Stanford University
Budget Plan

2002/03

Submitted for Action to the
Board of Trustees
June 13-14, 2002

Executive Summary

To The Board of Trustees:

I am pleased to submit Stanford University's 2002/03 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.

Stanford's 2002/03 Consolidated Budget for Operations reflects an anticipated surplus of $46 million on net revenues after transfers of $2,180 million and expenses of $2,134 million. This surplus results primarily from an excess of restricted revenue over expense.

Almost $575 million of Stanford's budget is categorized as general funds. These funds can be used for any university purpose. General funds of $500 million are under the direct control of the Provost, while the remaining $75 million flow directly into units in accordance with the formula agreements with the Graduate School of Business, the School of Medicine, the Hoover Institution, and the Continuing Studies Program. The general funds component of the Consolidated Budget is balanced for 2002/03.

The Capital Budget calls for $266 million in capital expenditures next year supporting a range of initiatives.

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

CONTEXT

The process of building a budget for a university the size, quality, and dynamism of Stanford is challenging under the best of circumstances. This was particularly true in developing the budget for 2002/03. Last spring and summer, as we updated the multi-year consolidated budget forecast, it was clear that the university was embarking on a more difficult financial period. A constrained revenue outlook, due principally to deteriorating financial markets, set against the need to fund many important programmatic areas, placed renewed importance on strategic fiscal planning.

In the budgets of recent years, we have seen strong growth in investment income, which has enabled Stanford to invest in undergraduate education, student financial aid, faculty and staff salaries, housing, research support, and new facilities. The results of this growth have been a fundamental strengthening of our undergraduate education program to one of the best in the nation, along with continued strengthening of our research and graduate programs. We have also built new state-of-the-art facilities in many parts of the university to support Stanford faculty and students in their research and educational endeavors. In projecting expenses for the next several years our planning priorities are to support a competitive salary program, to maintain a financial aid program that allows the best students to enroll, to fund the recruitment and retention of outstanding faculty, to enhance the opportunity for interdisciplinary work, and to provide necessary supporting infrastructure and facilities.

This year's capital planning process has been constrained by the restrictions of the General Use Permit (GUP), a more difficult environment for capital giving, and limitations in our debt capacity. Consequently, the capital plan included in this document reflects a slowing of capital construction from the levels of recent years, in addition to a considerably reduced reliance on debt for those projects we have put forward for approval.

Given Stanford's financial outlook, early in the budget process we asked academic and administrative units supported by general funds to plan for a general funds budget cut of 5% and 3% in 2002/03 and 2003/04, respectively. After a thorough review process, we have built into next year's budget a set of reductions averaging approximately 4% across most academic and support units. These reductions allow us to deliver a balanced budget while providing funds to cover commitments made in prior years and for reallocation to some of our most critical priorities.

In the schools and academic support areas the impact of the reductions will be felt in two ways. First, there will be across-the-board tightening of expenses accompanied by some delays in planned purchases or program enhancements. Second, schools and department will have to rely more on restricted funds to support their program expenses. We are not anticipating major reductions in programs.

Administrative units are also planning to reduce general expenses by approximately 5%. More significant cuts will be made in the maintenance and computer systems budgets. Specifically, planned maintenance budgets will be trimmed for roads and in several building maintenance areas, and efficiencies will be found in the operations of central computing systems in ways that will minimally affect service to university users.

Although the budget process focused principally on expense reduction, we have still been able to address important priorities in the following areas:

- COMPENSATION – After several years of strong staff compensation programs we have achieved our target to be at mid-market for most positions. As a result, and given the weakness in the local economy, our program for 2002/03 will be more modest than in prior years. However, it will be sufficient to maintain market competitiveness. The program for faculty will also provide funding to maintain our position in the top two or three in the country. In addition, our housing programs will be funded to allow Stanford to continue to attract and retain the best faculty.

- GRADUATE STUDENT SUPPORT – We made a concerted effort in the 2002/03 budget to improve support for graduate students. Minimum stipend levels will increase by 8%. We will also provide subsidies for graduate student health insurance to mitigate cost increases of more than 50%. Finally, Stanford will expand the off-campus apartment leasing program for graduate students in order to provide a more stable system and reduce the number of moves graduate students would otherwise make during their academic careers. With these enhancements, Stanford's programs supporting housing, tuition reimbursement, and other living costs will be extremely competitive with other institutions and will help mitigate the high cost of living in this area.

- UNDERGRADUATE FINANCIAL AID – Over the past four years we have expanded our financial aid program by about $9 million to reduce student loan expectations and to expand support to middle income families. While we are not adding any major enhancements to the aid program for next year, this budget does provide funds to meet the demonstrated financial need of all undergraduates. It is important to underscore that for those families whose financial circumstances do not keep pace with the cost of attending Stanford, we will meet their increased need through our financial aid program.

- **Support for New Buildings** – There are several new and renovated buildings coming on line in the remainder of this year and next year whose operating and debt service costs will affect the budget. These include Mechanical Engineering, the Clark Center, an off-site library storage facility, and Buildings 160 and 170. The costs of $13.1 million are included in the Consolidated Budget for Operations.

- **Investment in Development and Alumni Relations** – Over the past 18 months we have been engaged in an ongoing assessment of Stanford's longer-term programmatic needs, opportunities, and strategic priorities. While this process is still underway, it will most likely result in an expansion of our development agenda in the coming years. Consequently, we have included in this Budget Plan increased support for development and alumni relations activities.

- **Systems** – For the past several years Stanford has been engaged in a significant effort to replace its administrative systems and to upgrade the infrastructure supporting both academic and administrative computing. That effort will be nearly finished in 2002/03 with the completion of the Delphi financial system and the Axess student system. We are budgeting $16 million for system development projects and the infrastructure to support them in next year's budget.

- **Budget Reductions and Allocations of General Funds** – As noted above, about $500 million of Stanford's approximately $2 billion budget is comprised of general funds under the direct control of the Provost. Within this portion of the budget we are reducing base budget funding allocations to units by $16.3 million or approximately 4%. All of the budget units across the university supported by general funds participated in this reduction process.

  An important reason for making these reductions was to fund $11.5 million of commitments made in prior years to cover incremental critical program initiatives and to provide continuing funding for programs supported with one-time money. These commitments included increased budget support for the School of Humanities and Sciences, funding for undergraduate education initiatives, and debt service and operations and maintenance on new buildings. In addition, as part of the regular budget process we are funding $5.2 million of incremental items. Of this figure, $3.8 million will go to academic and academic support units. The remainder will support administrative units, principally Business Affairs, to pay for research administration previously funded by annual allocations of one-time money.

CONSOLIDATED BUDGET FOR OPERATIONS

The table on page vi shows the principal revenue and expense line items for 2002/03 and compares those numbers to the projected actuals 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, less student aid. The 5.5% growth rate over the projected year-end actuals results from a 5.0% increase in the general tuition rate, increases ranging from 4.5% to 12.5% in room and board rates, and a 6.6% increase in overall student aid expense.

Sponsored Research – The 3.5% growth in sponsored research results from: 1) an anticipated growth in direct research costs of 4.5%, and 2) a small, 0.7% increase in indirect cost recovery, resulting from a budgeted decrease in the indirect cost rate from 57% in 2001/02 to 55% in 2002/03.

PROJECTED CONSOLIDATED BUDGET FOR OPERATIONS, 2002/03

[IN MILLIONS OF DOLLARS]

2000/01 Actuals	20001/02 Projected Year-End		2002/03 Projected Current Funds
		Revenues and Other Additions	
299.7	320.0	Student Income	337.6
727.5	806.2	Sponsored Research Support	827.7
163.3	170.4	Health Care Services	187.9
125.3	130.0	Expendable Gifts in Support of Operations	140.0
419.8	462.4	Investment Income	489.7
226.7	236.5	Special Program Fees and Other Income	254.2
51.0	50.0	Net Assets Released from Restrictions	50.0
2,013.3	2,175.5	Total Revenues	2,287.1
(131.0)	(105.7)	Transfers	(107.1)
1,882.3	2,069.8	Net Revenues after Transfers	2180.0
		Expenses	
979.9	1,075.4	Salaries and Benefits	1,133.4
205.5	219.8	SLAC	219.9
686.7	746.4	Other Operating Expenses	780.8
1,872.1	2,041.6	Total Expenses	2,134.1
10.2	28.2	Surplus/(Deficit)	45.9

EXPENDABLE GIFTS – The Office of Development anticipates that revenue from non-capital gifts available for current expenses will reach $140 million in 2002/03, an increase of $10 million over the projected gift revenue in the current year. (This line does not include gifts to endowment or for capital projects.) In addition, net assets released from restrictions, which primarily represent payments made on prior year pledges, are expected to remain constant at $50 million in 2002/03.

INVESTMENT INCOME – This category consists of income paid out to operations from the endowment and from the Expendable Funds Pool (EFP). Income from endowment is expected to grow next year by 2.8%, including payout from new gifts to the endowment. The spending rates approved by the Board of Trustees in February 2002 are consistent with a smoothed payout rate of 5.13% compared to our target rate of 5.1%. The budgeted EFP income assumes a 5.0% total return on the investments of the EFP. This return is 100 basis points above the guaranteed payout approved by Board of Trustee policy. Overall revenue from the EFP is expected to be up by nearly 25% in 2002/03 over 2001/02 due to the fact that we expect to generate only the guaranteed payout of 4.0% in the current year, 2001/02.

EXPENSE

SALARIES AND BENEFITS – We anticipate total salaries and benefits expense to increase 5.4% over the projected year-end actuals. In the faculty marketplace we compete nationally and internationally and anticipate maintaining a strong salary position with a 3.5% basic program and some targeted funding to address equity and retention issues. In addition, we expect continued modest growth in academic staff of about 1.0%. The staff salary program for 2002/03 includes central funding of 2.7% for merit increases; 0.5% for one-time, non-base performance bonuses and incentives; and targeted funding for specific job groups that lag the market by 10% or more. Units may use additional restricted funding up to 1.0% in base and 2.0% in one-time funding to enhance the salary program. Staff growth is expected to slow compared to past years but is likely to add an additional 1.5% to staff salary costs. Furthermore, we expect increases in medical premium costs to result in an additional 0.5% increase in overall salaries and benefits expense next year.

Other Operating Expenses – These line items are comprised principally of operations and maintenance (O&M) costs, utilities, materials and supplies, travel, library materials, subcontracts, and professional services. We are budgeting a growth of 4.6% for these items.

CONSOLIDATED BUDGET FORECAST, 2002/03 – 2006/07

Stanford's financial position for the next several years looks strong, although there will be challenges, particularly in the general funds portion of the budget. A more constrained economy means a slowing of revenue from gifts and investments. Consequently, we must be careful and strategic in our planning. Our principal competition, Harvard, Princeton, and Yale, all have larger endowments per student and are emerging from a period in which they reinvested a greater fraction of their investment returns than we did. But we have many advantages, including a supportive environment for interdisciplinary work, an entrepreneurial faculty, the willingness to take prudent risks, and a strong development team.

In building the university's financial forecast for the next several years, we see a continuation of the trend of the past year or two: a Consolidated Budget for Operations showing a small surplus, while the general funds component of the Consolidated Budget remains under pressure. We are confident that we will be able to address the projected shortfalls in general funds, as we have done in the past, while continuing to strengthen the university.

Consolidated Budget Forecast, 2002/03 – 2006/07

[in millions of dollars]

	Projected	Budget	Forecast			
	01/02	02/03	03/04	04/05	05/06	06/07
Total Revenues after Transfers	2,069.8	2,180.0	2,274.5	2,376.6	2,480.6	2,589.5
Total Expenses	2,041.6	2,134.1	2,239.2	2,343.2	2,446.8	2,549.9
Surplus/(Deficit)	28.2	45.9	35.3	33.4	33.8	39.6

General Funds Budget Forecast (Excludes Formula Areas), 2002/03 - 2006/07

[in millions of dollars]

	Projected	Budget	Forecast			
	01/02	02/03	03/04	04/05	05/06	06/07
Total Revenues after Transfers	485.0	507.4	525.6	544.0	551.6	583.3
Total Expenses	485.0	507.4	537.7	561.8	577.9	613.2
Surplus/(Deficit)	0.0	0.0	(12.1)	(17.8)	(26.3)	(29.9)

CAPITAL BUDGET AND PLAN

The Capital Budget for 2002/03 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, 2002/03, as well as projects that will be started during the three-year period. Some of the projects in the plan will not be completed by the end of 2004/05. Thus it actually provides a rolling window of approximately five to six years of construction projects at the university.

In developing the Capital Plan for the next three-years we were faced with a far more constrained planning environment than in recent years. The total project dollar amount of the three-year Capital Plan has dropped by $530 million compared to last year's plan, from $1.6 billion to $1.07 billion. This is due to two factors: 1) the limitations on our future use of debt, given our policy of maintaining an AAA/Aaa bond rating in the face of declining investment markets, and 2) fundraising constraints due to the sluggish economic environment.

The projects included in the three-year Capital Plan can be accommodated within the constraints of the General Use Permit, and we are reasonably certain that the debt funding assumptions are realistic. However, 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.

CAPITAL BUDGET, 2002/03

The Capital Budget for 2002/03 represents expected capital expenditures and includes both committed and planned projects totaling $266 million. We categorize the projects in two ways: by use and by type of space.

- By Use: 45% for academic/research facilities; 21% for infrastructure; 25% for housing; and the remaining 9% to athletics, student activities, and academic support.
- By Type of Space: 63% for new projects (Clark Center, Lokey Laboratory, Escondido Village Graduate Student Housing, Law Student Housing Quad, School of Medicine Education Center); 16% for renovation projects (Branner Hall); 21% for infrastructure programs.

The 2002/03 Consolidated Budget for Operations includes incremental internal debt service and operations and maintenance expenses for projects completing in 2002/03 and for projects completed in 2001/02 that were operational for less than twelve months. The projected impact of the additional internal debt service and operations and maintenance expenses is $10.2 million and $2.9 million, respectively.

CAPITAL PLAN, 2002/03 – 2004/05

The three-year Capital Plan includes 34 major projects and numerous infrastructure projects and programs totaling $1.07 billion. Most of these projects are multi-year efforts and are scheduled to be completed by the end of 2007/08. The three-year plan will be funded from $175 million in current funds; $205 million in pledged gifts or pledges; $166 million in auxiliary and service center debt; $151 million in academic debt; and $370 million in other resources yet to be identified.

The three-year plan includes:

- $319.9 million for Committed Projects, those currently in Design & Construction,
- $531.7 million for Forecasted Projects, those anticipated to be presented to the Trustees for approval during the three-year period, and
- $216 million for Infrastructure Projects and Programs.

At plan completion, incremental annual internal debt service is expected to be $24.9 million, of which $12.4 million will be serviced by auxiliary or service center activities and $12.5 million will be paid for by unrestricted funds. Incremental O&M costs are expected to total $16.3 million per year, of which $9.9 million will be paid for by unrestricted funds.

REQUESTED APPROVAL AND ORGANIZATION OF THIS DOCUMENT

This Budget Plan provides a university-level perspective on Stanford's programmatic and financial plans for 2002/03. 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 reports, as necessary, 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 three sections and two appendices. Section 1 describes the financial elements of the plan, including details on the Consolidated Budget for Operations and the projected Statement of Activities for 2002/03. Section 2 addresses program issues in the academic areas of the university. Section 3 contains details on the Capital Plan for 2002/03 – 2004/05 and the Capital Budget for 2002/03. The Appendices include budgets for the major academic units and supplementary financial information.

CONCLUSION

Stanford is entering a period of modest retrenchment in both its general funds and capital budgets, after several years of steady growth. I do not view this as a cause for concern, but rather as an opportunity to consolidate our budget and rethink some of the more ambitious construction plans envisioned in recent years. Although this constrained budgeting process is healthy for the institution, it obviously demands a more difficult set of decisions on the part of everyone involved in the process. For this reason, I owe more than the usual thanks this year to the many people who contributed to the budgets presented in this book.

First and foremost, I want to thank those involved in the budgeting process within the schools and administrative units, both deans and directors, and their financial staffs. Although we were trimming budgets and shrinking capital plans, the attitude throughout the process was one of cooperation in solving a common problem. I believe this is, more than anything else, a tribute to the outstanding leadership shown by Stanford's very strong group of deans. The university is truly fortunate to have its current team of deans and administrative directors.

The budget and capital plan would not come together without the extraordinarily dedicated work of two advisory committees: the University Budget Group and the Capital Planning Group. The Budget Group this year consisted of Keith Baker, Mike Hindery, Charles Kruger, Randy Livingston, Channing Robertson, Dana Shelley, Bob Simoni, Buzz Thompson, and Tim Warner. This year, for the first time, I asked the Budget Group to hear presentations from and advise me on the budgets for every school and administrative unit. This required a great deal of time and effort from the committee, but made the group's advice particularly helpful to me in coming up with the final general funds budget.

This year's Capital Planning Group consisted of Chris Christofferson, Megan Davis, Margaret Dyer-Chamberlain, Stephanie Kalfayan, Randy Livingston, Sandy Louie, David Neuman, Tim Portwood, Bob Reidy, Craig Tanaka, Langston Trigg, Jeff Wachtel, and Tim Warner. The capital planning process is governed by the orthogonal constraints of GUP square footage, university debt, and fundraising capacity. To find a solution that maximally promotes the university's academic priorities while satisfying these three constraints is no easy task. The Capital Planning Group considered many successive iterations before successfully distilling the requests received from the schools and units into the plan described in Section 3. I am grateful for the group's hard work on this daunting task.

Finally, a huge amount of work is performed behind the scenes to support the efforts of these two advisory committees. In the Budget Office, Dana Shelley and Chuck Spielman do this work, under the able direction of Tim Warner. In the Capital Planning Office, Megan Davis and Margaret Dyer-Chamberlain lead the process, with guidance from Bob Reidy. I am extremely lucky to have the support of all of these dedicated and capable individuals.

John W. Etchemendy
Provost
June 2002

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