STANFORD UNIVERSITY
BUDGET PLAN
2007/08

This Budget Plan was approved by the Stanford University Board of Trustees June 14, 2007. Distribution of this document is made in the interest of greater understanding of the University's Budget and the processes through which it is annually determined.

This publication can also be found at:
http://www.stanford.edu/dept/pres-provost/budget/plans/plan08.html

EXECUTIVE SUMMARY

To The Board of Trustees:

I am pleased to submit Stanford University's 2007/08 Budget Plan for your approval. The Budget Plan has two parts. The first is the Consolidated Budget for Operations, which includes all of Stanford's anticipated operating revenue and expense for next year. The second is the Capital Budget, which is set in the context of a multi-year Capital Plan.[1]

Some of the highlights of the Plan:

- The Consolidated Budget for Operations reflects an anticipated surplus of $58.8 million on $3.5 billion of revenues, $3.3 billion in expenditures, and $125 million in transfers. The Consolidated Budget revenues are expected to grow by 3.4% over the 2006/07 projected actual results, driven principally by growth in investment income and health care services.
- The Consolidated Budget includes $861.8 million in general funds, of which $133.8 million flows to the Graduate School of Business, the School of Medicine, and the Continuing Studies and Summer Session Programs in accordance with previously agreed-upon formulas. After other transfers and adjustments, there remains $721.8 million in general funds to be allocated directly by the Provost. This represents a 7% increase in the non-formula general funds component of the Consolidated Budget and includes a $10 million budgeted surplus that we are holding in reserve for future needs.
- The Capital Budget calls for $386.3 million in expenditures next year. These expenditures are in support of a three-year Capital Plan that, if fully completed, would require $2.4 billion in total project funding. Principal expenditures next year will be directed to the seven remaining buildings in the Science, Engineering, and Medical Campus (SEMC) ($121 million); the Munger Graduate Residences ($96.4 million); and the new Graduate School of Business campus ($20.9 million).
- This Budget Plan also presents the projected 2007/08 Statement of Activities in a format consistent with Generally Accepted Accounting Principles, as reported in the university's annual financial report. The projected Statement of Activities shows a $110.8 million surplus.

Proposed Change in Endowment Policy

At the June, 2007, Board of Trustees meeting the administration will request an increase in the target endowment payout rate from 5% to 5.5% and a resetting of the actual rate to 5.5% in 2007/08. The numbers in this Budget Plan do <u>not</u> incorporate this policy change, as the details of implementation are yet to be completed. If the Trustees approve the proposed payout increase, we estimate it will generate approximately $160 million in additional payout. The amount of funds released due to the payout increase is between 80% and 85% of the increase. The released general funds would be sequestered in a special account to be allocated toward the completion of high priority capital projects. This increased flow of funds will allow us to keep the budgets of schools and programs whole while general funds are devoted to finishing new facilities. More detail on this proposal and its implications may be found on page 8.

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[1] The budgets for the Stanford Hospital and Clinics (SHC) and the Lucile Packard Children's Hospital at Stanford (LPCH), both separate corporations, are not included in this Budget Plan.

STRATEGIC PRIORITIES

With the launch of the Stanford Challenge in October 2006, the university's strategic priorities are clear. We seek to leverage our unique capabilities to address some of the most crucial problems of our time. The response of the Stanford community in supporting this effort has been encouraging, but much work remains. As we developed the budget for next year, the role of the Stanford Challenge was central to our planning in several respects. First, we worked with the deans of each school to identify how their budget requests fit with the goals of the campaign. Second, as funds are raised we have looked to fill in the inevitable gaps with general funds, where appropriate. Third, we have sought to provide adequate support to the Office of Development to continue addressing our key fundraising priorities. Throughout this document we will refer back to these planning initiatives and attempt to reflect our budget priorities within them.

BUDGETARY PRIORITIES

Next year's budget priorities reflect support for the strategic initiatives, as well as for a number of key objectives necessary to maintain the ongoing operation of the university. The most notable priorities reflected in the 2007/08 budget are:

- **Faculty Compensation, Recruitment, and Retention –** Perhaps the most critical issue in the budget process this year is maintaining our market position for the best faculty. We face strong competition in attracting the best new faculty and in retaining our tenured faculty. In this highly competitive marketplace we have allocated almost $6 million in incremental funds for retention, for lab startup costs, and for related faculty support costs. This is in addition to a competitive overall faculty salary program and supplementary funds allocated to salaries in areas where we have fallen behind the prevailing market.

- **Infrastructure –** An annual priority in the budget process is ensuring that our physical and systems infrastructure continues to meet the needs of a dynamic institution. Almost $5 million in incremental general funds will support the debt service and maintenance costs on new buildings. In addition, we have allocated over $4 million in incremental funds for our administrative systems group.

- **Compliance Costs –** Stanford's compliance function must keep pace with the growth and changes in research seen in recent years. Although the majority of this research is federally funded, an increasing proportion is funded by gifts and grants that do not cover indirect costs. This budget calls for an additional $2 million for research compliance staffing, as well as funds for environmental health and safety and other non-research based compliance areas.

- **Undergraduate Financial Aid –** As was announced in February, Stanford implemented significant improvements to its financial aid program for middle income families. These enhancements will be covered by a combination of endowed scholarship funds plus an additional $5.5 million general funds allocation. The details are discussed on page 11.

- **School-Based Academic Initiatives –** This budget reflects the expansion and enhancement of important academic priorities in many areas. Some examples include:

  - The School of Earth Sciences will focus on renewal of its undergraduate programs, as well as continue to expand its connection to the Stanford Challenge Initiative on the Environment and Sustainability.

  - The Business School will begin construction of its new campus, implement its new curriculum with the entering MBA class, and expand collaboration with other faculty around the university in support of the Stanford Challenge graduate education initiatives.

- The Medical School will continue to expand its regenerative medicine programs and launch the construction of the Learning and Knowledge Center, a critical element in the school's strategic plan.
- The Law School will initiate several new interdisciplinary and cross-campus programs in 2007/08, expanding educational opportunities for both law students and graduate students from around the university. The most critical new initiative to be launched by the school will be planning for a new academic building.
- The School of Engineering will focus on the build-out of the Bioengineering Department, in addition to numerous capital projects. It will open the Environment and Energy Building and continue to enhance its initiative in the nanosciences.
- The School of Humanities and Sciences faces strong competition for faculty, while it continues to grow many of its key program areas and initiatives. These include the campus-wide Arts Initiative; the Division of International, Comparative, and Area Studies; the Institute for Research in the Social Sciences; the Institute for Theoretical Physics; and the Mathematics Research Center.
- The Office of the Vice Provost for Undergraduate Education will focus next year on continued improvement of the advising program, reviewing the Introduction to the Humanities program, strengthening the relationship with academic departments, and launching a new Overseas Studies program in Spain.
- The newly created Office of the Vice Provost for Graduate Education will expand programs in support of the Stanford Challenge graduate initiatives, including the Stanford Interdisciplinary Graduate Fellowships and a major graduate diversity fellowship program.

CONSOLIDATED BUDGET FOR OPERATIONS

The table on page vi shows the main revenue and expense line items for 2007/08 and compares those numbers to the projection of actual results for the current year. These figures include the incremental costs for the programs and initiatives noted above. Some highlights of both income and expense follow.

Revenue

Student Income – This figure is the sum of tuition and room and board income and is expected to grow by 4.8%. Tuition income is projected to grow 5% over the projected 2006/07 actuals, as the result of a 5.5% increase in the general undergraduate and graduate tuition, and increases between 4.5% and 5.9% in the professional schools, and no increase in terminal graduate registration fees. Room and board income is projected to increase 3.8%, due to a 4.25% increase in the standard undergraduate room and board rate and the phase out of university-funded subsidies for graduate students living off campus.

Sponsored Research – Overall sponsored research is budgeted to drop by 2.1% over the projected year-end actuals, due mainly to a 10.8% reduction at SLAC due to construction which was recently completed. Growth in non-SLAC direct research revenue is anticipated to be 2%, an increase below the expected inflation rate. Indirect cost recovery (ICR) is expected to grow by 4.6% in 2007/08, due primarily to an increase in the indirect cost rate from 56.5% to 58.0%.

Health Care Services Income – Revenue for health care services is projected to increase 6.4% in 2007/08, due to increases in the amount paid to the Medical School by Stanford Hospital and Clinics and Lucile Packard Children's Hospital related to physician services of its faculty.

Consolidated Budget for Operations, 2007/08

[in millions of dollars]

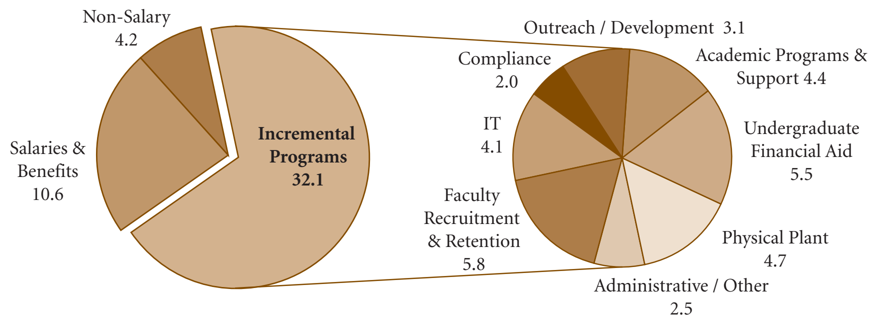
2005/06 Actuals	2006/07 Projected Actuals		2007/08 Consolidated Budget	Percent Change
		Revenues and Other Additions		
519.2	547.5	Total Student Income	573.9	4.8%
		Sponsored Research Support:		
523.5	523.5	Direct Costs-University	534.0	2.0%
298.0	379.0	Direct Costs-SLAC	338.1	(10.8%)
172.4	177.7	Indirect Cost	185.9	4.6%
993.9	1,080.2	Total Sponsored Research Support	1,058.0	(2.1%)
367.4	377.9	Health Care Services	402.1	6.4%
167.7	170.0	Expendable Gifts in Support of Operations	175.0	2.9%
628.5	740.2	Investment Income	827.6	11.8%
313.6	325.0	Special Program Fees and Other Income	333.2	2.5%
92.5	95.0	Net Assets Released from Restrictions	80.0	(15.8%)
3,082.8	3,335.8	Total Revenues	3,449.8	3.4%
		Expenses		
1,498.2	1,611.3	Salaries and Benefits	1,742.3	8.1%
297.9	379.0	SLAC	338.1	(10.8%)
142.9	155.0	Financial Aid	169.4	9.3%
921.1	987.4	Other Operating Expenses	1,016.0	2.9%
2,860.1	3,132.7	Total Expenses	3,265.8	4.2%
222.7	203.1	Operating Results	184.0	
(52.8)	(126.5)	Transfers, Principally to Facilities & Endowment	(125.2)	
169.9	76.6	Revenues less Expenses and Transfers	58.8	

Expendable Gifts – The Office of Development anticipates that revenue from non-capital gifts available for current expenses will grow by $5 million in 2007/08 to $175 million. This does not include gifts to endowment or for capital projects, which do not appear in the Consolidated Budget for Operations. Net assets released from restrictions, which include the payments made on prior year pledges and prior year gifts released for current use, are expected to drop from $95 to $80 million.

Investment Income – This category consists of income paid out to operations from the endowment and from other investment income—mainly earnings on the Expendable Funds Pool (EFP). Overall, investment income is expected to increase by 11.8%. Income from the endowment itself is expected to increase next year by 14.2%, including payout on $400 million in projected new gifts to the endowment. The spending rates approved by the Board of Trustees in February 2007 yield a projected smoothed payout rate of 4.33% compared to our target rate of 5.0%. Other investment income is expected to be flat. We assume a 2% increase in the average balance of the EFP, but this increase will be offset by moderating money market rates, resulting in a lower payout from the EFP than in the current year.

2007/08 Incremental General Funds Allocations: $46.9 Million

[IN MILLIONS OF DOLLARS]



Expense

Salaries and Benefits – We anticipate total compensation expense to increase 8.1% over the projected year-end actuals. Academic salary expense is expected to increase by 8.2%, driven by a competitive salary program, retention pressures, and a 1-2% increase in the number of faculty. Staff salary expense growth is budgeted to grow at 8.9% as a result of our merit program and an expected increase of 4% in staff headcount. The benefits rate will decrease from 29.7% to 28.1% for 2007/08. Total benefits expense is expected to increase by 5.8%.

Other Operating Expenses – This line item is composed principally of operations and maintenance (O&M) costs, utilities, capital equipment, materials and supplies, travel, library materials, subcontracts, and professional services. We are budgeting a growth of 2.9% for these items.

GENERAL FUNDS BUDGET

The General Funds budget is a critical component of the Consolidated Budget for Operations. The general funds allocations controlled directly by the Provost are expected to grow by about $46.9 million, or 7.1%, next year. $14.8 million of this is allocated for compensation growth and price inflation on non-salary items. This figure includes funding for the faculty and staff salary programs and benefits increases. The remaining $32.1 million is for incremental academic and administrative program expense. The pie chart above shows how the $32.1 million will be distributed among the various institutional priorities and categories. Because general funds support the bulk of Stanford's administrative, compliance, fund raising, and facilities costs for the entire consolidated budget, it is not surprising that much of the budgeted increment must be devoted to these costs.

CAPITAL BUDGET AND PLAN

The Capital Budget for 2007/08 has been developed in the context of a three-year Capital Plan. The three-year plan includes projects that were initiated prior to, but will not be completed by, 2007/08, as well as projects that will be started during the three-year period from 2007/08 to 2009/10. Since some projects in the plan will not be completed by the end of 2009/10, the three-year plan actually provides a rolling window of approximately five to six years of construction projects at the university.

Capital Budget, 2007/08

The Capital Budget for 2007/08 represents capital expenditures for the upcoming year. We have budgeted $386.3 million in project expenditures. This reflects only a portion of the total costs of the capital projects underway, as most projects have a duration exceeding one year. We categorize the projects in the 2007/08 Capital Budget in two ways:

- By use: 48% is devoted to academic/research facilities; the remaining uses are student housing (25%), infrastructure (19%), academic support (5%), and athletics/student activities (3%).
- By type of space: 72% of the funding is for new projects (Munger Graduate Residences, and SEMC buildings); 8% for renovation projects (Panama Mall and Encina projects); and 20% for infrastructure projects.

Completion of the projects in the Capital Budget including the Energy & Environment building, will add $3.9 million to internal debt service, bringing the total to $135.2 million in the 2007/08 Consolidated Budget for Operations. This building will also require incremental O&M expenses of $3.2 million.

Capital Plan, 2007/08 – 2009/10

This year's Capital Plan forecasts $2.4 billion in construction and infrastructure projects that are currently underway or planned to begin over the next three years. The major initiatives included in last year's plan continue to be the principal components of this plan. They are the Science, Engineering and Medical Campus (SEMC); a new campus and parking for the Graduate School of Business; the Redwood City campus redevelopment project; a performing arts center; Panama Mall renovations; and phase I of the undergraduate housing and dining master plan.

Although this year's plan presents a realistic view of our construction outlook, we do not expect all of the projects included in the Capital Plan to be completed in the envisioned timeframe. The projects included in the plan can all be accommodated within the constraints of the General Use Permit, and we are reasonably certain that the debt funding assumptions are realistic. But many of the projects assume substantial amounts of unidentified gift or reserve funding. These projects will only move forward when the stated funding goal is met with gifts or school reserves in hand.

The three-year Capital Plan includes a dozen major projects and numerous infrastructure projects and programs. Most of these projects are multi-year efforts, and all are scheduled to be initiated by the end of 2009/10. Financing such an ambitious Capital Plan is challenging. The fundraising goals for individual projects total $1.124 billion, of which only $567.2 million in gifts are now in hand or pledged. We currently anticipate allocating $443.5 million in school reserves and central university funds toward the projects, supplemented by $364.3 million in debt and $50.4 million in other identified sources. This still leaves $387 million in resources yet to be identified. At plan completion, incremental annual debt service is expected to be $28.6 million and incremental O&M costs will total $27.1 million per year.

This Capital Plan is clearly the most ambitious in Stanford's history. It will provide facility support for the major institutional initiatives described above. Upon completion, Stanford will have upgraded its capacity to make major advances in environmental studies, the biosciences and bioengineering, nanotechnology, and human health. Through the construction of the performing arts center and a new home for art and film studies, we will have achieved a long held goal of increasing the prominence of the arts on campus. Completing the Munger Residences and launching the new housing master plan will provide needed improvements to both graduate and undergraduate housing, and the new GSB and Law projects will yield facilities to support these schools' visionary curricular and interdisciplinary plans. Finally, the redevelopment of the Redwood City site allows for the centralization of important university services in modern facilities off campus, thereby freeing up space on the central campus for academic expansion.

REQUESTED APPROVAL AND ORGANIZATION OF THIS DOCUMENT

This Budget Plan provides a university-level perspective on Stanford's programmatic and financial plans for 2007/08. We seek approval of the planning directions, the principal assumptions, and the high-level supporting budgets contained herein. As the year unfolds, we will make periodic variance reports on the progress of actual expenses against the budget. In addition, we will bring forward individual capital projects for approval under normal Board of Trustees guidelines.

This document is divided into four sections and two appendices. Section 1 describes the financial elements of the plan, including details of the Consolidated Budget for Operations and the projected Statement of Activities for 2007/08. Section 2 provides a budgetary and programmatic overview of the major academic units of the university, and Section 3 provides a similar view of the administrative and auxiliary units. The structure and format of these two sections have been significantly changed this year, in ways that we hope are helpful. Section 4 contains details on the Capital Budget for 2007/08 and on the Capital Plan for 2007/08-2009/10. As usual, the Appendices include budgets for the major academic units, as well as supplementary financial and institutional data.

CONCLUSION

Stanford University is in an enviable position, both financially and—more important—academically. We are blessed with the most loyal and supportive alumni in the nation, and benefit from a remarkable endowment management team that skillfully shepherds university resources in support of our academic mission. The wise choices of past academic leaders have left our research capacity and educational programs in positions of unprecedented strength across the entire university. At the core of this strength is an innovative and entrepreneurial faculty, who in turn attract the highest quality students.

The Stanford Challenge sets out a vision that will leverage these strengths toward an extremely ambitious goal: to address, through our research contributions and the education of future leaders, some of the most daunting challenges facing the world. This goal is reflected throughout this document—in the multitude of choices made in constructing the annual budget, in the individual academic plans described by the schools, and, most strikingly, in the Capital Plan required to support these high aspirations.

In preparing the budget and capital plans described in this document, I have benefited from the advice and support of many individuals, starting with the excellent staff of our central budget and capital planning offices. Two dedicated advisory groups also assist in developing the general funds budget and capital plan. The University Budget Group consists of Patti Gumport, Stephen Hinton, Rosemary Knight, Randy Livingston, Maureen McNichols, Kären Nagy, Steve Olson, Channing Robertson, Bob Simoni, Buzz Thompson and Tim Warner, with Dana Shelley ably leading the charge. The Capital Planning Group consists of Megan Davis, Stephanie Kalfayan, Sandy Louie, Bob Reidy, Craig Tanaka, Bob Tatum, Tim Warner, and Mark Zoback,

with Margaret Dyer-Chamberlain orchestrating the affair. The university owes both groups a debt of gratitude for the many hours they put into the budget and capital planning process.

Finally, Stanford is fortunate to have an extraordinary set of Deans, whose leadership, cooperation and shared vision add immeasurably to the strength of both the individual schools and the university as a whole. It is a pleasure and privilege to propose a Budget and Capital Plan to support their vision.

John W. Etchemendy
Provost
June 2007

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INTRODUCTION: BUDGETING AT STANFORD

Budgeting at Stanford is a continuous process that takes place throughout the year and occurs at nearly every level within the university. The cycle starts with planning that considers programmatic needs and initiatives, continues with the establishment of cost drivers such as the approved salary program and fringe benefits rates, and is tempered by available funding sources. Stanford's "budget" is an amalgamation of thousands of smaller budgets, including everything from an individual faculty member's budget for a sponsored grant from the National Institutes of Health, to the budget for the Department of Psychology, to the budget for the School of Engineering, to the total of the Consolidated Budget for Operations. These budgets are created and managed by the areas that are governed by them, with oversight by the Provost, the chief budget officer of the university. There are general principles and guidelines to which the budgets must adhere, but schools and other units are allowed tremendous freedom in the development and execution of their budgets.

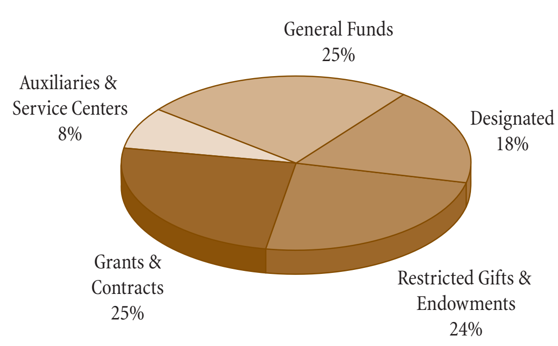
Fund Accounting

Stanford's budgets are developed and managed according to the principles of fund accounting. Revenue is segregated into a variety of fund types, and the use of the revenue is governed by the restrictions of the fund. For example, each expendable gift received is put into an individual fund, and the recipient must use the funds in accordance with the wishes of the donor. Gifts of endowment are also put into separate funds, but the corpus can never be spent. Only the payout on the endowment fund can be spent, but as with gift funds, only in accordance with the restrictions imposed by the donor. The segregation of each gift allows the university to ensure that the funds are spent appropriately and to report to the donors on the activities that their funds support. Monies received from government agencies, foundations, or other outside sponsors are also deposited in separate, individual funds to ensure strict adherence to the terms of the grants and/or contracts that govern the use of the funds. Non-gift and non-sponsored research revenue also reside in funds, but this type of revenue may be commingled in a single fund. Often, however, departments may choose to combine unrestricted monies into separate funds for a particular program, for a capital project, or to create a reserve. Stanford's 2007/08 recommended Consolidated Budget for Operations revenues by fund type is shown below.

Budget Management

So how does Stanford budget and manage its roughly 30,000 expendable and 6,000 endowment funds? It goes without saying that the university uses a sophisticated financial accounting system to set up the individual funds, to record each financial transaction, and to track fund balances. But nearly all of the decision-making for the use of Stanford's funds is made at the local level, consistent with the decentralized and entrepreneurial spirit of the university. Unlike a corporation, Stanford is closer to a collection of disparate, autonomous businesses with widely varying cost structures and resources. As such, each principal investigator is accountable for the responsible use of his/her grant funding, each gift recipient must ensure that the gift funds are used in accord with the donor's wishes, and each school must fulfill the expectations for teaching and scholarship within its available resources.

2007/08 Consolidated Revenues by Fund Type



Budget Control

The primary control on local unit budgets at Stanford is available funding. Except for general oversight and policies governing the appropriate and prudent use of university funds, the central administration does not place additional limits on spending. For example, if a faculty member needs to hire a post doctoral fellow to help carry out a particular research project, and if grant funding is secured to cover this expense, the university does not second-guess this decision.

Because the majority of Stanford's funding is under the direct control of a faculty member, a department, or a school, these entities are able to support programs as long as they maintain a positive fund balance. This, however, does not mean that the programs must operate with a surplus during any particular fiscal year. In fact, a "deficit" is usually reflective of a planned use of prior year fund balances. A simple example of this is when a department receives a gift of $5.0 million to be spent over five years. If the funds are spent evenly over the time period, the program will show a surplus of $4.0 million in the first year and will generate an ending fund balance of $4.0 million. In each of the next four years, this program will receive no revenue, will expend $1.0 million dollars, and will thus generate an annual deficit of $1.0 million while drawing down the fund balance of the gift.

The Consolidated Budget for Operations, the aggregate of all of Stanford's smaller budgets, is therefore not centrally managed in the corporate sense. Nonetheless, a great deal of planning goes into the development of the individual unit budgets that aggregate into the Consolidated Budget of the university.

Development of the Consolidated Budget & the Role of General Funds

The concepts of fund accounting and restricted funds were introduced above. Another key element in the development of the units' budgets and the Consolidated Budget are university general funds, which are funds that can be used for any university purpose. General funds play a particularly important role in the overall budget, because they cover many expenses for which it is difficult to raise restricted funds, such as administration and campus maintenance. The main sources of general funds are tuition income, indirect cost recovery, unrestricted endowment income, and income from the expendable funds pool.

Each school and administrative unit receives general funds in support of both academic and administrative functions. The process for allocating general funds is controlled by the Provost and aided by the Budget Group, which includes representation from both faculty and administration. The critical elements of the process are a forecast of available general funds, a thorough review of each unit's programmatic plans and available local funding, and an assessment of central university obligations such as building maintenance and debt service. Balancing the needs and the resources is the ultimate goal of the Provost's Budget Group. The general funds allocation process is described in more depth in Section 1.