thousand; that, pursuant to the requirements of the underlying documents, was used to reduce the principal amount of the bonds from \$70.5 million to \$70.4 million.

SHC has \$168.2 million of VRDBs outstanding, comprised of the CHFFA 2008 Series B-1 bonds which bear interest at a weekly rate which resets every 7 days, and the CHFFA 2008 Series B-2 bonds which bear interest at a commercial paper rate and are outstanding for various interest periods of 270 days or less. Bondholders investing in weekly VRDBs have the option to tender their bonds on a weekly basis. Bondholders in commercial paper mode have the option to tender their bonds only at the end of the commercial paper rate period. The CHFFA 2008 Series B bonds are supported by SHC's self-liquidity.

SHC has irrevocable standby letters of credit in the aggregate amount of \$43.4 million posted with certain beneficiaries in the following amounts and for the following respective purposes: (i) \$20.0 million to support collateral requirements under certain interest rate exchange agreements discussed in *Note 7*, (ii) \$13.4 million to serve as security for the workers' compensation self-insurance arrangement and (iii) \$10.0 million to serve as a security deposit for certain construction projects being undertaken by SHC. No amounts have been drawn on these letters of credit at August 31, 2011 and 2010.

LPCH

LPCH has \$93.5 million of VRDBs outstanding, consisting of the CHFFA 2008 Series A, B and C bonds, which may bear interest at a daily, weekly, commercial paper, long term or auction rate, as defined by the LPCH Master Indenture. The bonds of each series currently bear interest at a weekly rate, which resets every 7 days. Bondholders have the option to tender their bonds on a weekly basis. In order to ensure the availability of funds to purchase any bonds tendered that the remarketing agent is unable to remarket, LPCH has entered into a liquidity agreement with the University. The agreement, which expires November 9, 2013, allows access on a same-day basis of up to \$100.0 million of cash against LPCH's investments in the University's MP.

LPCH has irrevocable standby letters of credit in the aggregate amount of \$12.0 million posted with certain beneficiaries in the following amounts and for the following respective purposes: (i) \$5.4 million to serve as security for the workers' compensation self-insurance arrangement and (ii) \$6.6 million to serve as a security deposit for certain construction projects being undertaken by LPCH. No amounts have been drawn on these letters of credit at August 31, 2011 and 2010.

INTEREST

The Hospitals incurred interest expense of approximately \$50.3 million and \$42.4 million for the years ended August 31, 2011 and 2010, respectively, which is net of \$0 and \$19 thousand, respectively, of interest income and approximately \$1.7 million and \$1.3 million, respectively, in interest capitalized as a cost of construction. Interest expense includes net payments on interest rate exchange agreements of \$19.9 million and \$19.6 million for the years ended August 31, 2011 and 2010, respectively.

PRINCIPAL PAYMENTS

Estimated principal payments on bonds, promissory notes and capital lease obligations, in thousands of dollars, are as follows:

YEAR ENDING AUGUST 31	PRINCIPAL PAYMENTS
2012 Variable debt subject to remarketing	\$ 261,650
2012 Other	25,039
2013	13,230
2014	14,893
2015	14,120
2016	15,890
Thereafter	619,285
TOTAL	\$ 964,107

12. University Endowment

The University classifies a substantial portion of its financial resources as endowment, which is invested to generate income to be used to support operating and strategic initiatives. The endowment is comprised of pure endowment funds (which include endowed lands), term endowment funds, and funds functioning as endowment (FFE). Depending on the nature of the donor's stipulation, these resources are recorded as permanently restricted, temporarily restricted or unrestricted net assets. Term endowments are similar to other endowment funds except that, upon the passage of a stated period of time or the occurrence of a particular event, all or part of the principal may be expended. These resources are classified as temporarily restricted net assets. FFE are University resources designated by the Board as endowment and are invested for long-term appreciation and current income. These assets, however, remain available and may be spent at the Board's discretion. Accordingly, FFE are recorded as unrestricted net assets.

The University classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment and (b) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are authorized for expenditure. In the absence of donor stipulations or law to the contrary, net unrealized losses on permanently restricted endowment funds first reduce related appreciation on temporarily restricted net assets and then on unrestricted net assets, as needed, until such time as the fair value of the fund equals or exceeds historic value. The aggregate amount by which fair value was below historic value was \$34.9 million and \$130.1 million at August 31, 2011 and 2010, respectively.

Endowment funds by net asset classification at August 31, 2011 and 2010, in thousands of dollars, are as follows:

	UNRESTRICTED	TEMPORARILY RESTRICTED	PERMANENTLY RESTRICTED	TOTAL
2011				
Donor-restricted endowment funds	\$ (34,907)	\$ 5,215,842	\$ 4,645,015	\$ 9,825,950
Funds functioning as endowment	6,676,656	-	-	6,676,656
TOTAL ENDOWMENT FUNDS	\$ 6,641,749	\$ 5,215,842	\$ 4,645,015	\$ 16,502,606
2010				
Donor-restricted endowment funds	\$ (130,134)	\$ 4,340,344	\$ 4,349,295	\$ 8,559,505
Funds functioning as endowment	5,291,610	-	-	5,291,610
TOTAL ENDOWMENT FUNDS	\$ 5,161,476	\$ 4,340,344	\$ 4,349,295	\$ 13,851,115

Most of the University's endowment is invested in the MP. The return objective for the MP is to generate optimal long-term total return while maintaining an appropriate level of risk for the University. Investment returns are achieved through both capital appreciation (realized and unrealized gains) and current yield (interest and dividends). Portfolio asset allocation targets as well as expected risk, return and correlation among the asset classes are reevaluated annually by Stanford Management Company.

Through the combination of investment strategy and payout policy, the University is striving to provide a reasonably consistent payout from endowment to support operations, while preserving the purchasing power of the endowment adjusted for inflation.

The Board approves the amounts to be paid out annually from endowment funds invested in the MP. Consistent with the Uniform Prudent Management of Institutional Funds Act, when determining the appropriate payout the Board considers the purposes of the University and the endowment, the duration and preservation of the endowment, general economic conditions, the possible effect of inflation or deflation, the expected return from income and the appreciation of investments, other resources of the University, and the University's investment policy.

The current Board approved targeted spending rate is 5.5%. The sources of payout are earned income on endowment assets (interest, dividends, rents and royalties), realized capital gains and FFE, as needed and as available.

Changes in the University's endowment, excluding pledges, for the years ended August 31, 2011 and 2010, in thousands of dollars, are as follows:

	UNRESTRICTED	TEMPORARILY RESTRICTED	PERMANENTLY RESTRICTED	TOTAL
2011				
Endowment, beginning of year	\$ 5,161,476	\$ 4,340,344	\$ 4,349,295	\$ 13,851,115
Investment returns:				
Earned income	153,196	-	-	153,196
Unrealized and realized gains	1,253,259	1,337,066	19,611	2,609,936
Total investment returns	1,406,455	1,337,066	19,611	2,763,132
Amounts distributed for operations	(312,540)	(472,541)	-	(785,081)
Gifts, transfers and other changes in endowment:				
Current year gifts and pledge payments	4,234	14,062	144,497	162,793
Transfers of prior year gifts	3,439	(1,752)	76,079	77,766
Funds invested in endowment, net	63,880	2,120	55,358	121,358
EFP funds invested in the endowment	316,011	-	-	316,011
Other	(1,206)	(3,457)	175	(4,488)
Total gifts, transfers and other changes in endowment	386,358	10,973	276,109	673,440
Total net increase in endowment	1,480,273	875,498	295,720	2,651,491
ENDOWMENT, END OF YEAR	\$ 6,641,749	\$ 5,215,842	\$ 4,645,015	\$ 16,502,606
2010				
Endowment, beginning of year	\$ 4,520,298	\$ 3,917,921	\$ 4,180,875	\$ 12,619,094
Investment returns:				
Earned income	107,300	-	-	107,300
Unrealized and realized gains	538,524	909,306	14,458	1,462,288
Total investment returns	645,824	909,306	14,458	1,569,588
Amounts distributed for operations	(293,998)	(560,647)	-	(854,645)
Gifts, transfers and other changes in endowment:				
Current year gifts and pledge payments	1,247	1,473	108,763	111,483
Transfers of prior year gifts	3,910	-	49,816	53,726
Funds invested in endowment, net ¹	9,241	630	83,343	93,214
EFP funds invested in the endowment	251,023	-	-	251,023
Transfers due to donor redesignations and other reclassifications ²	34,700	81,828	(116,528)	-
Other	(10,769)	(10,167)	28,568	7,632
Total gifts, transfers and other changes in endowment	289,352	73,764	153,962	517,078
Total net increase in endowment	641,178	422,423	168,420	1,232,021
ENDOWMENT, END OF YEAR	\$ 5,161,476	\$ 4,340,344	\$ 4,349,295	\$ 13,851,115

¹ \$58.2 million of endowment funds used to support pediatric research programs were transferred from the Hospitals to the University in 2010.

² During the year ended August 31, 2010, the payout requirements of certain endowment funds were changed pursuant to donor requests or court decrees. Similar to many other endowment funds, income and a reasonable portion of gains as determined by the Board may be expended for donor intended purposes. Under U.S. GAAP, any accumulated appreciation related to these funds must be reclassified from permanently restricted net assets to unrestricted or temporarily restricted net assets.

13. Hospitals Endowments

The endowments of SHC and LPCH are intended to generate investment income that can be used to support their current operating and strategic initiatives. The Hospitals invest the majority of their endowments in the University's MP. As such, the Hospitals endowments are subject to the same investment and spending strategies as described in *Note 12*. These policies provide for annual amounts (payout) to be distributed for current use. "Amounts distributed for operations" in the table below represents the Hospitals' current year endowment payout spent for designated purposes during fiscal years 2011 and 2010.

The Hospitals classify as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment and (b) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are authorized for expenditure. In the absence of donor stipulations or law to the contrary, net unrealized losses on permanently restricted endowment funds first reduce related appreciation on temporarily restricted net assets and then on unrestricted net assets, as needed, until such time as the fair value of the fund equals or exceeds historic value. The aggregate amount by which fair value was below historic value was approximately \$277 thousand and \$2.3 million at August 31, 2011 and 2010, respectively.

Changes in Hospitals endowments, for the years ended August 31, 2011 and 2010, in thousands of dollars, are as follows:

	UNRESTRICTED	TEMPORARILY RESTRICTED	PERMANENTLY RESTRICTED	TOTAL
2011				
Endowments, beginning of year	\$ (2,285)	\$ 53,161	\$ 231,523	\$ 282,399
Investment returns:				
Earned income	-	13,275	-	13,275
Unrealized and realized gains	2,008	27,235	929	30,172
Total investment returns	2,008	40,510	929	43,447
Amounts distributed for operations	-	(13,977)	-	(13,977)
Gifts, transfers and other changes in endowments:				
Gifts and pledge payments	-	-	34	34
Transfer of funds to the University and other	-	(886)	(27,136)	(28,022)
Total gifts, transfers and other changes in endowments	-	(886)	(27,102)	(27,988)
Total net increase (decrease) in endowments	2,008	25,647	(26,173)	1,482
ENDOWMENTS, END OF YEAR	\$ (277)	\$ 78,808	\$ 205,350	\$ 283,881
2010				
Endowments, beginning of year	\$ (10,918)	\$ 46,037	\$ 289,081	\$ 324,200
Investment returns:				
Earned income	-	14,535	-	14,535
Unrealized and realized gains	8,633	10,511	510	19,654
Total investment returns	8,633	25,046	510	34,189
Amounts distributed for operations	-	(15,362)	-	(15,362)
Gifts, transfers and other changes in endowments:				
Gifts and pledge payments	-	368	213	581
Transfer of funds to the University and other	-	(2,928)	(58,281)	(61,209)
Total gifts, transfers and other changes in endowments	-	(2,560)	(58,068)	(60,628)
Total net increase (decrease) in endowments	8,633	7,124	(57,558)	(41,801)
ENDOWMENTS, END OF YEAR	\$ (2,285)	\$ 53,161	\$ 231,523	\$ 282,399

¹ \$58.2 million of endowment funds used to support pediatric research programs were transferred from the Hospitals to the University in 2010.

All of the Hospitals endowments are classified as donor-restricted.

14. University Gifts and Pledges

The University's Office of Development (OOD) reports total gifts based on contributions received in cash or property during the fiscal year. Gifts and pledges reported for financial statement purposes are recorded on the accrual basis. The following summarizes gifts and pledges reported for the years ended August 31, 2011 and 2010, per the *Statements of Activities* reconciled to the cash basis reported by OOD, in thousands of dollars:

	2011	2010
Current year gifts in support of operations	\$ 163,692	\$ 159,701
Donor advised funds, net	1,057	35,444
Current year gifts not included in operations	4,237	1,238
Temporarily restricted gifts and pledges, net	196,615	189,941
Permanently restricted gifts and pledges, net	150,813	107,352
TOTAL PER STATEMENT OF ACTIVITIES	516,414	493,676
Adjustments to arrive at gift total as reported by OOD:		
New pledges	(227,331)	(174,831)
Payments made on pledges	272,227	198,630
Pledge discounts and other adjustments	18,676	(5,097)
Donor advised funds not designated for Stanford	3,484	(22,851)
Non-cash gifts	4,791	3,248
Non-government grants, recorded as sponsored research support when earned	84,745	87,151
SHC gifts	35,152	15,630
Other	1,265	3,334
TOTAL AS REPORTED BY OOD	\$ 709,423	\$ 598,890

15. Functional Expenses

Expenses for each of the years ended August 31, 2011 and 2010 are categorized on a functional basis as follows, in thousands of dollars:

	2011			2010
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
Instruction and departmental research	\$ 1,160,021	\$ -	\$ 1,160,021	\$ 1,104,447
Organized research - direct costs	1,019,584	-	1,019,584	927,700
Patient services	-	2,187,914	2,187,914	1,960,074
Auxiliary activities	676,687	-	676,687	642,121
Administration and general	247,485	155,852	403,337	374,295
Libraries	159,112	-	159,112	148,430
Student services	126,644	-	126,644	130,587
Development	76,470	12,461	88,931	86,911
SLAC construction	44,076	-	44,076	48,523
TOTAL EXPENSES	\$ 3,510,079	\$ 2,356,227	\$ 5,866,306	\$ 5,423,088

Depreciation, interest, operations and maintenance expenses are allocated to program and supporting activities, except for SLAC construction. Auxiliary activities include housing and dining services, intercollegiate athletics, Stanford Alumni Association, other activities and patient care provided by the School of Medicine faculty.

16. University Retirement Plans

The University provides retirement benefits through both contributory and noncontributory retirement plans for substantially all of its employees.

DEFINED CONTRIBUTION PLAN

The University offers a defined contribution plan to eligible faculty and staff. University and participant contributions are primarily invested in annuities and mutual funds. University contributions under this plan, which are vested immediately to participants, were approximately \$104.4 million and \$99.4 million for the years ended August 31, 2011 and 2010, respectively.

DEFINED BENEFIT PLANS

The University provides retirement and postretirement medical and other benefits through three defined benefit plans: the *Staff Retirement Annuity Plan*, the *Faculty Retirement Incentive Program*, and the *University Postretirement Benefit Plan* (the "Plans"). The obligations for the Plans, net of plan assets, are recorded in the *Statements of Financial Position* as "accrued pension and post retirement benefit cost". These are described more fully below.

Staff Retirement Annuity Plan

Retirement benefits for certain employees are provided through the *Staff Retirement Annuity Plan* (SRAP), a noncontributory plan. The SRAP is closed to new participants. The University's policy is to fund pension costs in accordance with the Employee Retirement Income Security Act's requirements.

Faculty Retirement Incentive Program

The University also provides a retirement incentive bonus for eligible faculty through the University *Faculty Retirement Incentive Program* (FRIP). The University's faculty may become eligible for the FRIP program if they commit to retire within a designated window of time. At August 31, 2011 and 2010, there were no program assets. The University funds benefit payouts as they are incurred.

Postretirement Benefit Plan

The University also provides certain health care benefits for retired employees through its *Postretirement Benefit Plan* (PRBP). The University's employees and their covered dependents may become eligible for the PRBP upon the employee's retirement. Retiree health plans are paid for, in part, by retiree contributions, which are adjusted annually. Health benefits provided and the gross premiums charged (before University subsidies) to retirees under age 65 are the same as those provided to active employees. The University subsidy varies depending on whether the retiree is covered under the traditional design or the defined dollar benefit design. Medicare supplement options are provided for retirees over age 65.

The change in the Plans' assets, the related change in benefit obligations and the amounts recognized in the financial statements, in thousands of dollars, are as follows:

	STAFF RETIREMENT ANNUITY PLAN (SRAP)	FACULTY RETIREMENT INCENTIVE PROGRAM (FRIP)	POST RETIREMENT BENEFIT PLAN (PRBP)	TOTAL
2011				
Change in plan assets:				
Fair value of plan assets, beginning of year	\$ 242,859	\$ -	\$ 106,851	\$ 349,710
Actual return on plan assets	33,585	-	13,282	46,867
Employer contributions	-	1,256	22,147	23,403
Plan participants' contributions	-	-	6,839	6,839
Benefits and plan expenses paid	(17,548)	(1,256)	(20,128) *	(38,932)
FAIR VALUE OF PLAN ASSETS, END OF YEAR	258,896	-	128,991	387,887
Change in projected benefit obligation:				
Benefit obligation, beginning of year	302,698	140,299	461,081	904,078
Service cost	3,782	9,100	14,432	27,314
Interest cost	13,349	6,432	23,814	43,595
Plan participants' contributions	-	-	6,839	6,839
Actuarial (gain) loss	(8,548)	(9,032)	6,242	(11,338)
Benefits and plan expenses paid	(17,548)	(1,256)	(20,128) *	(38,932)
Plan amendments	(336)	-	(21,826)	(22,162)
BENEFIT OBLIGATION, END OF YEAR	293,397	145,543	470,454	909,394
NET LIABILITY RECOGNIZED IN THE STATEMENTS OF FINANCIAL POSITION				
	\$ (34,501)	\$ (145,543)	\$ (341,463)	\$ (521,507)
Prior service cost	\$ 1,879	\$ -	\$ 11,132	\$ 13,011
Net actuarial loss	22,308	107,352	167,753	297,413
ACCUMULATED PLAN BENEFIT COSTS NOT YET RECOGNIZED IN THE STATEMENTS OF ACTIVITIES				
	\$ 24,187	\$ 107,352	\$ 178,885	\$ 310,424
* Net of Medicare subsidy				
2010				
Change in plan assets:				
Fair value of plan assets, beginning of year	\$ 241,296	\$ -	\$ 100,085	\$ 341,381
Actual return on plan assets	18,620	-	5,659	24,279
Employer contributions	-	32,871	13,980	46,851
Plan participants' contributions	-	-	6,796	6,796
Benefits and plan expenses paid	(17,057)	(7,570)	(19,669) *	(44,296)
Settlements on Special Retirement Incentive programs (SRI)	-	(25,301)	-	(25,301)
FAIR VALUE OF PLAN ASSETS, END OF YEAR	242,859	-	106,851	349,710
Change in projected benefit obligation:				
Benefit obligation, beginning of year	270,979	165,937	320,212	757,128
Service cost	3,642	8,481	9,964	22,087
Interest cost	14,863	8,015	20,532	43,410
Plan participants' contributions	-	-	6,796	6,796
Actuarial loss (gain)	30,271	(9,263)	123,246	144,254
Benefits and plan expenses paid	(17,057)	(7,570)	(19,669) *	(44,296)
Settlements on SRI	-	(25,301)	-	(25,301)
BENEFIT OBLIGATION, END OF YEAR	302,698	140,299	461,081	904,078
NET LIABILITY RECOGNIZED IN THE STATEMENTS OF FINANCIAL POSITION				
	\$ (59,839)	\$ (140,299)	\$ (354,230)	\$ (554,368)
Prior service cost	\$ 2,889	\$ -	\$ 40,564	\$ 43,453
Net actuarial loss	50,874	123,806	174,846	349,526
ACCUMULATED PLAN BENEFIT COSTS NOT YET RECOGNIZED IN THE STATEMENTS OF ACTIVITIES				
	\$ 53,763	\$ 123,806	\$ 215,410	\$ 392,979
* Net of Medicare subsidy				

The accumulated benefit obligation for the SRAP was \$289.8 million and \$298.2 million at August 31, 2011 and 2010, respectively.

Net periodic benefit expense and other changes in net assets related to the Plans for the years ended August 31, 2011 and 2010, in thousands of dollars, includes the following components:

	STAFF RETIREMENT ANNUITY PLAN (SRAP)	FACULTY RETIREMENT INCENTIVE PROGRAM (FRIP)	POST RETIREMENT BENEFIT PLAN (PRBP)	TOTAL
2011				
Service cost	\$ 3,782	\$ 9,100	\$ 14,432	\$ 27,314
Interest cost	13,349	6,432	23,814	43,595
Expected return on plan assets	(16,065)	-	(8,643)	(24,708)
Amortization of:				
Prior service cost	674	-	7,605	8,279
Actuarial loss	2,498	7,422	8,696	18,616
NET PERIODIC BENEFIT EXPENSE	4,238	22,954	45,904	73,096
Net actuarial gain during period	(26,068)	(9,032)	-	(35,100)
Amortization of:				
Prior service cost	(674)	-	(7,605)	(8,279)
Actuarial loss	(2,498)	(7,422)	(7,094)	(17,014)
Plan amendments	(336)	-	(21,826)	(22,162)
TOTAL AMOUNTS RECOGNIZED IN CHANGES IN UNRESTRICTED NET ASSETS	(29,576)	(16,454)	(36,525)	(82,555)
TOTAL AMOUNT RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE AND CHANGES IN UNRESTRICTED NET ASSETS	\$ (25,338)	\$ 6,500	\$ 9,379	\$ (9,459)
2010				
Service cost	\$ 3,642	\$ 8,481	\$ 9,964	\$ 22,087
Interest cost	14,863	8,015	20,532	43,410
Expected return on plan assets	(16,002)	-	(8,007)	(24,009)
Amortization of:				
Prior service cost	1,501	-	7,605	9,106
Actuarial loss	-	8,549	2,481	11,030
SRI settlement loss recognized	-	24,319	-	24,319
NET PERIODIC BENEFIT EXPENSE	4,004	49,364	32,575	85,943
Net actuarial loss (gain) during period	27,653	(9,263)	125,594	143,984
Amortization of:				
Prior service cost	(1,501)	-	(7,605)	(9,106)
Actuarial loss	-	(8,549)	(2,481)	(11,030)
SRI settlement loss recognized	-	(24,319)	-	(24,319)
TOTAL AMOUNTS RECOGNIZED IN CHANGES IN UNRESTRICTED NET ASSETS	26,152	(42,131)	115,508	99,529
TOTAL AMOUNT RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE AND CHANGES IN UNRESTRICTED NET ASSETS	\$ 30,156	\$ 7,233	\$ 148,083	\$ 185,472

The prior service costs and net actuarial loss expected to be amortized from change in net assets to net periodic benefit expense in fiscal year 2012, in thousands of dollars, are as follows:

	STAFF RETIREMENT ANNUITY PLAN (SRAP)	FACULTY RETIREMENT INCENTIVE PROGRAM (FRIP)	POST RETIREMENT BENEFIT PLAN (PRBP)
Prior service cost	\$ 534	\$ -	\$ 2,569
Net actuarial loss	\$ -	\$ 6,485	\$ 8,214

ACTUARIAL ASSUMPTIONS

The weighted average assumptions used to determine the benefit obligations for the Plans are shown below:

	STAFF RETIREMENT ANNUITY PLAN (SRAP)		FACULTY RETIREMENT INCENTIVE PROGRAM (FRIP)		POST RETIREMENT BENEFIT PLAN (PRBP)	
	2011	2010	2011	2010	2011	2010
Discount rate	4.67%	4.61%	4.74%	4.67%	5.14%	5.10%
Covered payroll growth rate	4.41%	4.76%	4.43%	4.14%	3.50%	3.50%

The weighted average assumptions used to determine the net periodic benefit cost for the Plans are shown below:

	STAFF RETIREMENT ANNUITY PLAN (SRAP)		FACULTY RETIREMENT INCENTIVE PROGRAM (FRIP)		POST RETIREMENT BENEFIT PLAN (PRBP)	
	2011	2010	2011	2010	2011	2010
Discount rate	4.61%	5.75%	4.67%	5.75%	5.10%	6.00%
Expected returns on plan assets	7.00%	7.00%	N/A	N/A	8.00%	8.00%
Covered payroll growth rate	4.76%	4.21%	4.14%	3.50%	3.50%	3.50%

To develop the 7% and the 8% expected long-term rate of return on asset assumptions for the SRAP and PRBP plans, respectively, the University's Retirement Program Investment Committee (RPIC) considered historical returns and future expectations for returns in each asset class, as well as the target asset allocation of the portfolios.

Expected returns on plan assets, a component of net periodic (income)/benefit cost, represent the long-term return on plan assets based on the calculated market-related value of plan assets. These rates of return are developed using an arithmetic average and are tested for reasonableness against historical returns. The use of expected long-term returns on plan assets may result in income that is greater or less than the actual returns of those plan assets in any given year. Over time, however, the expected long-term returns are designed to approximate the actual long-term returns, and therefore result in a pattern of income and cost recognition that more closely matches the pattern of the services provided by the employees. Differences between actual and expected returns are recognized as a component of change in unrestricted net assets and amortized as a component of net periodic (income)/benefit cost over the service life expectancy of the plan participants, depending on the plan, provided such amounts exceed the accounting standards threshold.

To determine the accumulated PRBP obligation at August 31, 2011, an 8% annual rate of increase in the per capita costs of covered health care was assumed for the year ending August 31, 2012, declining gradually to 4.75% by 2024 and remaining at this rate thereafter. For covered dental plans, a constant 5% annual rate of increase was assumed.

Health care cost trend rate assumptions have a significant effect on the amounts reported for the health care plans. Increasing the health care cost trend rate by 1% in each future year would increase the accumulated PRBP obligation by \$70.5 million and the aggregate annual service and interest cost by \$7.2 million. Decreasing the health care cost trend rate by 1% in each future year would decrease the accumulated PRBP obligation by \$57.5 million and the aggregate annual service and interest cost by \$5.7 million.

EXPECTED CONTRIBUTIONS

The University expects to contribute \$10.2 million and \$26.7 million to its SRAP and PRBP, respectively, during the year ending August 31, 2012.

EXPECTED BENEFIT PAYMENTS

The following benefit payments, which reflect expected future service, are expected to be paid, in thousands of dollars, for the years ending August 31:

YEAR ENDING AUGUST 31	STAFF	FACULTY	POST RETIREMENT BENEFIT	
	RETIREMENT ANNUITY PLAN (SRAP)	RETIREMENT INCENTIVE PROGRAM (FRIP)	PLAN (PRBP) EXCLUDING MEDICARE SUBSIDY	MEDICARE PART D SUBSIDY
2012	\$ 25,342	\$ 3,668	\$ 18,625	\$ 2,358
2013	23,543	6,890	19,960	2,632
2014	22,676	8,755	21,271	2,911
2015	23,310	11,426	22,633	3,219
2016	23,454	12,307	23,980	3,569
2017 - 2021	110,048	73,994	144,207	24,193

INVESTMENT STRATEGY

The RPIC, acting in a fiduciary capacity, has established formal investment policies for the assets associated with the University's funded plans (SRAP and PRBP). The investment strategy of the plans is to preserve and enhance the value of the plans' assets within acceptable levels of risk. Investments in the plans are diversified among asset classes, striving to achieve an optimal balance between risk and return, and income and capital appreciation. Because the liabilities of each of the plans are long-term, the investment horizon is primarily long-term, with adequate liquidity to meet short-term benefit payment obligations.

CONCENTRATION OF RISK

The University manages a variety of risks, including market, credit, and liquidity risks, across its plan assets. Concentration of risk is defined as an undiversified exposure to one of the above-mentioned risks that increases the exposure of the loss of plan assets unnecessarily. Risk is minimized by predominately investing in broadly diversified index funds for public equities and fixed income. As of August 31, 2011, the University did not have concentrations of risk in any single entity, counterparty, sector, industry or country.

PLAN ASSET ALLOCATIONS

Actual allocations by asset category at August 31, 2011 and 2010 are as follows:

ASSET CATEGORY	STAFF RETIREMENT ANNUITY PLAN (SRAP)		POST RETIREMENT BENEFIT PLAN (PRBP)	
	2011	2010	2011	2010
Cash and cash equivalents	1%	1%	0%	0%
Public equities	40%	44%	74%	75%
Fixed income	59%	55%	26%	25%
Private equities	<1%	<1%	0%	0%
TOTAL PORTFOLIO	100%	100%	100%	100%

For fiscal years 2011 and 2010, the weighted-average target allocations by asset category are as follows:

ASSET CATEGORY	STAFF RETIREMENT ANNUITY PLAN (SRAP)		POST RETIREMENT BENEFIT PLAN (PRBP)	
	2011	2010	2011	2010
Public equities	45%	45%	75%	75%
Fixed income	55%	55%	25%	25%
TARGET PORTFOLIO	100%	100%	100%	100%

FAIR VALUE OF PLAN ASSETS

Current U.S GAAP defines a hierarchy of valuation inputs for the determination of the fair value of plan assets as described in *Note 5*. The plan assets measured at fair value at August 31, 2011 and 2010, in thousands of dollars, are as follows:

	AS OF AUGUST 31,			
	2011	LEVEL 1	LEVEL 2	LEVEL 3
SRAP:				
Cash and cash equivalents	\$ 1,721	\$ 1,721	\$ -	\$ -
Public equities	103,246	103,246	-	-
Fixed income	153,282	149,106	4,176	-
Private equities	647	-	-	647
TOTAL	\$ 258,896	\$ 254,073	\$ 4,176	\$ 647
PRBP:				
Public equities	\$ 95,358	\$ 95,358	\$ -	\$ -
Fixed income	33,633	33,633	-	-
TOTAL	\$ 128,991	\$ 128,991	\$ -	\$ -
TOTAL FAIR VALUE OF PLAN ASSETS	\$ 387,887	\$ 383,064	\$ 4,176	\$ 647

	AS OF AUGUST 31,			
	2010	LEVEL 1	LEVEL 2	LEVEL 3
SRAP:				
Cash and cash equivalents	\$ 1,093	\$ 1,093	\$ -	\$ -
Public equities	105,939	105,939	-	-
Fixed income	135,142	130,350	4,792	-
Private equities	685	-	-	685
TOTAL	\$ 242,859	\$ 237,382	\$ 4,792	\$ 685
PRBP:				
Public equities	\$ 80,147	\$ 80,147	\$ -	\$ -
Fixed income	26,704	26,704	-	-
TOTAL	\$ 106,851	\$ 106,851	\$ -	\$ -
TOTAL FAIR VALUE OF PLAN ASSETS	\$ 349,710	\$ 344,233	\$ 4,792	\$ 685

The following table presents a reconciliation of beginning and ending balances for Level 3 investments in the SRAP for the years ended August 31, 2011 and 2010, in thousands of dollars:

FAIR VALUE MEASUREMENTS USING SIGNIFICANT UNOBSERVABLE INPUTS (LEVEL 3)	BEGINNING BALANCE AS OF SEPTEMBER 1, 2010	NET PURCHASES (SALES AND MATURITIES)	REALIZED GAINS (LOSSES)	CHANGE IN UNREALIZED GAINS (LOSSES)	NET TRANSFERS IN (OUT)	ENDING BALANCE AS OF AUGUST 31, 2011
Private equities	\$ 685	\$ -	\$ -	\$ (38)	\$ -	\$ 647
TOTAL	\$ 685	\$ -	\$ -	\$ (38)	\$ -	\$ 647

FAIR VALUE MEASUREMENTS USING SIGNIFICANT UNOBSERVABLE INPUTS (LEVEL 3)	BEGINNING BALANCE AS OF SEPTEMBER 1, 2009	NET PURCHASES (SALES AND MATURITIES)	REALIZED GAINS (LOSSES)	CHANGE IN UNREALIZED GAINS (LOSSES)	NET TRANSFERS IN (OUT)	ENDING BALANCE AS OF AUGUST 31, 2010
Private equities	\$ 700	\$ -	\$ -	\$ (15)	\$ -	\$ 685
TOTAL	\$ 700	\$ -	\$ -	\$ (15)	\$ -	\$ 685

17. Hospitals Retirement Plans

The Hospitals provide retirement benefits through defined benefit and defined contribution retirement plans covering substantially all regular employees.

DEFINED CONTRIBUTION PLAN

Employer contributions to the defined contribution retirement plan are based on a percentage of participant annual compensation. Employer contributions to this plan amounted to approximately \$65.4 million and \$61.3 million for the years ended August 31, 2011 and 2010, respectively.

DEFINED BENEFIT PLANS

Certain employees of the Hospitals are covered by the *Staff Pension Plan* (the "Pension Plan"), a noncontributory, defined benefit pension plan. Benefits of certain prior employees of LPCH are covered by a frozen defined benefit plan. Benefits are based on years of service and the employee's compensation. Contributions to the plans are based on actuarially determined amounts sufficient to meet the benefits to be paid to plan participants.

POST RETIREMENT MEDICAL BENEFIT PLAN

The Hospitals currently provide health insurance coverage for certain retired employees through its *Post Retirement Medical Benefit Plan* (PRMB). The Hospitals' employees and their covered dependents may become eligible for the PRMB upon the employee's retirement as early as age 55, with years of service as defined by specific criteria. Retiree health plans are paid, in part, by retiree contributions, which are adjusted annually. The Hospitals provide a subsidy which varies depending on whether the retiree is covered under the traditional design or the defined dollar benefit design. A Medicare supplement option is provided for retirees over age 65. The obligation for these benefits has been recorded in the *Statements of Financial Position* as "accrued pension and post retirement benefit cost".

The change in Pension Plan and PRMB plans' assets, the related change in benefit obligations and the amounts recognized in the financial statements, in thousands of dollars, are as follows:

	STANFORD PENSION PLAN	POST RETIREMENT MEDICAL BENEFIT PLAN (PRMB)	TOTAL
2011			
Change in plan assets:			
Fair value of plan assets, beginning of year	\$ 135,133	\$ -	\$ 135,133
Actual return on plan assets	14,271	-	14,271
Employer contributions	19,200	3,733	22,933
Plan participants' contributions	-	992	992
Benefits and plan expenses paid	(9,021)	(4,725)	(13,746)
FAIR VALUE OF PLAN ASSETS, END OF YEAR	159,583	-	159,583
Change in projected benefit obligation:			
Benefit obligation, beginning of year	211,610	90,850	302,460
Service cost	2,516	2,775	5,291
Interest cost	10,311	4,157	14,468
Plan participants' contributions	-	992	992
Actuarial gain	(2,600)	(5,843)	(8,443)
Benefits and plan expenses paid	(9,021)	(4,725)	(13,746)
BENEFIT OBLIGATION, END OF YEAR	212,816	88,206	301,022
NET LIABILITY RECOGNIZED IN THE STATEMENTS OF FINANCIAL POSITION			
Prior service cost	\$ -	\$ 3,168	\$ 3,168
Net actuarial loss	81,163	3,356	84,519
ACCUMULATED PLAN BENEFIT COSTS NOT YET RECOGNIZED IN THE STATEMENTS OF ACTIVITIES			
	\$ 81,163	\$ 6,524	\$ 87,687
2010			
Change in plan assets:			
Fair value of plan assets, beginning of year	\$ 116,779	\$ -	\$ 116,779
Actual return on plan assets	14,383	-	14,383
Employer contributions	13,830	3,298	17,128
Plan participants' contributions	-	782	782
Benefits and plan expenses paid	(7,511)	(4,080)	(11,591)
Settlements	(2,348)	-	(2,348)
FAIR VALUE OF PLAN ASSETS, END OF YEAR	135,133	-	135,133
Change in projected benefit obligation:			
Benefit obligation, beginning of year	183,256	78,828	262,084
Service cost	1,723	2,357	4,080
Interest cost	10,895	4,458	15,353
Plan participants' contributions	-	782	782
Actuarial loss	25,119	8,505	33,624
Benefits and plan expenses paid	(7,511)	(4,080)	(11,591)
Settlements	(1,872)	-	(1,872)
BENEFIT OBLIGATION, END OF YEAR	211,610	90,850	302,460
NET LIABILITY RECOGNIZED IN THE STATEMENTS OF FINANCIAL POSITION			
Prior service cost	\$ -	\$ 2,594	\$ 2,594
Net actuarial loss	90,024	9,895	99,919
ACCUMULATED PLAN BENEFIT COSTS NOT YET RECOGNIZED IN THE STATEMENTS OF ACTIVITIES			
	\$ 90,024	\$ 12,489	\$ 102,513

The accumulated benefit obligation for the Pension Plan was \$209.2 million and \$207.2 million at August 31, 2011 and 2010, respectively.

Net periodic benefit expense and other changes in net assets related to the plans for the years ended August 31, 2011 and 2010, in thousands of dollars, includes the following components:

	STANFORD PENSION PLAN	POST RETIREMENT MEDICAL BENEFIT PLAN (PRMB)	TOTAL
2011			
Service cost	\$ 2,516	\$ 2,775	\$ 5,291
Interest cost	10,311	4,157	14,468
Expected return on plan assets	(13,187)	-	(13,187)
Amortization of:			
Prior service credit	-	(574)	(574)
Actuarial loss	5,177	696	5,873
NET PERIODIC BENEFIT EXPENSE	4,817	7,054	11,871
Net actuarial gain during period	(3,684)	(5,843)	(9,527)
Amortization of:			
Prior service credit	-	574	574
Actuarial loss	(5,177)	(696)	(5,873)
TOTAL AMOUNTS RECOGNIZED IN CHANGES IN UNRESTRICTED NET ASSETS	(8,861)	(5,965)	(14,826)
TOTAL AMOUNT RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE AND CHANGES IN UNRESTRICTED NET ASSETS	\$ (4,044)	\$ 1,089	\$ (2,955)
2010			
Service cost	\$ 1,723	\$ 2,357	\$ 4,080
Interest cost	10,895	4,458	15,353
Expected return on plan assets	(12,866)	-	(12,866)
Amortization of:			
Prior service credit	-	(574)	(574)
Actuarial loss	1,346	105	1,451
NET PERIODIC BENEFIT EXPENSE	1,098	6,346	7,444
Net actuarial loss during period	24,078	8,505	32,583
Amortization of:			
Prior service credit	-	574	574
Actuarial loss	(1,346)	(105)	(1,451)
TOTAL AMOUNTS RECOGNIZED IN CHANGES IN UNRESTRICTED NET ASSETS	22,732	8,974	31,706
TOTAL AMOUNT RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE AND CHANGES IN UNRESTRICTED NET ASSETS	\$ 23,830	\$ 15,320	\$ 39,150

The prior service cost and net actuarial loss expected to be amortized from change in net assets to net periodic benefit expense in fiscal year 2012, in thousands of dollars, are as follows:

	STANFORD PENSION PLAN	POST RETIREMENT MEDICAL BENEFIT PLAN (PRMB)	TOTAL
Prior service cost	\$ -	\$ 264	\$ 264
Net actuarial loss	\$ 5,607	\$ 245	\$ 5,852

ACTUARIAL ASSUMPTIONS

The weighted average assumptions used to determine the benefit obligations for the Pension Plan and PRMB are shown below:

	STANFORD PENSION PLAN		POST RETIREMENT MEDICAL BENEFIT PLAN (PRMB)	
	2011	2010	2011	2010
Discount rate	4.83% - 5.03%	4.79% - 4.99%	4.79%	4.70%
Covered payroll growth rate	5.50%	5.50%	N/A	N/A

The weighted average assumptions used to determine the net periodic benefit cost for the Pension Plan and PRMB are shown below:

	STANFORD PENSION PLAN		POST RETIREMENT MEDICAL BENEFIT PLAN (PRMB)	
	2011	2010	2011	2010
Discount rate	4.79% - 4.99%	5.93% - 6.10%	4.70%	5.83%
Expected return on plan assets	6.25% - 8.00%	6.25% - 8.00%	N/A	N/A
Covered payroll growth rate	5.50%	5.50%	N/A	N/A

To develop the expected long-term rate of return on assets assumptions, the Hospitals considered the historical returns and the future expectations for returns for each asset class, as well as the target asset allocation of the pension portfolio.

To determine the accumulated PRMB obligation at August 31, 2011, an 8.5% annual rate of increase in the pre-65 per capita costs, an 8.5% annual rate of increase in the post-65 prescription drug per capita costs, and a 7.0% rate of increase in the post-65 per capita cost of all other medical benefits was assumed for 2011, all declining gradually to 4.75% by 2024 and remaining at this rate thereafter.

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. Increasing the health care cost trend rate by 1% in each future year would increase the accumulated PRMB obligation by \$2.9 million and the aggregate annual service and interest cost by \$262 thousand. Decreasing the health care cost trend rate by 1% in each future year would decrease the accumulated PRMB obligation by \$2.6 million and the aggregate annual service and interest cost by \$236 thousand.

EXPECTED CONTRIBUTIONS

The Hospitals expect to contribute \$9.4 million to their Pension Plan and \$4.9 million to their PRMB during the fiscal year ending August 31, 2012.

EXPECTED BENEFIT PAYMENTS

The following benefit payments, which reflect expected future service, are expected to be paid for the fiscal years ending August 31, in thousands of dollars:

YEAR ENDING AUGUST 31	STANFORD PENSION PLAN	POST RETIREMENT MEDICAL BENEFIT PLAN (PRMB)	
		EXCLUDING MEDICARE SUBSIDY	EXPECTED MEDICARE PART D SUBSIDY
2012	\$ 10,151	\$ 5,427	\$ 515
2013	10,790	6,040	572
2014	11,486	6,579	632
2015	12,233	7,027	696
2016	12,914	7,376	762
2017 - 2021	72,127	38,338	4,729

INVESTMENT STRATEGY

The Hospitals' investment strategy for the Pension Plan is to maximize the total rate of return (income and appreciation) within the limits of prudent risk taking and Section 404 of the Employee Retirement Income Security Act. The funds are diversified across asset classes to achieve an optimal balance between risk and return and between income and capital appreciation. Many of the pension liabilities are long-term. The investment horizon is also long-term; however, the investment plan also ensures adequate near-term liquidity to meet benefit payments.

CONCENTRATION OF RISK

The Hospitals manage a variety of risks, including market, credit, and liquidity risks, across its plan assets. Concentration of risk is defined as an undiversified exposure to one of the above-mentioned risks that increases the exposure of the loss of plan assets unnecessarily. Risk is minimized by diversifying the Hospitals' exposure to such risks across a variety of instruments, markets, and counterparties. As of August 31, 2011, the Hospitals did not have concentrations of risk in any single entity, counterparty, sector, industry or country.

PLAN ASSETS

Actual allocations by asset category at August 31, 2011 and 2010 are as follows:

ASSET CATEGORY	STANFORD PENSION PLAN	
	2011	2010
Cash equivalents	0%	0%
Public equities	44%	43%
Fixed income	56%	51%
Real estate	0%	6%
TOTAL PORTFOLIO	100%	100%

The Hospitals' investment policy is to invest in assets that result in a favorable long-term rate of return from a diversified portfolio. For fiscal years 2011 and 2010, the weighted-average target allocations by asset category are as follows:

ASSET CATEGORY	STANFORD PENSION PLAN	
	2011	2010
Cash equivalents	<1%	<1%
Public equities	46%	46%
Fixed income	44%	44%
Real estate	10%	10%
TARGET PORTFOLIO	100%	100%

FAIR VALUE OF PLAN ASSETS

Current U.S. GAAP defines a hierarchy of valuation inputs for the determination of the fair value of plan assets as described in *Note 5*. The Pension Plan assets measured at fair value at August 31, 2011 and 2010, in thousands of dollars, are as follows:

	AS OF			
	AUGUST 31, 2011	LEVEL 1	LEVEL 2	LEVEL 3
Cash and cash equivalents	\$ 727	\$ 727	\$ -	\$ -
Public equities	70,609	70,609	-	-
Fixed income	88,247	88,247	-	-
TOTAL FAIR VALUE OF PENSION PLAN ASSETS	\$ 159,583	\$ 159,583	\$ -	\$ -

	AS OF			
	AUGUST 31, 2010	LEVEL 1	LEVEL 2	LEVEL 3
Cash and cash equivalents	\$ 670	\$ 670	\$ -	\$ -
Public equities	58,384	58,384	-	-
Fixed income	68,609	68,609	-	-
Real estate	7,458	-	-	7,458
Other	12	12	-	-
TOTAL FAIR VALUE OF PENSION PLAN ASSETS	\$ 135,133	\$ 127,675	\$ -	\$ 7,458

The following table presents a reconciliation of beginning and ending balances for Level 3 investments in the Pension Plan for the years ended August 31, 2011 and 2010, in thousands of dollars:

FAIR VALUE MEASUREMENTS USING SIGNIFICANT UNOBSERVABLE INPUTS (LEVEL 3)	BEGINNING BALANCE AS OF SEPTEMBER 1, 2010	NET PURCHASES (SALES AND MATURITIES)	REALIZED GAINS (LOSSES)	CHANGE IN UNREALIZED GAINS (LOSSES)	NET TRANSFERS IN (OUT)	ENDING BALANCE AS OF AUGUST 31, 2011
Real estate	\$ 7,458	\$ (8,256)	\$ (2,457)	\$ 3,255	\$ -	\$ -
TOTAL	\$ 7,458	\$ (8,256)	\$ (2,457)	\$ 3,255	\$ -	\$ -

FAIR VALUE MEASUREMENTS USING SIGNIFICANT UNOBSERVABLE INPUTS (LEVEL 3)	BEGINNING BALANCE AS OF SEPTEMBER 1, 2009	NET PURCHASES (SALES AND MATURITIES)	REALIZED GAINS (LOSSES)	CHANGE IN UNREALIZED GAINS (LOSSES)	NET TRANSFERS IN (OUT)	ENDING BALANCE AS OF AUGUST 31, 2010
Real estate	\$ 8,301	\$ (146)	\$ 473	\$ (1,170)	\$ -	\$ 7,458
TOTAL	\$ 8,301	\$ (146)	\$ 473	\$ (1,170)	\$ -	\$ 7,458

18. Operating Leases

The University and the Hospitals lease certain equipment and facilities under operating leases expiring at various dates. Total rental expense under these leases for the years ended August 31, 2011 and 2010 was \$32.8 million and \$28.9 million, respectively, for the University and \$50.0 million and \$51.6 million, respectively, for the Hospitals.

Net minimum future operating lease payments and related present value, assuming a 3.95% discount rate for periods subsequent to August 31, 2011, in thousands of dollars, are as follows:

YEAR ENDING AUGUST 31	MINIMUM LEASE PAYMENTS		PRESENT VALUE OF MINIMUM LEASE PAYMENTS	
	UNIVERSITY	HOSPITALS	UNIVERSITY	HOSPITALS
2012	\$ 23,443	\$ 41,630	\$ 22,552	\$ 40,048
2013	19,756	41,114	18,283	38,049
2014	16,035	31,799	14,276	28,310
2015	13,113	25,659	11,230	21,976
2016	12,920	23,490	10,645	19,354
Thereafter	63,376	114,659	42,553	84,103
TOTAL	\$ 148,643	\$ 278,351	\$ 119,539	\$ 231,840

19. Related Party Transactions

Members of the University's Board and senior management may, from time to time, be associated, either directly or indirectly, with companies doing business with the University. For senior management, the University requires annual disclosure of significant financial interests in, or employment or consulting relationships with, entities doing business with the University. These annual disclosures cover both senior management and their immediate family members. When such relationships exist, measures are taken to appropriately manage the actual or perceived conflict in the best interests of the University. The University has a written conflict of interest policy that requires, among other things, that no member of the Board can participate in any decision in which he or she (or an immediate family member) has a material financial interest. Each trustee is required to certify compliance with the conflict of interest policy on an annual basis and indicate whether the University does business with an entity in which a trustee has a material financial interest. When such relationships exist, measures are taken to mitigate any actual or perceived conflict, including requiring that such transactions be conducted at arm's length, for good and sufficient consideration, based on terms that are fair and reasonable to and for the benefit of the University, and in accordance with applicable conflict of interest laws. No such associations are considered to be significant.

20. Commitments and Contingencies

Management is of the opinion that none of the following commitments and contingencies will have a material adverse effect on the University's consolidated financial position.

SPONSORED PROJECTS

The University conducts substantial research for the federal government pursuant to contracts and grants from federal agencies and departments. The University records reimbursements of direct and indirect costs (facilities and administrative costs) from grants and contracts as operating revenues. The Office of Naval Research is the University's cognizant federal agency for determining indirect cost rates charged to federally sponsored agreements. It is supported by the Defense Contract Audit Agency, which has the responsibility for auditing direct and indirect charges under those agreements. Costs recovered by the University in support of sponsored research are subject to audit and adjustment. Fringe benefit costs for the fiscal years ended August 31, 2007 to 2011 are still subject to audit. The University does not anticipate that any adjustments will be material to the consolidated financial statements.

HEALTH CARE

Cost reports filed under the Medicare program for services based upon cost reimbursement are subject to audit. The estimated amounts due to or from the program are reviewed and adjusted annually based upon the status of such audits and subsequent appeals. Differences between final settlements and amounts accrued in previous years are reported as adjustments to "patient care, net" revenue in the year the examination is substantially completed. Medicare cost reports have been audited by the Medicare fiscal intermediary through August 31, 2004 for SHC and August 31, 2009 for LPCH.

The healthcare industry is subject to numerous laws and regulations of federal, state and local governments. Compliance with these laws and regulations can be subject to future government review and interpretation, as well as to regulatory actions unknown or unasserted at this time. Government activity with respect to investigations and allegations concerning possible violations by healthcare providers of regulations could result in the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. The Hospitals are subject to similar regulatory reviews, and while such reviews may result in repayments and/or civil remedies that could have a material effect on the Hospitals' financial results of operations in a given period, each Hospital's management believes that such repayments and/or civil remedies would not have a material effect on its financial position.

MEDICAL CENTER RENEWAL PROJECT

In July 2011, the University and Hospitals obtained local approval for a Renewal Project to rebuild SHC and expand LPCH to assure adequate capacity and provide modern, technologically-advanced hospital facilities. The Renewal Project also includes replacement of outdated laboratory facilities at the Stanford School of Medicine and remodeling of Hoover Pavilion.

California's Hospital Seismic Safety Act requires licensed acute care functions to be conducted only in facilities that meet specified seismic safety standards which have varying deadlines. The Renewal Project as approved is also designed to meet these standards and deadlines.

SHC's and LPCH's share of the estimated total cost of the Renewal Project is \$2 billion and \$1.2 billion, respectively. Through August 2011, the Hospitals have recorded \$247 million in construction in progress related to this project. Based on current estimated schedules, management currently projects that the Renewal Project construction will be complete in 2017.

LABOR AGREEMENTS

Approximately 11% of the University's, 36% of SHC's and 47% of LPCH's employees are covered under union contract arrangements and are, therefore, subject to labor stoppages when contracts expire. There are currently no expired contracts under these union contract arrangements.

LITIGATION

The University and the Hospitals are defendants in a number of legal actions. While the final outcome cannot be determined at this time, management is of the opinion that the liability, if any, resulting from these legal actions will not have a material adverse effect on the consolidated financial position.

CONTRACTUAL COMMITMENTS

At August 31, 2011, the University had contractual obligations of approximately \$169.5 million in connection with major construction projects. Remaining expenditures on construction in progress are estimated to be \$486.1 million, which will be financed with certain unexpended plant funds, gifts and debt.

Commitments on contracts for the construction and remodeling of Hospital facilities were approximately \$152.2 million at August 31, 2011.

As described in *Note 5*, the University is obligated under certain alternative investment agreements to advance additional funding up to specified levels over a period of years.

GUARANTEES AND INDEMNIFICATIONS

The University and the Hospitals enter into mutual indemnification agreements with third parties in the normal course of business. The impact of these agreements is not expected to be material. As a result, no liabilities related to guarantees and indemnifications have been recorded at August 31, 2011.

21. Subsequent Events

The University and the Hospitals have evaluated subsequent events for the period from August 31, 2011 through December 14, 2011, the date the consolidated financial statements were available to be issued.

In November 2011, the University paid down \$61.6 million and redeemed \$50.0 million of CEFA Series R tax-exempt bonds with proceeds from the Series 2009A taxable bonds. In December 2011, the University redeemed \$89.6 million of CEFA Series O tax-exempt bonds.

Report from the Stanford Management Company

The Stanford Management Company (SMC) was established in 1991 to manage Stanford's financial assets. SMC is a division of the University with oversight by a Board of Directors appointed by the University Board of Trustees. The SMC Board consists of investment professionals, the University president, the University chief financial officer, the chairman of the Board of Trustees and the CEO of SMC. The Board approves SMC asset allocation targets, oversees the hiring of external asset managers, evaluates the performance of SMC investments and professionals, and manages significant portions of endowment, trust assets and expendable funds for the University and the Hospitals.

The majority of the University's endowment assets are invested through the Merged Pool (MP), which is a diversified portfolio of actively managed financial and real estate assets valued at approximately \$19.5 billion as of June 30, 2011. To facilitate the comparison of returns with results of other endowments and foundations, MP performance measurements are calculated on the 12 months ending June 30, 2011. The following discussion of endowment performance relates solely to investments in the MP. The MP realized a 22.4% investment gain for the 12 months ending June 30, 2011. Over the past 10 years, the MP achieved an annualized rate of return of 9.3%, growing from \$7.9 billion to \$19.5 billion.

The MP portfolio is constructed on a foundation of modern portfolio theory and strategic asset allocation. The portfolio is designed to optimize long-term returns, create consistent annual payouts to the University's operating budget and preserve purchasing power for future generations of Stanford faculty and students.

SMC, with assistance from its Board of Directors, actively manages the MP, selecting third-party managers to deploy the MP's capital. Stanford University's brand and SMC's reputation as a stable long-term source of capital enable SMC to gain access to the best third-party managers in the world. Within each asset class, we endeavor to place capital with a diversified set of managers across geographies and investment strategies. We seek to benefit from drivers of economic growth through a broadly diversified portfolio that is less subject to drawdown than the more concentrated portfolio of the late 1990's. SMC also seeks to add value through effective risk management, tactical portfolio rebalancing and opportunistic investment tilts.

STANFORD MP ASSET ALLOCATION Given the perpetual nature of the University, SMC's investment horizon is long-term. Our objective is to generate optimal total return relative to an appropriate level of risk for Stanford. Each June, SMC and the Board reevaluate portfolio asset allocation targets, as well as expected risk, return and correlation among asset classes. This annual review takes into account current market conditions and historical characteristics of each asset class. The strategic asset allocation targets for the MP as of June 30, 2011 are listed below:

LONG-TERM POLICY TARGETS

Long-Term Policy Targets	
Asset Class	Strategic Allocation
Public Equity	37%
Real Estate	16%
Private Equity	12%
Natural Resources	7%
Absolute Return	18%
Fixed Income	10%

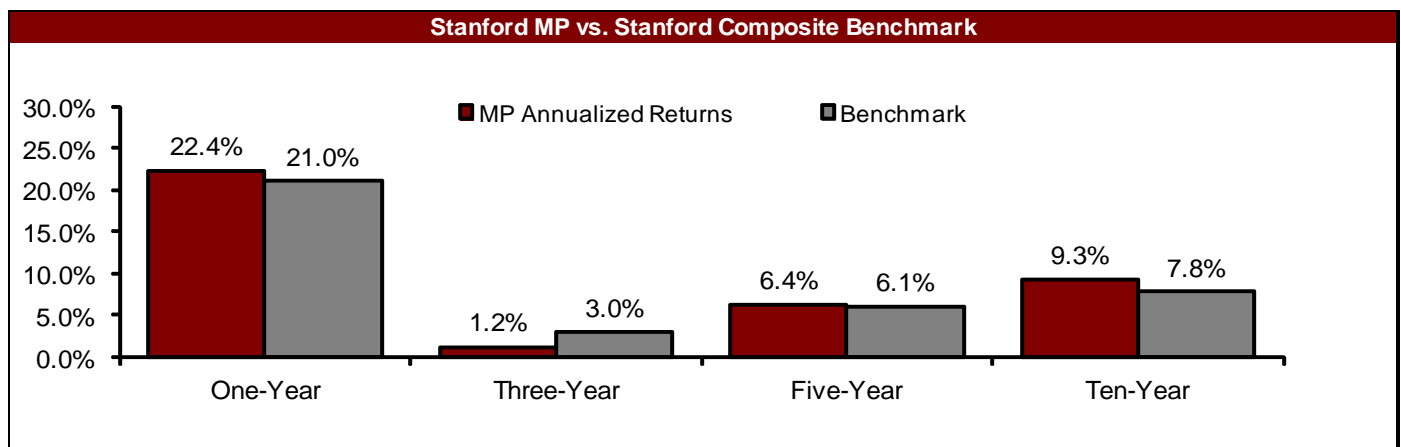
STANFORD MP PERFORMANCE COMPARED TO INFLATION The table below outlines annualized returns for various periods ending June 30, 2011.

MP PERFORMANCE COMPARED TO INFLATION

MP Performance Compared to Inflation				
	One-Year	Three-Year	Five-Year	Ten-Year
Nominal Endowment Return	22.4%	1.2%	6.4%	9.3%
GDP Deflator	2.4%	1.5%	1.9%	2.2%
Real Endowment Return	20.0%	-0.2%	4.5%	7.0%

STANFORD MP PERFORMANCE COMPARED TO BENCHMARKS SMC evaluates the performance of investment managers by comparing their returns to benchmarks that are appropriate for each individual asset class. The SMC Board reviews asset class benchmarks on an annual basis to ensure comparability. SMC reviews overall MP performance against the composite benchmark return, which represents a blend of the benchmark returns for each asset class weighted by the strategic allocations above. In the table below, actual performance, net of management fees, is compared to the composite benchmark for periods ended June 30, 2011.

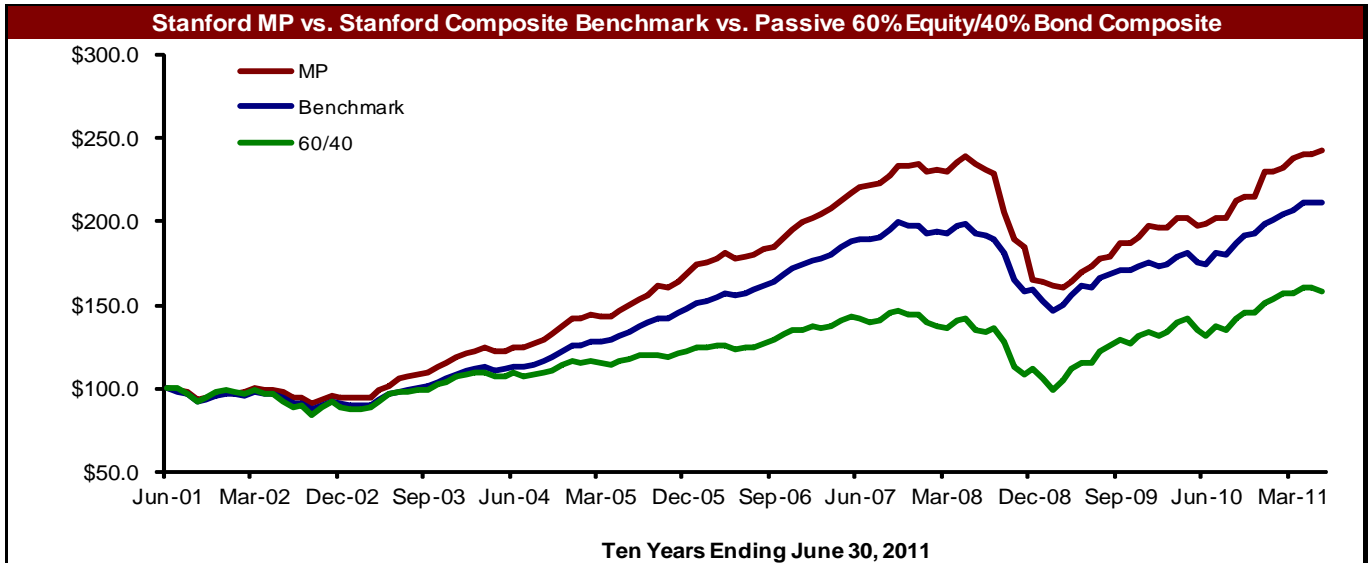
STANFORD MP VS. STANFORD COMPOSITE BENCHMARK



SMC's effectiveness in implementing its investment strategies through top-level manager selection has resulted in consistent and long-term outperformance over the composite benchmark. This has added an excess of \$2.5 billion to the value of the MP

over this 10-year period. The cumulative return chart below compares the growth of \$100 in Stanford's MP, a composite benchmark portfolio, and a 60% stock/40% bond portfolio over the past 10 years:

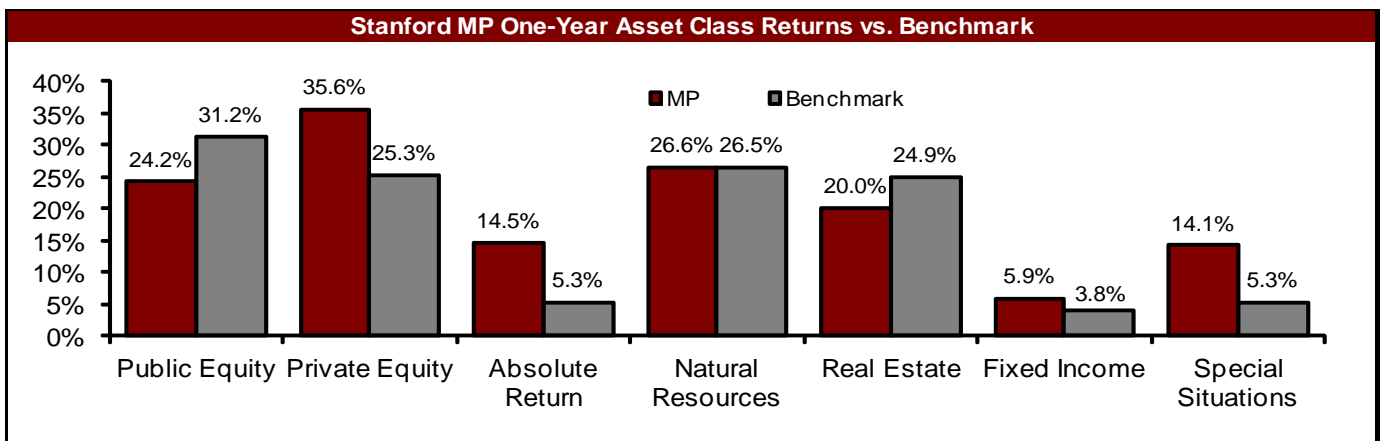
STANFORD MP VS. STANFORD COMPOSITE BENCHMARK & PASSIVE 60%EQUITY/40%BOND COMPOSITE



The relative one-year performance of the MP versus the benchmark was 1.4%.

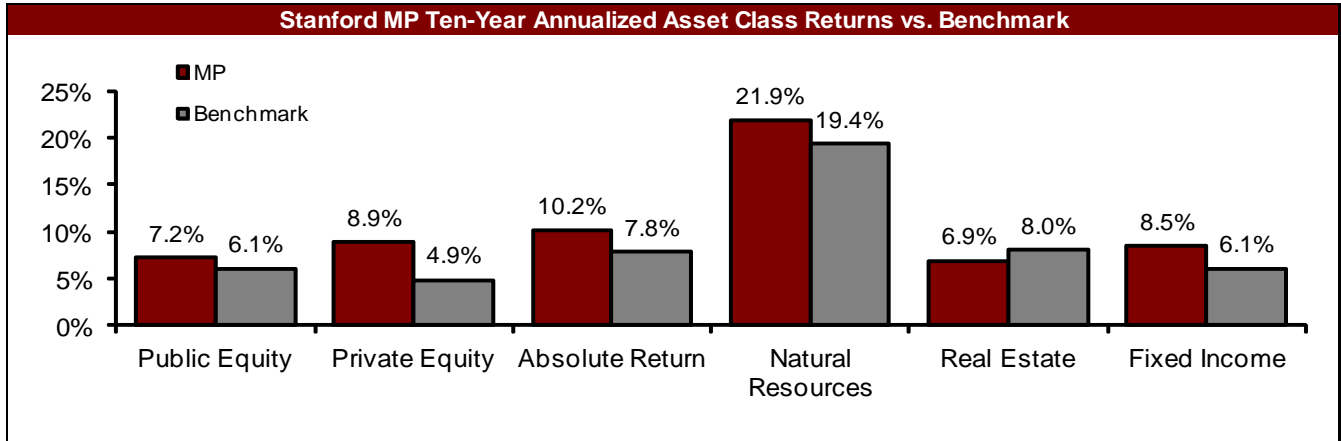
INDIVIDUAL ASSET CLASS PERFORMANCE The performance of individual asset classes for the 12 months ended June 30, 2011, relative to each asset class benchmark, is illustrated in the graph below:

STANFORD MP ONE-YEAR ASSET CLASS RETURNS VS. BENCHMARK



As outlined below, the results of 10-year asset class returns, relative to benchmark, illustrate the value of SMC's ability to shift investment styles/strategies and identify outstanding managers in each asset class:

STANFORD MP TEN-YEAR ASSET CLASS RETURNS VS. BENCHMARK



In the 12 months through June 30, 2011, the Merged Pool returns were 22.4%. During the same period, the S&P 500 Total Return Index returned 30.9%, the Barclays Aggregate returned 3.9%, and a 60/40 equity/fixed income mix would have returned 20.0%. Markets were strong almost across the board, with our private equity exposure contributing the most to the year. Almost immediately as the fiscal year ended, macroeconomic worries came to the fore and market volatility spiked. In this challenging climate the draw down in the MP has been moderate, and the portfolio has a more defensive positioning than in the drawdown of late 2008. At the same time, periods of volatility can create substantial buying opportunities, even in the face of significant uncertainty. Thus, we expect compelling investments in equity and credit markets as the multi-year global deleveraging process continues.

JOHN F. POWERS President and Chief Executive Officer, Stanford Management Company