

Stanford University

Annual Financial Report

For the years ended August 31, 2012 and 2011

STANFORD UNIVERSITY 2012 FINANCIAL REVIEW

MANAGEMENT'S DISCUSSION AND ANALYSIS	3
SELECTED FINANCIAL AND OTHER DATA	11
MANAGEMENT RESPONSIBILITY FOR FINANCIAL STATEMENTS	12
REPORT OF INDEPENDENT AUDITORS	13
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION	14
CONSOLIDATED STATEMENTS OF ACTIVITIES	15
CONSOLIDATED STATEMENTS OF CASH FLOWS	17
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS.....	18
1. BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES	
2. ACCOUNTS RECEIVABLE	
3. PLEDGES RECEIVABLE	
4. LOANS RECEIVABLE	
5. INVESTMENTS	
6. INVESTMENT POOLS	
7. DERIVATIVES	
8. PLANT FACILITIES	
9. LIABILITIES UNDER SECURITY LENDING AGREEMENTS	
10. UNIVERSITY NOTES AND BONDS PAYABLE	
11. HOSPITALS NOTES AND BONDS PAYABLE	
12. UNIVERSITY ENDOWMENT	
13. HOSPITALS ENDOWMENTS	
14. UNIVERSITY GIFTS AND PLEDGES	
15. FUNCTIONAL EXPENSES	
16. UNIVERSITY RETIREMENT PLANS	
17. HOSPITALS RETIREMENT PLANS	
18. OPERATING LEASES	
19. RELATED PARTY TRANSACTIONS	
20. COMMITMENTS AND CONTINGENCIES	
21. SUBSEQUENT EVENTS	
REPORT FROM THE STANFORD MANAGEMENT COMPANY	66

MANAGEMENT'S DISCUSSION AND ANALYSIS

Stanford experienced solid financial results in fiscal year 2012 (FY12), marking the third year of growth after the 2008-09 financial downturn. Consolidated net assets increased \$1.6 billion to end the year at \$26.7 billion. Consolidated operating revenues exceeded expenses by \$516 million, compared to \$515 million in FY11. Stanford's FY12 financial results benefitted from record gifts, modest investment returns, and increased health care services and other revenue sources.

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 FY12, the University continued to strengthen its financial position. FY12 net assets increased \$951 million to \$23.5 billion compared to \$22.6 billion in the prior year. The University's FY12 endowment rose in value by 3.2% over the prior year, ending FY12 at \$17.0 billion, just shy of its \$17.2 billion high at year-end 2008. Donor support and investment returns were the major factors contributing to these positive results.

FY12 FINANCIAL HIGHLIGHTS

Record support from donors. The University continues to benefit from the overwhelming generosity of its donors. FY12 gifts as reported by the University's Office of Development exceeded \$1.0 billion, 46% above the prior year and 14% more than Stanford's previous best in FY06. These results are evidence of the extraordinary support of our donor community and donors' endorsement of Stanford's vision and direction. Gifts and pledges of \$927 million—up 80% from FY11—are reported in the financial statements on an accrual basis.

The FY12 results included the final months of The Stanford Challenge, a five-year public fundraising campaign which ended December 31, 2011. The Stanford Challenge raised \$6.2 billion to support University-wide initiatives and multi-disciplinary research focused on some of society's most complex problems including the environment, human health, international affairs, K-12 education and the arts. These gifts also enable Stanford to remain accessible to the brightest students, to recruit and retain top faculty, and to create and maintain state of the art buildings and facilities.

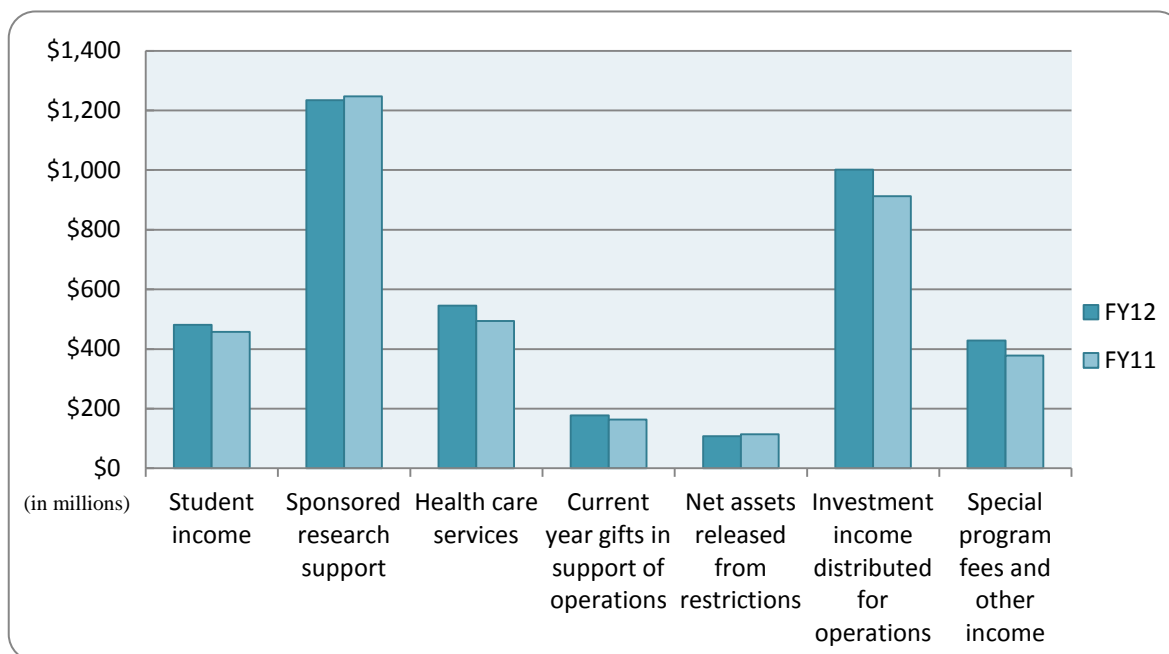
Positive investment performance. University investment returns in FY12 were \$1.3 billion, compared to \$3.4 billion in FY11. The positive FY12 returns were achieved during another volatile year in the financial markets, especially for international equities.

OPERATING RESULTS

The *Statements of Activities* include results from both operating and non-operating changes in the net assets of the University. Operating activities include the revenues earned and expenses incurred in the current year to support the University's core activities of teaching and research and other University priorities. The University ended the year with a surplus from operations of \$211 million in FY12 compared to \$257 million in FY11. FY12 operating revenues increased 6% compared to an increase in expenses of 7% during the same period.

Other changes in net assets are discussed in the *Financial Position* section of this analysis.

FIGURE 1
OPERATING REVENUES



OPERATING REVENUES

FY12 operating revenues were \$4.0 billion, reflecting a 6% increase over FY11. The components of the University’s operating revenues are shown in Figure 1 above.

Student Income

Total student income, which represents 12% of University operating revenues, increased 5% to \$481 million in FY12. Total student income includes tuition and fees from undergraduate and graduate programs and room and board; this amount is partially offset by financial aid. Revenues from student tuition and fees increased 4% in FY12 primarily as a result of 3.5% undergraduate and graduate tuition increases and a slight increase in both undergraduate and graduate student enrollment. Revenues from room and board increased 6% in FY12 primarily due to a slight increase in student enrollment and a 3.5% increase in the room and board rate.

Financial aid increased \$10.3 million or 4.5% in FY12 to \$241 million, reflecting Stanford’s continued commitment to provide an affordable education for all students. Approximately 59% of undergraduate students and 83% of graduate

students were awarded financial aid from Stanford in FY12, including scholarships, grants, loans and jobs.

Sponsored Research Support

Sponsored research support represents approximately one third of the University’s operating revenues. This category declined slightly from FY11 levels to \$1.2 billion in FY12, as the reductions in funds from the federal economic stimulus funding were almost fully offset by increases in other sources of sponsored research support.

The federal economic stimulus bill, the American Recovery and Reinvestment Act (ARRA), has been a major driver of sponsored research support for the past several years. As of August 31, 2012, Stanford had been awarded \$310 million of ARRA funding; approximately \$51 million of this amount was spent by the University and SLAC National Accelerator Laboratory (SLAC) in FY12 (compared to \$131 million in FY11) bringing the total amount spent to date to \$275 million.

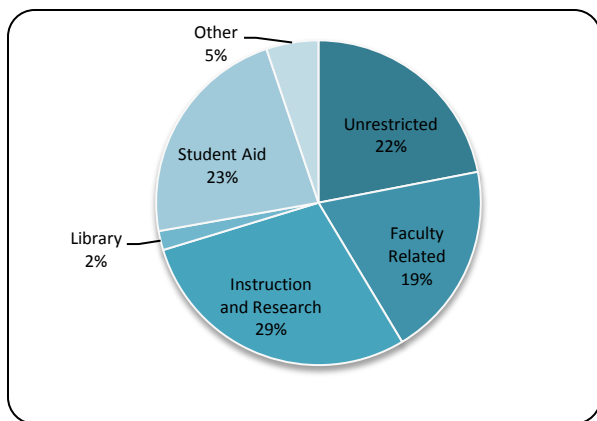
The majority of the University’s sponsored research support (84% including SLAC), is received directly or indirectly from the federal

government. The largest federal sponsor, the Department of Health and Human Services, provided revenue of \$417 million in FY12 compared to \$449 million in the prior year. Most of these funds support research within the University's School of Medicine.

Direct costs for SLAC increased \$2 million or less than 1% over FY11. Increased funding for Basic Energy Sciences and other programs of \$37 million was nearly offset by lower ARRA funding, down \$35 million to \$13 million in FY12.

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. This amount covers costs related to facilities, utilities and administrative costs incurred in connection with sponsored research. For FY12, the federal and non-federal indirect cost recovery increased \$6 million to \$226 million as a result of slightly higher indirect cost rates on new awards.

**FIGURE 2
ENDOWMENT PAYOUT BY PURPOSE**



Health Care Services

FY12 health care services revenue for the University increased \$51 million or 10% from FY11 to \$545 million and represented 14% 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

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, 2012, the endowment totaled \$17.0 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.

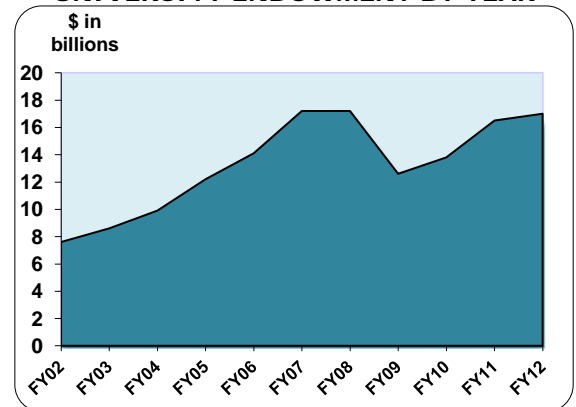
Gifts and pledge payments, investment returns, and other invested funds added \$1.4 billion to the endowment in FY12.

Payout to operations from the endowment continues to be a significant source of operating revenue for the University, covering approximately 23% of expenses in FY12, compared to 22% in FY11.

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, 19% covers faculty salaries and support, 22% is unrestricted and the remainder is split between library support and other purposes.

UNIVERSITY ENDOWMENT BY YEAR



addition, the Hospitals pay the University for other essential services such as medical direction, telecommunication, legal and internal audit services. Health care services revenues of \$520 million represent the net value of services provided by the University to the Hospitals; these amounts are eliminated in consolidation.

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

Current year gifts in support of operations increased 9% to \$178 million in FY12. Net assets released from restrictions decreased 5% to \$108 million.

Total Investment Income Distributed for Operations

Total investment income distributed for operations represented 25% of University revenue, the second highest source of operating revenue for the University, and up from 24% in FY11.

- Endowment income distributed for operations increased 11% to \$871 million in FY12, from \$785 million in FY11. The endowment payout as a percentage of the beginning endowment value decreased from 5.7% for FY11 to 5.3% for FY12 as a result of growth in the endowment value.
- Expendable funds pools and other investment income distributed for operations was \$131 million in FY12, compared to \$128 million in FY11. 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. Positive returns in both FY11 and FY10 resulted in the payouts to these funds over the past two years. See Note 6 to the FY12 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 FY12 Consolidated Financial Statements.

OPERATING EXPENSES

Total expenses increased \$256 million, or 7%, to \$3.8 billion in FY12. 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 7% in FY12 to \$2.3 billion. The increase resulted from a combination of modest salary programs designed to maintain Stanford's competitive position, higher benefit costs, and increases in headcount to support new programs and facilities recently placed in service.
- Depreciation expense increased by 7% to \$277 million in FY12 from \$259 million in FY11. The increase in this category resulted from buildings recently placed in service as described in the Capital Projects section below.
- Other operating expenses increased 7% to \$1.2 billion in FY12 from \$1.1 billion in FY11. These increases, in large part, were due to additional expenses incurred in support of new programs and facilities.

FINANCIAL POSITION

The University's *Statements of Financial Position* reflect strong donor support, solid investment returns and strong operating results over the past three years. Total University assets increased \$1.3 billion in FY12 to end the year at \$29.0 billion. Total University liabilities increased slightly from \$5.1 billion to \$5.5 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, 2012, the University's cash position included approximately \$427 million of the April 2009 taxable bond proceeds.

Investments

Investments increased by \$1.1 billion, up 5% from FY11 due to positive investment returns and new gifts received from our generous donors. Alternative investments, including various types of limited partnerships, private equity funds, venture capital funds, natural resources investments, real estate and hedge funds, represent approximately 71% of total investments at August 31, 2012. 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 FY12, the University invested \$403 million in capital projects, bringing gross plant facilities before accumulated depreciation to \$6.9 billion. Plant facilities, net of accumulated depreciation, increased \$152 million to \$3.8 billion.

Buildings completed and opened in FY12 include the Arrillaga Family Dining Commons and the Jill and John Freidenrich Center for Translational Research. Construction continued on the Bing Concert Hall and the Bioengineering/Chemical Engineering Building. In FY12, preparations also began for the new central energy facility—the Stanford Energy Systems Innovation (SESI)—which will reduce overall energy consumption and use cleaner energy sources.

The Knight Management Center (the new Graduate School of Business) and the William H. Neukom building in the law school opened in FY11.

The University is committed to being a leader in environmental sustainability. This effort is reflected in the design, construction and operation of campus facilities where the goal is to provide safe, productive indoor environments that use energy, water and other natural resources efficiently. Under the University's sustainability

standards, new buildings must use 30% less energy than current code requirements and 25% less water than similar buildings.

Debt

Total debt decreased \$18 million to \$2.7 billion as of August 31, 2012. During FY12, 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 designed 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.

The University issued \$221 million in taxable and tax-exempt debt to refinance certain tax-exempt bonds and commercial paper notes, achieving savings in interest costs.

Unrestricted Net Assets

In total, unrestricted net assets of the University increased \$851 million to \$12.1 billion, with \$211 million resulting from operating activities. The most significant components of non-operating changes in unrestricted net assets in FY12 were the \$394 million increase in realized and unrealized investment gains and \$253 million in gifts not related to current year operating activities.

Temporarily Restricted Net Assets

Temporarily restricted net assets decreased \$211 million to \$6.0 billion in FY12. The University received \$229 million of new temporarily restricted gifts and pledges in FY12 that partially offset a \$216 million decrease in realized and unrealized investment gains and \$233 million in transfers relating to capital and other gifts released from their restrictions for assets placed in service and for operating activities.

Permanently Restricted Net Assets

Permanently restricted net assets increased \$310 million to \$5.4 billion during FY12. The increase was driven by \$227 million in new gifts and pledges and \$55 million of transfers from other net asset categories 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), referred to as the Hospitals, are combined in the FY12 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. SHC is preparing to break ground by March 2013 and construction is now well underway at LPCH. Based on current estimates, management expects these facilities to be completed by 2017. These improvements will assure that the Hospitals have adequate inpatient capacity in modern, technologically-advanced, and patient centered 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 FY12 Consolidated Financial Statements.

STANFORD HOSPITAL AND CLINICS

SHC produced solid operating results in FY12, generating income from operations of \$237 million compared to \$173 million for FY11. SHC's favorable operating results were due in part to the growth in the number of physicians performing clinical services at the hospital. Net assets grew by \$391 million, or 30%, to \$1.7 billion mainly due to high patient

volumes, effective cost controls, strong operating performance and successful fundraising.

Operating Results

Operating revenues increased by 15% to \$2.4 billion. Net patient revenues accounted for \$2.3 billion of operating revenues. Both inpatient and outpatient revenues, which represent 51% and 49% of patient revenues, respectively, grew significantly due to strong volume growth and physician recruitment, including the acquisition of medical practices by University HealthCare Alliance (UHA), SHC's community physician foundation. Operating revenues also included \$49.6 million from the Hospital Quality Assurance Fee Program (QAF) which provides supplemental payments to hospitals for Medi-Cal patients.

Operating expenses increased 13% to \$2.2 billion in FY12. Salaries and benefits grew by 11% to \$988 million primarily in response to growth in patient volumes (including UHA) and to maintain SHC's position in the competitive market for health care professionals.

Physicians' services and support increased by 9% to \$368 million. This category includes all payments to the University for services provided by the School of Medicine for its clinical services. Other operating expenses were up by 22% to \$746 million as a result of costs related to increased patient activity (including UHA), enhanced IT infrastructure, and \$43.5 million in Hospital Fee Program payments to the State of California.

Statement of Financial Position (Balance Sheet)

SHC's *Statement of Financial Position* reflected 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 \$196 million to \$1.9 billion during FY12. As of August 31, 2012, SHC recorded \$230 million in construction in progress related to rebuilding SHC.

In FY12, SHC completed a new tax-exempt bond offering and refunding of bonds in the amount of \$568 million. The purpose of the new tax-exempt bonds is to provide support for the construction of SHC's new hospital.

Other SHC highlights

Costs of charity care and uncompensated costs including those related to services provided to patients under Medi-Cal and Medicare in excess of reimbursement, were \$366 million in FY12, up 12% from FY11.

In FY12, SHC was one of 65 hospitals in the nation named a 2011 Top Hospital by The Leapfrog Group, an honor that rewards medical centers for quality and efficiency, including success in such areas as infection rates, safety practices, mortality rates for common procedures and measures of efficiency. SHC was also re-designated as a Magnet hospital, which recognizes excellence in nursing.

LUCILE PACKARD CHILDREN'S HOSPITAL AT STANFORD

LPCH's net assets increased \$225 million in FY12, compared to \$155 million in the prior year. Solid operating results and strong donor support contributed to the FY12 results.

LPCH's net assets were \$1.5 billion at August 31, 2012.

Operating Results

Income from operations was \$69 million in FY12, compared to \$92 million in FY11. Net revenues over expenses of \$35 million and \$33 million from the Hospital Quality Assurance Fee Program (QAF) and Hospital Fee Program—programs which provide supplemental payments to certain hospitals for Medi-Cal patients—contributed to the FY12 and FY11 results, respectively.

Net patient revenues before the provision for doubtful accounts were \$931 million in FY12, compared to \$871 million in FY11. The FY12 results reflected an increase in the acuity of the patients, stronger payer mix and higher commercial contract rates.

Operating expenses increased by 11% in FY12. The majority of the increase stemmed from salary and benefit costs associated with treating patients with higher acuity and payments to the University for physician and other purchased services.

Statement of Financial Position (Balance Sheet)

LPCH's *Statement of Financial Position* reflected significant donor contributions, funding from the State of California (Proposition 3, Children's Hospital Bond Act of 2008) and investments in the facilities and systems required to continue to provide children's hospital services to the community. Gross property and equipment increased \$89 million during FY12, bringing the net investment in property and equipment to \$521 million at August 31, 2012.

In FY12, LPCH completed a \$200 million new fixed rate debt offering to finance a portion of its major facilities replacement project. In addition, LPCH restructured \$51 million of revenue bonds and converted \$93 million of variable rate debt to five-year fixed rate put bonds.

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 \$230 million in FY12 compared to \$164 million in FY11.

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. Management is assessing and planning for the impact of the Acts and other significant changes in the health care industry.

Looking Forward

Stanford enters FY13 in a solid financial position. Our financial resources, together with our existing physical infrastructure and planned capital improvements provide a strong foundation to further develop and enhance our core teaching, research and patient care missions. We are excited about future opportunities in higher education, research and health care. We continue to pursue avenues to expand our ability to deliver Stanford's education through efforts such as online learning, entrepreneurship education, and investments in the arts and humanities. We are well positioned to focus on complex problems such as global poverty and health care transformation.

At the same time, Stanford tempers its future optimism and remains mindful of significant risks and challenges ahead in an uncertain economic environment. The outlook for federal research

funding remains uncertain as the Federal government addresses a significant budget deficit and rapidly growing entitlement obligations. The 2009 fiscal stimulus funding plan is ending. Global economic malaise continues to put pressure on investment returns. We remain committed to funding our strong financial aid programs to offset continuing financial pressures on students and their families. The Stanford Medical Center faces significant uncertainty as it plans for the impact of existing and future healthcare reform, which remains unknown. We continue to monitor and plan for these variables.

We are grateful for the continued commitment, trust and support of the Stanford community, including students, alumni, friends, faculty and staff, as we approach the opportunities and challenges ahead.



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



Daniel J. Morissette
Chief Financial Officer
Stanford Hospital and Clinic



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



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

SELECTED FINANCIAL AND OTHER DATA

Fiscal Years Ended August 31

	2012	2011	2010	2009	2008
(dollars in millions)					
CONSOLIDATED STATEMENT OF ACTIVITIES HIGHLIGHTS:					
Total Revenues (D)	\$ 6,814	\$ 6,289	\$ 5,707	\$ 5,542	\$ 5,345
Student income (A)	481	458	436	401	405
Sponsored research support	1,234	1,247	1,143	1,031	1,076
Health care services (D)	3,245	2,902	2,542	2,364	2,135
Total Expenses (D)	6,298	5,774	5,345	5,033	4,899
Change in net assets from operating activities	516	515	362	509	446
Other changes in net assets	1,043	3,194	1,131	(5,450)	471
Net change in total net assets	\$ 1,559	\$ 3,709	\$ 1,493	\$ (4,941)	\$ 917
CONSOLIDATED STATEMENT OF FINANCIAL POSITION HIGHLIGHTS:					
University					
Investments at fair value	\$ 22,247	\$ 21,189	\$ 17,804	\$ 16,501	\$ 21,758
Plant facilities, net of accumulated depreciation	3,826	3,674	3,584	3,270	2,887
Notes and bonds payable	2,709	2,727	2,816	2,517	1,532
Total assets	28,981	27,698	24,553	22,672	26,704
Total liabilities	5,476	5,143	5,118	4,633	4,013
Total net assets	23,505	22,555	19,435	18,039	22,691
Hospitals					
Investments at fair value	1,899	1,796	1,359	1,257	1,712
Plant facilities, net of accumulated depreciation	1,494	1,333	1,283	1,260	1,080
Notes and bonds payable	1,700	983	992	999	1,007
Total assets	5,803	4,283	3,658	3,472	3,670
Total liabilities	2,633	1,722	1,686	1,597	1,506
Total net assets	3,170	2,561	1,972	1,875	2,164
OTHER UNIVERSITY FINANCIAL DATA AND METRICS:					
Total endowment at year end	\$ 17,036	\$ 16,503	\$ 13,851	\$ 12,619	\$ 17,214
Endowment payout in support of operations	871	785	855	957	882
As a % of beginning of year endowment	5.3%	5.7%	6.8%	5.6%	5.1%
As a % of total expenses	23.1%	22.4%	25.9%	30.6%	27.8%
Total gifts (B)	1,035	709	599	640	785
STUDENTS:					
ENROLLMENT: (C)					
Undergraduate	6,999	6,927	6,887	6,878	6,812
Graduate	8,871	8,796	8,779	8,441	8,328
DEGREES CONFERRED:					
Bachelor degrees	1,715	1,670	1,671	1,680	1,646
Advanced degrees	3,305	3,199	3,046	2,932	2,928
FACULTY:					
Total Professoriate	1,934	1,903	1,910	1,876	1,829
ANNUAL UNDERGRADUATE TUITION RATE (IN DOLLARS)	\$ 40,050	\$ 38,700	\$ 37,380	\$ 36,030	\$ 34,800

(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.

(D) Certain prior year amounts have been reclassified to conform to the current year's presentation.

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 accounting principles generally accepted in the United States of America.

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 accounting principles generally accepted in the United States of America, 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 and Compliance 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 and Compliance Committees. Both meet with the respective Audit and Compliance 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 at August 31, 2012 and 2011, 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 Stanford 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.

A handwritten signature in black ink that reads "PricewaterhouseCoopers LLP".

December 12, 2012

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

At August 31, 2012 and 2011 (in thousands of dollars)

	2012			2011
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
ASSETS				
Cash and cash equivalents	\$ 1,140,088	\$ 594,760	\$ 1,734,848	\$ 1,694,215
Assets limited as to use, held by trustee	-	728,324	728,324	-
Accounts receivable, net	388,518	682,027	1,070,545	703,009
Receivables (payables) from SHC and LPCH, net	55,287	(55,287)	-	-
Prepaid expenses and other assets	81,335	99,314	180,649	155,763
Pledges receivable, net	707,378	360,876	1,068,254	894,694
Student loans receivable, net	76,699	-	76,699	75,722
Faculty and staff mortgages and other loans receivable, net	459,382	-	459,382	465,344
Investments at fair value, including securities pledged or on loan of \$97,788 and \$125,033 for 2012 and 2011, respectively	22,246,700	1,898,984	24,145,684	22,985,197
Plant facilities, net of accumulated depreciation	3,826,387	1,494,058	5,320,445	5,007,107
Works of art and special collections	-	-	-	-
TOTAL ASSETS	\$ 28,981,774	\$ 5,803,056	\$ 34,784,830	\$ 31,981,051
LIABILITIES AND NET ASSETS				
LIABILITIES:				
Accounts payable and accrued expenses	\$ 589,466	\$ 778,619	\$ 1,368,085	\$ 1,110,645
Accrued pension and post retirement benefit cost	649,318	154,227	803,545	662,946
Pending trades of securities	410,120	-	410,120	209,683
Liabilities under security lending agreements	141,199	-	141,199	182,027
Deferred rental and other income	556,728	-	556,728	548,363
Income beneficiary share of split interest agreements	367,037	-	367,037	387,947
Notes and bonds payable	2,708,706	1,700,427	4,409,133	3,709,785
U.S. government refundable loan funds	53,783	-	53,783	53,760
TOTAL LIABILITIES	5,476,357	2,633,273	8,109,630	6,865,156
NET ASSETS:				
Unrestricted	12,086,359	2,251,986	14,338,345	13,236,421
Temporarily restricted	6,032,515	710,447	6,742,962	6,597,966
Permanently restricted	5,386,543	207,350	5,593,893	5,281,508
TOTAL NET ASSETS	23,505,417	3,169,783	26,675,200	25,115,895
TOTAL LIABILITIES AND NET ASSETS	\$ 28,981,774	\$ 5,803,056	\$ 34,784,830	\$ 31,981,051

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

CONSOLIDATED STATEMENTS OF ACTIVITIES

For the years ended August 31, 2012 and 2011 (in thousands of dollars)

	2012			2011
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
UNRESTRICTED NET ASSETS				
OPERATING REVENUES:				
Student income:				
Undergraduate programs	\$ 298,049	\$ -	\$ 298,049	\$ 285,582
Graduate programs	287,225	-	287,225	274,784
Room and board	135,879	-	135,879	127,785
Student financial aid	(240,649)	-	(240,649)	(230,307)
TOTAL STUDENT INCOME	480,504	-	480,504	457,844
Sponsored research support:				
Direct costs - University	639,630	-	639,630	660,684
Direct costs - SLAC National Accelerator Laboratory	368,187	-	368,187	366,435
Indirect costs	226,424	-	226,424	220,248
TOTAL SPONSORED RESEARCH SUPPORT	1,234,241	-	1,234,241	1,247,367
Health care services:				
Patient care, net	-	3,220,020	3,220,020	2,880,250
Physicians' services and support - SHC and LPCH, net	519,930	(519,930)	-	-
Physicians' services and support - other facilities, net	25,019	-	25,019	22,033
TOTAL HEALTH CARE SERVICES	544,949	2,700,090	3,245,039	2,902,283
CURRENT YEAR GIFTS IN SUPPORT OF OPERATIONS	178,214	6,305	184,519	170,651
Net assets released from restrictions:				
Payments received on pledges	79,943	1,930	81,873	85,127
Prior year gifts released from donor restrictions	28,260	2,590	30,850	31,055
TOTAL NET ASSETS RELEASED FROM RESTRICTIONS	108,203	4,520	112,723	116,182
Investment income distributed for operations:				
Endowment	871,106	12,319	883,425	799,058
Expendable funds pools and other investment income	131,330	739	132,069	128,456
TOTAL INVESTMENT INCOME DISTRIBUTED FOR OPERATIONS	1,002,436	13,058	1,015,494	927,514
SPECIAL PROGRAM FEES AND OTHER INCOME	428,679	113,423	542,102	467,767
TOTAL OPERATING REVENUES	3,977,226	2,837,396	6,814,622	6,289,608
OPERATING EXPENSES:				
Salaries and benefits	2,334,359	1,377,549	3,711,908	3,448,611
Depreciation	277,479	129,089	406,568	394,405
Other operating expenses	1,154,472	1,025,198	2,179,670	1,931,332
TOTAL OPERATING EXPENSES	3,766,310	2,531,836	6,298,146	5,774,348
CHANGE IN NET ASSETS FROM OPERATING ACTIVITIES	\$ 210,916	\$ 305,560	\$ 516,476	\$ 515,260

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

CONSOLIDATED STATEMENTS OF ACTIVITIES, Continued

For the years ended August 31, 2012 and 2011 (in thousands of dollars)

	2012			2011
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
UNRESTRICTED NET ASSETS (continued)				
CHANGE IN NET ASSETS FROM OPERATING ACTIVITIES	\$ 210,916	\$ 305,560	\$ 516,476	\$ 515,260
Non-operating activities:				
Increase in reinvested gains	394,277	51,349	445,626	1,762,358
Donor advised funds, net	38,998	-	38,998	1,057
Current year gifts not included in operations	253,390	-	253,390	4,237
Equity and fund transfers from Hospitals, net	15,072	(15,072)	-	-
Capital and other gifts released from restrictions	124,865	5,865	130,730	248,921
Pension and other post employment benefit related changes other than net periodic benefit expense	(106,716)	(15,355)	(122,071)	97,381
Transfer to permanently restricted net assets, net	(36,361)	-	(36,361)	(56,247)
Transfer to temporarily restricted net assets, net	(21,032)	-	(21,032)	(16,121)
Swap interest and unrealized losses	(21,610)	(69,805)	(91,415)	(1,275)
Other	(897)	(11,520)	(12,417)	3,331
NET CHANGE IN UNRESTRICTED NET ASSETS	850,902	251,022	1,101,924	2,558,902
TEMPORARILY RESTRICTED NET ASSETS				
Gifts and pledges, net	229,441	375,140	604,581	343,759
Increase (decrease) in reinvested gains	(215,549)	10,222	(205,327)	932,343
Change in value of split interest agreements, net	6,195	(492)	5,703	(240)
Net assets released to operations	(108,203)	(23,883)	(132,086)	(137,948)
Capital and other gifts released to unrestricted net assets	(124,865)	(5,865)	(130,730)	(248,921)
Gift transfers from Hospitals, net	2,141	(2,141)	-	-
Transfer from unrestricted net assets, net	21,032	-	21,032	16,121
Transfer to permanently restricted net assets, net	(18,349)	(1,099)	(19,448)	(24,300)
Other	(2,505)	3,776	1,271	(4,947)
NET CHANGE IN TEMPORARILY RESTRICTED NET ASSETS	(210,662)	355,658	144,996	875,867
PERMANENTLY RESTRICTED NET ASSETS				
Gifts and pledges, net	227,079	420	227,499	150,847
Increase in reinvested gains	4,612	-	4,612	15,150
Change in value of split interest agreements, net	23,984	481	24,465	26,791
Transfer from unrestricted net assets, net	36,361	-	36,361	56,247
Transfer from temporarily restricted net assets, net	18,349	1,099	19,448	24,300
Other	-	-	-	408
NET CHANGE IN PERMANENTLY RESTRICTED NET ASSETS	310,385	2,000	312,385	273,743
NET CHANGE IN TOTAL NET ASSETS	950,625	608,680	1,559,305	3,708,512
Total net assets, beginning of year	22,554,792	2,561,103	25,115,895	21,407,383
TOTAL NET ASSETS, END OF YEAR	\$ 23,505,417	\$ 3,169,783	\$ 26,675,200	\$ 25,115,895

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the years ended August 31, 2012 and 2011 (in thousands of dollars)

	2012			2011
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
CASH FLOW FROM OPERATING ACTIVITIES				
Change in net assets	\$ 950,625	\$ 608,680	\$ 1,559,305	\$ 3,708,512
Adjustments to reconcile change in net assets to net cash provided by (used for) operating activities:				
Depreciation	277,479	129,089	406,568	394,405
Amortization, loss on disposal of fixed assets and other adjustments	17,523	1,279	18,802	19,026
Net gains on investments and security agreements	(947,706)	(32,305)	(980,011)	(3,420,395)
Net losses (gains) on derivatives	17,279	69,805	87,084	(3,645)
Changes in split interest agreements	8,901	11	8,912	45,755
Investment losses (gains) for restricted purposes	(13,388)	5,732	(7,656)	(37,798)
Gifts restricted for long-term investments	(293,970)	(316,040)	(610,010)	(292,145)
Equity and fund transfers from Hospitals	(17,214)	17,214	-	-
Gifts of securities and properties	(355,313)	-	(355,313)	(51,904)
Premiums received from bond issuance	21,434	59,614	81,048	1,534
Changes in operating assets and liabilities:				
Accounts receivable, pledges receivable and receivables from SHC and LPCH, net	(1,702)	(150,790)	(152,492)	(104,004)
Prepaid expenses and other assets	(19,387)	(915)	(20,302)	(4,852)
Accounts payable and accrued expenses	33,204	82,436	115,640	74,535
Accrued pension and post retirement benefit costs	127,811	12,788	140,599	(58,749)
Deferred rental and other income	8,365	-	8,365	22,126
Other	1,965	(6,984)	(5,019)	(10,649)
NET CASH PROVIDED BY (USED FOR) OPERATING ACTIVITIES	(184,094)	479,614	295,520	281,752
CASH FLOW FROM INVESTING ACTIVITIES				
Land, building and equipment purchases	(402,939)	(268,567)	(671,506)	(567,301)
Student, faculty and other loans:				
New loans made	(56,060)	-	(56,060)	(76,749)
Principal collected	56,852	-	56,852	48,996
Increase in assets limited as to use, held by trustees	-	(728,324)	(728,324)	-
Purchases of investments	(12,990,781)	(159,218)	(13,149,999)	(18,057,837)
Sales and maturities of investments	13,357,744	82,150	13,439,894	17,913,773
NET CASH PROVIDED BY (USED FOR) INVESTING ACTIVITIES	(35,184)	(1,073,959)	(1,109,143)	(739,118)
CASH FLOW FROM FINANCING ACTIVITIES				
Gifts and reinvested income for restricted purposes	227,680	50,732	278,412	203,515
Equity and fund transfers from Hospitals	21,117	(21,117)	-	-
Proceeds from borrowing	336,056	912,815	1,248,871	272,615
Bond issuance costs and interest rate swaps	(1,394)	(7,415)	(8,809)	(1,813)
Repayment of notes and bonds payable	(369,545)	(253,868)	(623,413)	(365,862)
Increase (decrease) in liabilities under security lending agreements	(40,828)	-	(40,828)	22,003
Other	23	-	23	320
NET CASH PROVIDED BY FINANCING ACTIVITIES	173,109	681,147	854,256	130,778
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(46,169)	86,802	40,633	(326,588)
Cash and cash equivalents, beginning of year	1,186,257	507,958	1,694,215	2,020,803
CASH AND CASH EQUIVALENTS, END OF YEAR	\$ 1,140,088	\$ 594,760	\$ 1,734,848	\$ 1,694,215
SUPPLEMENTAL DATA:				
Interest paid during the year	\$ 104,210	\$ 62,862	\$ 167,072	\$ 158,010
Cash collateral received under security lending agreements	\$ 106,581	\$ -	\$ 106,581	\$ 142,963
Increase (decrease) in payables for plant facilities	\$ 26,138	\$ 36,216	\$ 62,354	\$ (19,911)

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 its 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

SHC and LPCH are California not-for-profit public benefit corporations. The University is the sole member of each of these entities. SHC and LPCH support the mission of medical education and clinical research of the University’s School of Medicine (SoM). Collectively, these entities comprise the Stanford Medical Center. 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 University has partnered with SHC and LPCH, respectively, to establish physician practice management organizations to support the Stanford Medical Center’s mission of delivering quality care to the community and conducting research and education.

The “Hospitals” category presented in the consolidated financial statements comprises all of the accounts of SHC, LPCH, the University HealthCare Alliance and Packard Children’s Health Alliance physician practice management organizations, and a captive insurance company which SHC and LPCH jointly control. 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 of America ("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 which are not subject to donor-imposed restrictions. 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.

The operating activities of the University and the Hospitals include the revenues earned and expenses incurred in the current year to support the University's core activities of teaching and research or the Hospitals' patient care, teaching and research missions. The non-operating activities of the University and Hospitals include increases or decreases in reinvested gains, current year gifts not included in operations, capital and other gifts released from restrictions, pension and other post employment benefit related changes other than net periodic benefit expense and certain other non-operating activities.

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 which 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*).

ASSETS LIMITED AS TO USE, HELD BY TRUSTEES

Assets limited as to use include various accounts for the Hospitals 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. Assets limited as to use consist of cash and cash equivalents and short-term investments, recorded at cost, which approximates fair value.

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, 2012 and 2011 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 "donor advised funds, net" 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 "donor advised funds, net" at the time the transfer is made. At August 31, 2012 and 2011, approximately \$251.0 million and \$207.3 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 \$632.2 million and \$628.7 million at August 31, 2012 and 2011, respectively, 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 2% 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 2012 and 2011, 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 \$31.2 million and \$18.1 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 bonds and notes. 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 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 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 Medicare, Medi-Cal and other third-party 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, it is reasonably possible 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 SoM, 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 estimated cost of providing charity care was \$27.8 million and \$22.4 million for the years ended August 31, 2012 and 2011, respectively. This cost is estimated by calculating a ratio of total costs to gross patient service charges at established rates, and then multiplying that ratio by gross uncompensated patient service charges at established rates associated with providing care to charity patients.

The Hospitals did not receive any funding to subsidize the costs of providing charity care for the years ended August 31, 2012 and 2011. The Hospitals also provide services to other patients under Medicare, 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 Medicare, Medi-Cal and other publicly sponsored programs for the years ended August 31, 2012 and 2011 were \$568.1 million and \$467.5 million, respectively.

Provider Fee

The State of California enacted legislation in 2009 through 2012 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. Certain rates under these programs are pending approval from the Centers for Medicare & Medicaid Services.

For the years ended August 31, 2012 and 2011, the Hospitals recorded \$76.5 million and \$47.8 million, respectively, in "other operating expenses" and recognized \$117.6 million and \$88.6 million, respectively, in "patient care, net" revenue under these programs.

Electronic Health Records Program

The Hospitals are participating in the Medicare and Medicaid Electronic Health Records (EHR) Incentive Programs, which provide payments to eligible professionals, eligible hospitals and critical access hospitals as they adopt, implement, upgrade or demonstrate meaningful use of certified EHR technology. For the year ended August 31, 2012, the Hospitals recognized \$13.4 million of revenue under these programs in "special program fees and other income."

RECENT ACCOUNTING PRONOUNCEMENTS

In December 2011, the Financial Accounting Standards Board (FASB) issued an update to the Accounting Standards Codification (ASC) which expanded the required disclosures about offsetting and related arrangements of an entity's financial assets and liabilities. The disclosures are intended to provide additional information to assist financial statements users in understanding the effect of those arrangements on the entity's financial position. This guidance is effective for annual periods beginning after January 1, 2013. The University and Hospitals are currently evaluating the impact that this guidance will have on its consolidated financial statement disclosures.

In July 2011, the FASB issued an update to the ASC to improve the transparency about a health care entity's net patient service revenue and the related allowance for doubtful accounts. The guidance requires the provision for bad debts related to patient service revenue to be presented as a deduction from patient service revenue. This guidance is effective for annual periods beginning after December 15, 2012. The Hospitals early adopted this guidance and recorded provision for bad debts of \$108.3 million in "patient care, net" in the "health care services" category for the year ended August 31, 2012. The Hospitals also applied this guidance retroactively and reclassified \$92.0 million of provision for bad debts from "other operating expenses" to "health care services" for the year ended August 31, 2011.

In May 2011, the FASB issued an update to the 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 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 the University and the Hospitals adopted for the year ended August 31, 2012.

2. Accounts Receivable

Accounts receivable, net of bad debt allowances, at August 31, 2012 and 2011, in thousands of dollars, are as follows:

	2012			2011
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
U.S. government	\$ 72,194	\$ -	\$ 72,194	\$ 66,173
Non-federal sponsors and programs	27,883	159,884	187,767	28,614
Pending trades of securities	241,458	-	241,458	109,793
Accrued interest on investments	7,255	-	7,255	7,645
Student	6,984	-	6,984	9,582
Patient and third-party payers	-	586,828	586,828	520,295
Other	34,917	36,325	71,242	54,645
	390,691	783,037	1,173,728	796,747
Less bad debt allowances	(2,173)	(101,010)	(103,183)	(93,738)
ACCOUNTS RECEIVABLE, NET	\$ 388,518	\$ 682,027	\$ 1,070,545	\$ 703,009

3. Pledges Receivable

Pledges are recorded at applicable risk-adjusted discount rates, ranging from 1.1% to 6.0% for the University and from 1.1% to 5.8% for the Hospitals, commensurate with the duration of the donor's payment plan. At August 31, 2012 and 2011, pledges receivable, net of discounts and allowances, in thousands of dollars, are as follows:

	2012			2011
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
One year or less	\$ 136,158	\$ 57,795	\$ 193,953	\$ 166,586
Between one year and five years	700,403	231,007	931,410	758,111
More than five years	84,283	109,351	193,634	199,847
	920,844	398,153	1,318,997	1,124,544
Less discounts and allowances	(213,466)	(37,277)	(250,743)	(229,850)
PLEDGES RECEIVABLE, NET	\$ 707,378	\$ 360,876	\$ 1,068,254	\$ 894,694

Conditional pledges for the University, which depend on the occurrence of a specified future and uncertain event, were \$10.7 million and \$12.9 million at August 31, 2012 and 2011, respectively. The Hospitals had conditional pledges of \$136.6 million and \$126.7 million at August 31, 2012 and 2011, 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 SoM.

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, 2012 and 2011, in thousands of dollars, are as follows:

	2012	2011
Institutional loans	\$ 19,350	\$ 18,082
Federally-sponsored loans	57,935	58,580
	77,285	76,662
Less allowance for student loan losses	(586)	(940)
STUDENT LOANS RECEIVABLE, NET	\$ 76,699	\$ 75,722

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 primarily 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 subordinated loans. Notes receivable amounting to \$456.6 million and \$462.5 million at August 31, 2012 and 2011, 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 2012 and 2011 are discussed below.

Investments held by the University and the Hospitals at August 31, 2012 and 2011, in thousands of dollars, are as follows:

	2012			2011
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
Cash and cash equivalents	\$ 993,908	\$ 41,295	\$ 1,035,203	\$ 425,251
Collateral held for securities loaned	106,581	-	106,581	142,963
Public equities	4,580,668	115,096	4,695,764	4,557,962
Derivatives	(12,999)	-	(12,999)	(13,834)
Fixed income	916,857	-	916,857	756,822
Real estate	4,988,534	-	4,988,534	4,500,588
Natural resources	1,688,315	-	1,688,315	1,683,569
Private equities	5,196,771	-	5,196,771	5,319,813
Absolute return	5,157,640	-	5,157,640	5,253,470
Assets held by other trustees	154,462	13,604	168,066	177,016
Other	204,952	-	204,952	181,577
	23,975,689	169,995	24,145,684	22,985,197
Hospital funds invested in the University's Merged Pool	(1,728,989)	1,728,989	-	-
INVESTMENTS AT FAIR VALUE	\$ 22,246,700	\$ 1,898,984	\$ 24,145,684	\$ 22,985,197

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, 2012 and 2011, 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*).

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 is 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 tables summarize the University's and the Hospitals' investments and other assets within the fair value hierarchy and asset categories at August 31, 2012 and 2011, in thousands of dollars:

	AS OF			
	AUGUST 31, 2012	LEVEL 1	LEVEL 2	LEVEL 3
UNIVERSITY*				
Cash and cash equivalents	\$ 993,908	\$ 898,162	\$ 95,746	\$ -
Collateral held for securities loaned	106,581	-	106,581	-
Public equities	4,580,668	2,209,678	265,186	2,105,804
Derivatives	(12,999)	23	(13,022)	-
Fixed income	916,857	325,271	591,586	-
Real estate	4,988,534	-	-	4,988,534
Natural resources	1,688,315	281,334	-	1,406,981
Private equities	5,196,771	33,617	-	5,163,154
Absolute return	5,157,640	156,269	1,790,422	3,210,949
Assets held by other trustees	154,462	-	-	154,462
Other	204,952	4	903	204,045
TOTAL	23,975,689	3,904,358	2,837,402	17,233,929
HOSPITALS				
Cash and cash equivalents	41,295	37,141	4,154	-
Public equities	115,096	66,907	48,189	-
Assets held by other trustees	13,604	-	-	13,604
TOTAL	169,995	104,048	52,343	13,604
CONSOLIDATED TOTAL	\$ 24,145,684	\$ 4,008,406	\$ 2,889,745	\$ 17,247,533

* Amounts include the Hospitals' cross investment in the University's investment pools of \$1.7 billion.

	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.

The University manages the majority of the Hospitals' investments, including the Hospitals' investment in the Merged Pool (MP), with a combined fair value of \$1.7 billion and \$1.6 billion at August 31, 2012 and 2011, 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, 2012 and 2011, in thousands of dollars:

FAIR VALUE MEASUREMENTS USING SIGNIFICANT UNOBSERVABLE INPUTS (LEVEL 3)	BEGINNING BALANCE AS OF SEPTEMBER 1, 2011	PURCHASES	SALES AND MATURITIES	NET REALIZED AND UNREALIZED GAINS (LOSSES)	TRANSFERS IN (OUT)	ENDING BALANCE AS OF AUGUST 31, 2012
UNIVERSITY						
Public equities	\$ 1,818,837	\$ 144,949	\$ (196,660)	\$ 246,955	\$ 91,723	\$ 2,105,804
Real estate	4,500,588	455,238	(404,832)	437,540	-	4,988,534
Natural resources	1,465,589	164,985	(189,785)	(29,685)	(4,123)	1,406,981
Private equities	5,304,442	694,159	(885,894)	50,447	-	5,163,154
Absolute return	3,390,273	263,678	(611,871)	(7,156)	176,025	3,210,949
Assets held by other trustees	163,044	61,238	(61,798)	(8,022)	-	154,462
Other	180,775	24,156	(10,283)	9,397	-	204,045
TOTAL	16,823,548	1,808,403	(2,361,123)	699,476	263,625	17,233,929
HOSPITALS						
Assets held by other trustees	13,972	-	-	(368)	-	13,604
TOTAL	13,972	-	-	(368)	-	13,604
CONSOLIDATED TOTAL	\$ 16,837,520	\$ 1,808,403	\$ (2,361,123)	\$ 699,108	\$ 263,625	\$ 17,247,533

FAIR VALUE MEASUREMENTS USING SIGNIFICANT UNOBSERVABLE INPUTS (LEVEL 3)	BEGINNING BALANCE AS OF SEPTEMBER 1, 2010	PURCHASES	SALES AND MATURITIES	NET REALIZED AND UNREALIZED GAINS	TRANSFERS IN (OUT)	ENDING BALANCE AS OF AUGUST 31, 2011
UNIVERSITY						
Public equities	\$ 1,360,802	\$ 494,886	\$ (219,550)	\$ 180,428	\$ 2,271	\$ 1,818,837
Real estate	3,402,206	406,211	(173,901)	856,250	9,822	4,500,588
Natural resources	1,283,095	180,044	(199,704)	207,290	(5,136)	1,465,589
Private equities	3,860,044	847,287	(646,726)	1,243,837	-	5,304,442
Absolute return	3,398,011	288,390	(578,744)	370,832	(88,216)	3,390,273
Assets held by other trustees	152,744	718	(5,649)	15,231	-	163,044
Other	150,335	37,184	(19,749)	28,275	(15,270)	180,775
TOTAL	13,607,237	2,254,720	(1,844,023)	2,902,143	(96,529)	16,823,548
HOSPITALS						
Assets held by other trustees	13,628	-	-	344	-	13,972
TOTAL	13,628	-	-	344	-	13,972
CONSOLIDATED TOTAL	\$ 13,620,865	\$ 2,254,720	\$ (1,844,023)	\$ 2,902,487	\$ (96,529)	\$ 16,837,520

Net realized and 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, 2012 and 2011, the change in unrealized gains (losses) for Level 3 investments still held at August 31, 2012 and 2011 was \$436.7 million and \$2.5 billion, respectively.

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. 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 years ended August 31, 2012 and 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, 2012, in thousands of dollars:

ASSET CLASS	FAIR VALUE	UNFUNDED COMMITMENT	REMAINING LIFE (YEARS)	REDEMPTION TERMS AND RESTRICTIONS
Public equities	\$ 2,370,936	\$ 65,543	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	1,854,770	945,514	0 to 13	Not eligible for redemption
Natural resources	894,688	472,322	0 to 15	Not eligible for redemption
Private equities	5,162,766	1,883,023	0 to 16	Not eligible for redemption
Absolute return	4,942,334	378,615	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	\$15,225,494	\$ 3,745,017		

At August 31, 2012, 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, 2012 and 2011, in thousands of dollars, are as follows:

	2012			2011
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
Investment income	\$ 277,208	\$ 13,782	\$ 290,990	\$ 229,949
Net realized and unrealized gains	974,508	47,778	1,022,286	3,453,911
TOTAL INVESTMENT RETURN	\$ 1,251,716	\$ 61,560	\$ 1,313,276	\$ 3,683,860

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, 2012, in thousands of dollars, is as follows:

YEAR ENDING AUGUST 31	FUTURE MINIMUM RENTAL INCOME
2013	\$ 91,615
2014	92,204
2015	88,445
2016	81,404
2017	75,700
Thereafter	1,740,970
TOTAL	\$ 2,170,338

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, 2012 and 2011, in thousands of dollars:

	2012	2011
UNIVERSITY		
Merged Pool	\$ 20,253,370	\$ 19,547,086
Expendable Funds Pool	3,004,565	2,648,621
Endowment Income Funds Pool	368,868	355,917
Other Investment Pools	394,407	392,285
Specific Investments	3,327,430	2,843,907
	<u>27,348,640</u>	<u>25,787,816</u>
Less:		
Amounts included in "cash and cash equivalents" in the <i>Statements of Financial Position</i>	(698,433)	(639,020)
Funds cross-invested in investment pools	(2,670,364)	(2,361,238)
Hospital funds invested in the University's investment pools	(1,733,143)	(1,598,071)
TOTAL	<u>22,246,700</u>	<u>21,189,487</u>
HOSPITALS		
Investments	1,898,984	1,795,710
TOTAL	<u>1,898,984</u>	<u>1,795,710</u>
CONSOLIDATED TOTAL	<u>\$ 24,145,684</u>	<u>\$ 22,985,197</u>

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, 2012 and 2011, the results of the EFP, in thousands of dollars, are as follows:

	2012	2011
Total investment return of the EFP	\$ 85,052	\$ 399,210
Less distributions to fund holders and operations	(95,483)	(83,199)
AMOUNTS ADDED TO (WITHDRAWN FROM) FFE	<u>\$ (10,431)</u>	<u>\$ 316,011</u>

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 manage 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, 2012 and 2011, and gains and losses for the years ended August 31, 2012 and 2011, in thousands of dollars:

	AS OF AUGUST 31, 2012			YEAR ENDED AUGUST 31, 2012
	NOTIONAL AMOUNT ¹	GROSS DERIVATIVE ASSETS ²	GROSS DERIVATIVE LIABILITIES ²	REALIZED AND UNREALIZED GAINS (LOSSES) ³
Interest-rate contracts	\$ 1,149,827	\$ 240	\$ 10,059	\$ (669)
Foreign exchange contracts	271,698	261	10,122	9,230
Equity contracts	112,677	4,799	20	(14,329)
Credit contracts	191,996	2,507	605	(6,860)
TOTAL	\$ 1,726,198	\$ 7,807	\$ 20,806	\$ (12,628)

	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)

¹ The notional amount is representative of the volume and activity of the respective derivative type during the years ended August 31, 2012 and 2011.

² Gross derivative assets less gross derivative liabilities are 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 "non-operating activities".

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, 2012 and 2011, 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	
2012				
Single name credit default swaps:				
A- to AA+	\$ 8,787	\$ 13,800	\$ 22,587	\$ 203
BBB- to BBB+	2,100	2,575	4,675	(257)
Total single name credit default swaps	10,887	16,375	27,262	(54)
Index credit default swaps ³	-	500	500	(11)
TOTAL CREDIT DEFAULT SWAPS SOLD	\$ 10,887	\$ 16,875	\$ 27,762	\$ (65)
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)

¹ The notional amount is representative of the volume and activity of the respective derivative type during the years ended August 31, 2012 and 2011.

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, 2012, the University had interest rate exchange agreements related to \$130.0 million of the outstanding balance of the CEFA Series S bonds in variable rate mode (see *Note 10*). The agreements, which have an interest rate of 3.69%, 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 \$37.5 million and \$25.0 million at August 31, 2012 and 2011, respectively, and is included in the *Statements of Financial Position*. In addition, the University issued an irrevocable standby letter of credit of \$15.0 million to support collateral requirements at August 31, 2012 (see *Note 10*).

At August 31, 2012, SHC had interest rate exchange agreements expiring through November 2045 (see *Note 11*). The agreements pay fixed interest rates to the counterparties varying from 3.37% to 4.08% in exchange for variable rate payments from the counterparties 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 \$27.5 million and \$7.1 million at August 31, 2012 and 2011, respectively, and was met by the posting of a standby letter of credit in the aggregate amount of \$30.0 million and \$20.0 million at August 31, 2012 and 2011, respectively, which may only be drawn upon in the event of a default by SHC. In July 2012, SHC terminated certain interest rate exchange agreements and recognized a loss of \$1.3 million in "non-operating activities" in the *Statements of Activities*.

The following table presents amounts for debt-related derivatives including the notional amount, the fair values at August 31, 2012 and 2011, and gains and losses for the years ended August 31, 2012 and 2011, in thousands of dollars:

	AS OF AUGUST 31, 2012		YEAR ENDED AUGUST 31, 2012	AS OF AUGUST 31, 2011		YEAR ENDED AUGUST 31, 2011
	NOTIONAL AMOUNT ¹	GROSS DERIVATIVE LIABILITIES ²	REALIZED AND UNREALIZED LOSSES ³	NOTIONAL AMOUNT ¹	GROSS DERIVATIVE LIABILITIES ²	REALIZED AND UNREALIZED GAINS ³
Debt-related interest-rate contracts:						
University	\$ 130,000	\$ 56,247	\$ (17,279)	\$ 130,000	\$ 38,968	\$ 3,645
Hospitals	747,150	236,183	(69,805)	749,400	165,693	672
TOTAL	\$ 877,150	\$ 292,430	\$ (87,084)	\$ 879,400	\$ 204,661	\$ 4,317

¹ The notional amount is representative of the volume and activity of the respective derivative type during the years ended August 31, 2012 and 2011.

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 "non-operating activities".

8. Plant Facilities

Plant facilities, net of accumulated depreciation, at August 31, 2012 and 2011, in thousands of dollars, are as follows:

	2012			2011
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
Land and improvements	\$ 498,741	\$ 93,667	\$ 592,408	\$ 555,153
Buildings and building improvements	4,360,595	1,195,038	5,555,633	5,446,557
Furniture, fixtures and equipment	1,733,009	860,638	2,593,647	2,523,924
Construction in progress	345,062	514,239	859,301	482,726
	6,937,407	2,663,582	9,600,989	9,008,360
Less accumulated depreciation	(3,111,020)	(1,169,524)	(4,280,544)	(4,001,253)
PLANT FACILITIES, NET OF ACCUMULATED DEPRECIATION	\$ 3,826,387	\$ 1,494,058	\$ 5,320,445	\$ 5,007,107

At August 31, 2012, \$1.2 billion and \$671.3 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 or cash and cash equivalents 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, 2012 and 2011, these amounts, in thousands of dollars, are as follows:

	2012	2011
Collateral deposits for certain securities loaned temporarily to brokers ^{1, 2}	\$ 106,581	\$ 142,963
Forward sale and purchase agreements ¹	34,618	39,064
LIABILITIES UNDER SECURITY LENDING AGREEMENTS	\$ 141,199	\$ 182,027

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, 2012 and 2011 was \$97.8 million and \$125.0 million, respectively.

10. University Notes and Bonds Payable

Notes and bonds payable for the University at August 31, 2012 and 2011, in thousands of dollars, are as follows:

	YEAR OF MATURITY	EFFECTIVE INTEREST RATE 2012/2011	OUTSTANDING PRINCIPAL	
			2012	2011
Tax-exempt:				
CEFA Fixed Rate Revenue Bonds:				
Series O	2031	5.13%	\$ -	\$ 89,555
Series P	2013	5.25%	51,260	51,260
Series Q	2032	5.25%	-	101,860
Series R	2011-2021	4.00% - 5.00%	-	111,585
Series T	2014-2039	4.00% - 5.00%	361,310	361,310
Series U	2032-2040	5.00% - 5.25%	293,135	215,375
CEFA Variable Rate Revenue Bonds and Notes:				
Series L	2014-2022	0.13%/0.12%	83,818	83,818
Series S	2039-2050	0.19%-0.22%/0.22%-0.36%*	181,200	181,200
Commercial Paper	2012	0.16%/0.10%	92,682	92,682
Taxable:				
Fixed Rate Notes and Bonds:				
Stanford University Bonds	2024	6.88%	150,000	150,000
Medium Term Note	2026	7.65%	50,000	50,000
Stanford University Series 2009A	2014-2019	3.63% - 4.75%	1,000,000	1,000,000
Stanford University Series 2012A	2042	4.01%	143,235	-
Other	2013-2015	Various	68,291	67,799
Variable Rate Notes:				
Commercial Paper	2012	0.21%/0.17%*	157,000	108,976
University notes and bonds payable			2,631,931	2,665,420
Unamortized original issue premiums/discounts, net			76,775	61,187
TOTAL			\$ 2,708,706	\$ 2,726,607

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

At August 31, 2012 and 2011, the fair value of these debt instruments was approximately \$3.1 billion and \$3.0 billion, respectively.

The University borrows at tax-exempt rates through the California Educational Facilities Authority (CEFA). 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 March 2012 by Standard and Poor's, Moody's Investors Service and Fitch Ratings, respectively.

In April 2012, CEFA Series U-2 bonds were issued in the amount of \$77.8 million plus an original issue premium of \$21.4 million. The bonds bear interest at a rate of 5.00% and mature on October 1, 2032. Proceeds were used (1) to refinance commercial paper notes which were issued to redeem CEFA Series Q bonds in February 2012; and (2) to pay bond issuance costs.

In April 2012, the University issued taxable fixed rate Series 2012A bonds in the amount of \$143.2 million. The bonds bear interest at a rate of 4.01% and mature on May 1, 2042. Proceeds were used (1) to refinance commercial paper notes which were issued to redeem CEFA Series O bonds in December 2011; (2) to refinance the outstanding CEFA Series R bonds which were redeemed in November 2011; and (3) to pay bond issuance costs.

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, 2012, irrevocable standby letters of credit of \$30.0 million were outstanding in the following amounts and for the following respective purposes: (1) \$15.0 million to support collateral requirements under certain interest rate exchange agreements discussed in *Note 7*; and (2) \$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, 2012.

Stanford holds controlling interests in several investment entities which were consolidated in the financial statements in fiscal years 2012 and 2011. At August 31, 2012 and 2011, taxable debt included \$66.2 million and \$66.5 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, 2012 and 2011, in thousands of dollars, are as follows:

COMMERCIAL PAPER	POTENTIAL BORROWINGS	OUTSTANDING BALANCE AT AUGUST 31	WEIGHTED AVERAGE DAYS TO MATURITY	AVERAGE EFFECTIVE INTEREST RATE
2012				
Taxable	\$ 500,000	\$ 157,000	44.1	0.21%
Tax-exempt	\$ 300,000	\$ 92,682	35.9	0.16%
2011				
Taxable	\$ 350,000	\$ 108,976	26.3	0.17%
Tax-exempt	\$ 300,000	\$ 92,682	32.3	0.10%

The University had \$265.0 million of revenue bonds in variable rate mode outstanding in addition to commercial paper notes at August 31, 2012. 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 these bonds, 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's interest expense, which includes amortized bond issuance costs and amortized bond premium or discount, in thousands of dollars, is as follows:

	2012	2011
Interest expense, gross	\$ 96,190	\$ 103,685
Less:		
Interest income earned on unspent proceeds	(433)	(782)
Interest capitalized as a cost of construction	(1,071)	(1,648)
Interest expense on Series 2009A bonds which is classified as an investment expense	(22,907)	(29,913)
Interest expense, net	\$ 71,779	\$ 71,342

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 losses” in the *Statements of Activities*, totaled \$4.3 million and \$5.6 million for the years ended August 31, 2012 and 2011, respectively.

At August 31, 2012, scheduled principal payments on notes and bonds, in thousands of dollars, are as follows:

YEAR ENDING AUGUST 31	PRINCIPAL PAYMENTS
2013 Commercial paper	\$ 249,682
2013 Variable debt subject to remarketing	265,018
2013 Other	67,706
2014	573,720
2015	55
2016	250,000
2017	-
Thereafter	1,225,750
TOTAL	\$ 2,631,931

11. Hospitals Notes and Bonds Payable

Notes, bonds and capital lease obligations for the Hospitals at August 31, 2012 and 2011, in thousands of dollars, are as follows:

	YEAR OF MATURITY	EFFECTIVE INTEREST RATE* 2012/2011	OUTSTANDING PRINCIPAL	
			2012	2011
SHC:				
CHFFA Fixed Rate Revenue Bonds:				
2003 Series A	2023	2.00%-5.00%	\$ -	\$ 78,595
2008 Series A-1	2040	2.25%-5.15%	69,760	70,360
2008 Series A-2	2040	1.00%-5.25%	103,200	104,100
2008 Series A-3	2040	1.00%-5.50%	83,415	84,165
2010 Series A	2031	4.00%-5.75%	144,860	149,345
2010 Series B	2036	4.50%-5.75%	146,710	146,710
2012 Series A	2051	5.00%	340,000	-
2012 Series B	2023	2.00%-5.00%	68,320	-
Promissory Note	2014	7.03%	363	539
CHFFA Variable Rate Revenue Bonds:				
2008 Series B	2045	0.17%	168,200	168,200
2012 Series C	2051	0.25%	60,000	-
2012 Series D	2051	0.78%	100,000	-
LPCH:				
CHFFA Fixed Rate Revenue Bonds:				
2003 Series C	2013-2027	3.25%	-	55,000
2008 Series A	2027-2033	1.45%	30,340	-
2008 Series B	2027-2033	1.45%	30,340	-
2008 Series C	2015-2023	1.45%	32,770	-
2012 Series A	2044-2051	5.00%	200,000	-
CHFFA Variable Rate Revenue Bonds:				
2008 Series A	2027-2033	0.13%	-	30,340
2008 Series B	2027-2033	0.16%	-	30,340
2008 Series C	2015-2023	0.16%	-	32,770
2012 Series B	2013-2027	3.00%	51,045	-
Capital lease obligations			-	13,643
Hospitals notes, bonds and capital lease obligations			1,629,323	964,107
Unamortized original issue premiums/discounts, net			71,104	19,071
TOTAL			\$ 1,700,427	\$ 983,178

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

At August 31, 2012 and 2011, the fair value of these debt instruments was approximately \$1.8 billion and \$1.0 billion, respectively.

The Hospitals borrow at tax-exempt rates through the California Health Facilities Financing Authority (CHFFA). 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. At August 31, 2012, there were no liquidity agreements between or among SHC, LPCH and 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 May 2012, CHFFA, on behalf of SHC, issued four series of revenue bonds in the aggregate principal amount of \$568.3 million. The bonds were comprised of \$340.0 million of 2012 Series A bonds, \$68.3 million of 2012 Series B bonds, \$60.0 million of 2012 Series C bonds and \$100.0 million of 2012 Series D bonds. Proceeds of the 2012 Series A, C and D bonds will be used to finance a portion of the Renewal Project (see *Note 20*). Proceeds of the 2012 Series B bonds were used to advance refund the 2003 Series A bonds. As a result of the refunding, the unamortized bond issuance costs and original issue premium of \$2.5 million related to the 2003 Series A bonds were included in "non-operating activities" in the *Statements of Activities* for the year ended August 31, 2012.

In June 2011, SHC remarketed the 2008 Series A-2, A-3 and B-2 bonds in the aggregate principal amount of \$272.4 million. SHC converted both the 2008 Series A-2 bonds from a weekly interest rate mode and the 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 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 2008 Series B-2 bonds from a weekly interest rate mode to a commercial paper mode.

At August 31, 2012, SHC has \$328.2 million revenue bonds in variable rate mode outstanding. The 2008 Series B-1 bonds bear interest at a weekly rate, and bondholders have the option to tender their bonds on a weekly basis. The 2008 Series B-2 bonds bear interest at a commercial paper rate and are outstanding for various interest periods of 270 days or less. Bondholders in commercial paper mode have the option to tender their bonds only at the end of the commercial paper rate period.

The 2012 Series C bonds are in a Windows weekly floating index mode and cannot be tendered for 180 days after a 30 day notice and remarketing period. The 2012 Series D bonds are also in a floating index mode with monthly interest rate resets and were directly placed with U.S. Bank. The 2012 Series D bonds are not subject to remarketing or tender until May 23, 2019.

In the event SHC receives notice of any optional tender of the 2008 Series B-1 bonds or the 2012 Series C bonds, 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, SHC will have a current obligation to purchase the bonds tendered. SHC has identified several sources of funding including cash and money market funds to provide for the full and timely purchase price of any bonds tendered in the event of a failed remarketing.

At August 31, 2012, SHC has irrevocable standby letters of credit in the aggregate amount of \$53.3 million posted with certain beneficiaries in the following amounts and for the following respective purposes: (i) \$30.0 million to support collateral requirements under certain interest rate exchange agreements discussed in *Note 7*, (ii) \$13.3 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, 2012 and 2011.

LPCH

In March 2012, CHFFA, on behalf of LPCH, issued 2012 Series A bonds and 2012 Series B bonds in the aggregate principal amount of \$251.0 million. Proceeds of the 2012 Series A bonds will be used to finance a portion of the Renewal Project and to pay bond issuance costs. Proceeds of the 2012 Series B bonds were used to advance refund the 2003 Series C bonds and to pay bond issuance costs. As a result of the refunding, the unamortized bond issuance costs and original issue premium of \$3.7 million related

to the 2003 Series C bonds were included in “non-operating activities” in the *Statements of Activities* for the year ended August 31, 2012.

In March 2012, LPCH converted the 2008 Series A, B and C revenue bonds in the aggregate principal amount of \$93.4 million from weekly variable rate mode to five-year fixed rate put bonds.

At August 31, 2012, LPCH has irrevocable standby letters of credit in the aggregate amount of \$13.3 million posted with certain beneficiaries in the following amounts and for the following respective purposes: (i) \$6.7 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, 2012 and 2011.

INTEREST

The Hospitals’ interest expense, which includes settlements under the interest rate exchange agreements, amortized bond issuance costs and amortized bond premium or discount, in thousands of dollars, is as follows:

	2012	2011
Interest expense, gross, excluding settlements under the interest rate exchange agreements	\$ 42,435	\$ 30,880
Settlements under the interest rate exchange agreements	19,926	19,864
Less:		
Interest capitalized as a cost of construction	(7,246)	(1,701)
Interest expense, net	\$ 55,115	\$ 49,043

PRINCIPAL PAYMENTS

At August 31, 2012, scheduled principal payments on notes, bonds and capital lease obligations, in thousands of dollars, are as follows:

YEAR ENDING AUGUST 31	PRINCIPAL PAYMENTS
2013 Variable debt subject to remarketing	\$ 228,200
2013 Other	12,694
2014	14,854
2015	17,075
2016	18,930
2017	19,065
Thereafter	1,318,505
TOTAL	\$ 1,629,323

12. University Endowment

The University classifies a substantial portion of its financial resources as endowment, which is invested to generate income 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 \$37.5 million and \$34.9 million at August 31, 2012 and 2011, respectively.

Endowment funds by net asset classification at August 31, 2012 and 2011, in thousands of dollars, are as follows:

	UNRESTRICTED	TEMPORARILY RESTRICTED	PERMANENTLY RESTRICTED	TOTAL
2012				
Donor-restricted endowment funds	\$ (37,537)	\$ 5,016,796	\$ 4,951,569	\$ 9,930,828
Funds functioning as endowment	7,104,976	-	-	7,104,976
TOTAL ENDOWMENT FUNDS	\$ 7,067,439	\$ 5,016,796	\$ 4,951,569	\$ 17,035,804
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

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, 2012 and 2011, in thousands of dollars, are as follows:

	UNRESTRICTED	TEMPORARILY RESTRICTED	PERMANENTLY RESTRICTED	TOTAL
2012				
Endowment, beginning of year	\$ 6,641,749	\$ 5,215,842	\$ 4,645,015	\$ 16,502,606
Investment returns:				
Earned income	208,731	-	-	208,731
Unrealized and realized gains	507,530	280,109	4,076	791,715
Total investment returns	716,261	280,109	4,076	1,000,446
Amounts distributed for operations	(390,375)	(480,731)	-	(871,106)
Gifts, transfers and other changes in endowment:				
Current year gifts and pledge payments	3,390	26,490	234,530	264,410
Transfers of prior year gifts	50,255	95	18,030	68,380
EFP funds withdrawn from the endowment	(10,431)	-	-	(10,431)
Other funds invested in (withdrawn from) the endowment, net	54,603	(19,994)	47,072	81,681
Other	1,987	(5,015)	2,846	(182)
Total gifts, transfers and other changes in endowment	99,804	1,576	302,478	403,858
Total net increase (decrease) in endowment	425,690	(199,046)	306,554	533,198
ENDOWMENT, END OF YEAR	\$ 7,067,439	\$ 5,016,796	\$ 4,951,569	\$ 17,035,804
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
EFP funds invested in the endowment	316,011	-	-	316,011
Other funds invested in the endowment, net	63,880	2,120	55,358	121,358
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

13. Hospitals Endowments

The endowments of SHC and LPCH are intended to generate investment income to support their current operating and strategic initiatives. The following table summarizes each hospital's share of the Hospitals endowments at August 31, 2012 and 2011, in thousands of dollars:

	2012	2011
LPCH	\$ 266,393	\$ 270,361
SHC	14,822	13,520
TOTAL ENDOWMENT FUNDS	\$ 281,215	\$ 283,881

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 2012 and 2011.

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 \$216 thousand and \$277 thousand at August 31, 2012 and 2011, respectively.

Changes in Hospitals endowments, for the years ended August 31, 2012 and 2011, in thousands of dollars, are as follows:

	UNRESTRICTED	TEMPORARILY RESTRICTED	PERMANENTLY RESTRICTED	TOTAL
2012				
Endowments, beginning of year	\$ (277)	\$ 78,808	\$ 205,350	\$ 283,881
Investment returns:				
Earned income	-	13,786	-	13,786
Unrealized and realized gains (losses)	61	(5,728)	481	(5,186)
Total investment returns	61	8,058	481	8,600
Amounts distributed for operations	-	(12,319)	-	(12,319)
Gifts, transfers and other changes in endowments:				
Gifts and pledge payments	-	45	777	822
Other	-	(511)	742	231
Total gifts, transfers and other changes in endowments	-	(466)	1,519	1,053
Total net increase (decrease) in endowments	61	(4,727)	2,000	(2,666)
ENDOWMENTS, END OF YEAR	\$ (216)	\$ 74,081	\$ 207,350	\$ 281,215
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

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, 2012 and 2011, per the *Statements of Activities* reconciled to the cash basis reported by OOD, in thousands of dollars:

	2012	2011
Current year gifts in support of operations	\$ 178,214	\$ 163,692
Donor advised funds, net	38,998	1,057
Current year gifts not included in operations	253,390	4,237
Temporarily restricted gifts and pledges, net	229,441	196,615
Permanently restricted gifts and pledges, net	227,079	150,813
TOTAL PER STATEMENTS OF ACTIVITIES	927,122	516,414
Adjustments to arrive at gift total as reported by OOD:		
New pledges	(265,141)	(227,331)
Payments made on pledges	259,402	272,227
Pledge discounts and other adjustments	29,560	18,676
Donor advised funds not designated for Stanford	(35,811)	3,484
Non-cash gifts	4,982	4,791
Non-government grants, recorded as sponsored research support when earned	79,243	84,745
SHC gifts	33,357	35,152
Other	2,135	1,265
TOTAL AS REPORTED BY OOD	\$ 1,034,849	\$ 709,423

15. Functional Expenses

Expenses for each of the years ended August 31, 2012 and 2011 are categorized on a functional basis as follows, in thousands of dollars:

	2012			2011
	UNIVERSITY	HOSPITALS	CONSOLIDATED	CONSOLIDATED
Instruction and departmental research	\$ 1,240,458	\$ -	\$ 1,240,458	\$ 1,160,021
Organized research - direct costs	1,017,081	-	1,017,081	1,019,584
Patient services	-	2,289,310	2,289,310	2,187,914
Auxiliary activities	748,800	-	748,800	676,687
Administration and general	317,244	228,648	545,892	311,379
Libraries	169,456	-	169,456	159,112
Student services	151,502	-	151,502	126,644
Development	80,976	13,878	94,854	88,931
SLAC construction	40,793	-	40,793	44,076
TOTAL EXPENSES	\$ 3,766,310	\$ 2,531,836	\$ 6,298,146	\$ 5,774,348

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 SoM 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 through the *Stanford Contributory Retirement Plan* (SCRCP). University and participant contributions are primarily invested in annuities and mutual funds. University contributions under the SCRCP, which are vested immediately to participants, were approximately \$110.7 million and \$104.4 million for the years ended August 31, 2012 and 2011, 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 *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 (ERISA)'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, 2012 and 2011, 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
2012				
Change in plan assets:				
Fair value of plan assets, beginning of year	\$ 258,896	\$ -	\$ 128,991	\$ 387,887
Actual return on plan assets	43,856	-	10,251	54,107
Employer contributions	10,211	3,256	26,005	39,472
Plan participants' contributions	-	-	6,854	6,854
Benefits and plan expenses paid	(22,706)	(3,256)	(22,303) *	(48,265)
FAIR VALUE OF PLAN ASSETS, END OF YEAR	290,257	-	149,798	440,055
Change in projected benefit obligation:				
Benefit obligation, beginning of year	293,397	145,543	470,454	909,394
Service cost	3,298	9,419	13,221	25,938
Interest cost	13,110	6,812	24,388	44,310
Plan participants' contributions	-	-	6,854	6,854
Actuarial loss	62,027	21,151	67,964	151,142
Benefits and plan expenses paid	(22,706)	(3,256)	(22,303) *	(48,265)
BENEFIT OBLIGATION, END OF YEAR	349,126	179,669	560,578	1,089,373
NET LIABILITY RECOGNIZED IN THE STATEMENTS OF FINANCIAL POSITION	\$ (58,869)	\$ (179,669)	\$ (410,780)	\$ (649,318)
<i>* Net of Medicare subsidy</i>				
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)
<i>* Net of Medicare subsidy</i>				

The accumulated benefit obligation for the SRAP was \$345.0 million and \$289.8 million at August 31, 2012 and 2011, respectively.

Net periodic benefit expense and non-operating activities related to the Plans for the years ended August 31, 2012 and 2011, in thousands of dollars, includes the following components:

	STAFF RETIREMENT ANNUITY PLAN (SRAP)	FACULTY RETIREMENT INCENTIVE PROGRAM (FRIP)	POST RETIREMENT BENEFIT PLAN (PRBP)	TOTAL
2012				
Service cost	\$ 3,298	\$ 9,419	\$ 13,221	\$ 25,938
Interest cost	13,110	6,812	24,388	44,310
Expected return on plan assets	(17,296)	-	(10,480)	(27,776)
Amortization of:				
Prior service cost	534	-	2,569	3,103
Actuarial loss	-	6,485	8,214	14,699
NET PERIODIC BENEFIT EXPENSE	(354)	22,716	37,912	60,274
Net actuarial loss during period	35,467	21,151	67,900	124,518
Amortization of:				
Prior service cost	(534)	-	(2,569)	(3,103)
Actuarial loss	-	(6,485)	(8,214)	(14,699)
TOTAL AMOUNTS RECOGNIZED IN NON-OPERATING ACTIVITIES	34,933	14,666	57,117	106,716
TOTAL AMOUNT RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE AND NON-OPERATING ACTIVITIES	\$ 34,579	\$ 37,382	\$ 95,029	\$ 166,990
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 NON-OPERATING ACTIVITIES	(29,576)	(16,454)	(36,525)	(82,555)
TOTAL AMOUNT RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE AND NON-OPERATING ACTIVITIES	\$ (25,338)	\$ 6,500	\$ 9,379	\$ (9,459)

Cumulative amounts recognized in non-operating activities, but not yet recognized in net periodic benefit expense in the *Statements of Activities*, are presented in the following table for the years ended August 31, 2012 and 2011, in thousands of dollars:

	STAFF RETIREMENT ANNUITY PLAN (SRAP)	FACULTY RETIREMENT INCENTIVE PROGRAM (FRIP)	POST RETIREMENT BENEFIT PLAN (PRBP)	TOTAL
2012				
Prior service cost	\$ 1,394	\$ -	\$ 8,564	\$ 9,958
Net actuarial loss	57,726	122,018	227,438	407,182
ACCUMULATED PLAN BENEFIT COSTS NOT YET RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE				
	\$ 59,120	\$ 122,018	\$ 236,002	\$ 417,140
2011				
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 NET PERIODIC BENEFIT EXPENSE				
	\$ 24,187	\$ 107,352	\$ 178,885	\$ 310,424

The prior service costs and net actuarial loss expected to be amortized from non-operating activities to net periodic benefit expense in fiscal year 2013, in thousands of dollars, are as follows:

	STAFF RETIREMENT ANNUITY PLAN (SRAP)	FACULTY RETIREMENT INCENTIVE PROGRAM (FRIP)	POST RETIREMENT BENEFIT PLAN (PRBP)	Total
Prior service cost	\$ 540	\$ -	\$ 2,569	\$ 3,109
Net actuarial loss	\$ 2,970	\$ 7,464	\$ 11,165	\$ 21,599

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)	
	2012	2011	2012	2011	2012	2011
Discount rate	3.36%	4.67%	3.33%	4.74%	3.78%	5.14%
Covered payroll growth rate	3.54%	4.41%	4.42%	4.43%	N/A	N/A

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)	
	2012	2011	2012	2011	2012	2011
Discount rate	4.67%	4.61%	4.74%	4.67%	5.14%	5.10%
Expected returns on plan assets	7.00%	7.00%	N/A	N/A	8.00%	8.00%
Covered payroll growth rate	4.41%	4.76%	4.43%	4.14%	N/A	N/A

The expected long-term rate of return on asset assumptions for both the SRAP and PRBP plans is 7%. 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, and the future expectations for returns in each asset class, as well as the target asset allocation of the portfolios. 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 non-operating activities 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, 2012, a 7.5% annual rate of increase in the per capita costs of covered health care was assumed for the year ending August 31, 2013, 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 \$104.1 million and the aggregate annual service and interest cost by \$7.1 million. Decreasing the health care cost trend rate by 1% in each future year would decrease the accumulated PRBP obligation by \$82.1 million and the aggregate annual service and interest cost by \$5.6 million.

EXPECTED CONTRIBUTIONS

The University expects to contribute \$4.6 million, \$6.9 million, and \$2.5 million to its SRAP, FRIP, and PRBP, respectively, during the year ending August 31, 2013.

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 RETIREMENT ANNUITY PLAN (SRAP)	FACULTY RETIREMENT INCENTIVE PROGRAM (FRIP)	POST RETIREMENT BENEFIT PLAN (PRBP)	
			EXCLUDING MEDICARE SUBSIDY	EXPECTED MEDICARE PART D SUBSIDY
2013	\$ 28,265	\$ 6,936	\$ 17,369	\$ 2,629
2014	23,992	10,009	18,688	2,877
2015	24,843	11,989	19,908	3,146
2016	24,293	12,116	21,118	3,444
2017	23,791	12,826	22,521	3,757
2018 - 2022	111,899	75,879	134,261	24,436

INVESTMENT STRATEGY

The University's Retirement Program Investment Committee, 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, 2012, 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, 2012 and 2011 are as follows:

ASSET CATEGORY	STAFF RETIREMENT ANNUITY PLAN (SRAP)		POST RETIREMENT BENEFIT PLAN (PRBP)	
	2012	2011	2012	2011
Cash and cash equivalents	<1%	1%	0%	0%
Public equities	44%	40%	75%	74%
Fixed income	56%	59%	25%	26%
Private equities	<1%	<1%	0%	0%
TOTAL PORTFOLIO	100%	100%	100%	100%

For fiscal years 2012 and 2011, the weighted-average target allocations by asset category are as follows:

ASSET CATEGORY	STAFF RETIREMENT ANNUITY PLAN (SRAP)		POST RETIREMENT BENEFIT PLAN (PRBP)	
	2012	2011	2012	2011
Public equities	45%	45%	75%	75%
Fixed income	55%	55%	25%	25%
Private equities	<1%	0%	0%	0%
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, 2012 and 2011, in thousands of dollars, are as follows:

	AS OF AUGUST 31, 2012	LEVEL 1	LEVEL 2	LEVEL 3
SRAP:				
Cash and cash equivalents	\$ 1,111	\$ 1,111	\$ -	\$ -
Public equities	126,913	126,913	-	-
Fixed income	161,804	157,804	4,000	-
Private equities	429	-	-	429
TOTAL	\$ 290,257	\$ 285,828	\$ 4,000	\$ 429
PRBP:				
Public equities	\$ 112,239	\$ 112,239	\$ -	\$ -
Fixed income	37,559	37,559	-	-
TOTAL	\$ 149,798	\$ 149,798	\$ -	\$ -
TOTAL FAIR VALUE OF PLAN ASSETS	\$ 440,055	\$ 435,626	\$ 4,000	\$ 429

	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

The following table presents a reconciliation of beginning and ending balances for Level 3 investments in the SRAP for the years ended August 31, 2012 and 2011, in thousands of dollars:

FAIR VALUE MEASUREMENTS USING SIGNIFICANT UNOBSERVABLE INPUTS (LEVEL 3)	BEGINNING BALANCE AS OF SEPTEMBER 1, 2011	PURCHASES	SALES AND MATURITIES	NET REALIZED AND UNREALIZED LOSSES	TRANSFERS IN (OUT)	ENDING BALANCE AS OF AUGUST 31, 2012
Private equities	\$ 647	\$ -	\$ -	\$ (218)	\$ -	\$ 429
TOTAL	\$ 647	\$ -	\$ -	\$ (218)	\$ -	\$ 429

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

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 \$68.1 million and \$65.4 million for the years ended August 31, 2012 and 2011, 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:

	STAFF PENSION PLAN	POST RETIREMENT MEDICAL BENEFIT PLAN (PRMB)	TOTAL
2012			
Change in plan assets:			
Fair value of plan assets, beginning of year	\$ 159,583	\$ -	\$ 159,583
Actual return on plan assets	29,548	-	29,548
Employer contributions	11,025	3,617	14,642
Plan participants' contributions	-	1,152	1,152
Benefits and plan expenses paid	(9,452)	(4,769)	(14,221)
FAIR VALUE OF PLAN ASSETS, END OF YEAR	190,704	-	190,704
Change in projected benefit obligation:			
Benefit obligation, beginning of year	212,816	88,206	301,022
Service cost	2,589	2,528	5,117
Interest cost	10,436	4,108	14,544
Plan participants' contributions	-	1,152	1,152
Actuarial loss (gain)	41,392	(4,075)	37,317
Benefits and plan expenses paid	(9,452)	(4,769)	(14,221)
BENEFIT OBLIGATION, END OF YEAR	257,781	87,150	344,931
NET LIABILITY RECOGNIZED IN THE STATEMENTS OF FINANCIAL POSITION	\$ (67,077)	\$ (87,150)	\$ (154,227)
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	\$ (53,233)	\$ (88,206)	\$ (141,439)

The accumulated benefit obligation for the Pension Plan was \$253.4 million and \$209.2 million at August 31, 2012 and 2011, respectively.

Net periodic benefit expense and non-operating activities related to the plans for the years ended August 31, 2012 and 2011, in thousands of dollars, includes the following components:

	STAFF PENSION PLAN	POST RETIREMENT MEDICAL BENEFIT PLAN (PRMB)	TOTAL
2012			
Service cost	\$ 2,589	\$ 2,528	\$ 5,117
Interest cost	10,436	4,108	14,544
Expected return on plan assets	(13,708)	-	(13,708)
Amortization of:			
Prior service cost	-	264	264
Actuarial loss	5,613	245	5,858
NET PERIODIC BENEFIT EXPENSE	4,930	7,145	12,075
Net actuarial loss (gain) during period	25,552	(4,075)	21,477
Amortization of:			
Prior service cost	-	(264)	(264)
Actuarial loss	(5,613)	(245)	(5,858)
TOTAL AMOUNTS RECOGNIZED IN NON-OPERATING ACTIVITIES	19,939	(4,584)	15,355
TOTAL AMOUNT RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE AND NON-OPERATING ACTIVITIES	\$ 24,869	\$ 2,561	\$ 27,430
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 NON-OPERATING ACTIVITIES	(8,861)	(5,965)	(14,826)
TOTAL AMOUNT RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE AND NON-OPERATING ACTIVITIES	\$ (4,044)	\$ 1,089	\$ (2,955)

Cumulative amounts recognized in non-operating activities, but not yet recognized in net periodic benefit expense in the *Statements of Activities*, are presented in the following table for the years ended August 31, 2012 and 2011, in thousands of dollars:

	STAFF PENSION PLAN	POST RETIREMENT MEDICAL BENEFIT PLAN (PRMB)	TOTAL
2012			
Prior service cost	\$ -	\$ 2,904	\$ 2,904
Net actuarial loss (gain)	101,102	(964)	100,138
ACCUMULATED PLAN BENEFIT COSTS NOT YET RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE			
	\$ 101,102	\$ 1,940	\$ 103,042
2011			
Prior service cost	\$ -	\$ 3,168	\$ 3,168
Net actuarial loss	81,163	3,356	84,519
ACCUMULATED PLAN BENEFIT COSTS NOT YET RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE			
	\$ 81,163	\$ 6,524	\$ 87,687

The prior service cost and net actuarial loss expected to be amortized from non-operating activities to net periodic benefit expense in fiscal year 2013, in thousands of dollars, are as follows:

	STAFF PENSION PLAN	POST RETIREMENT MEDICAL BENEFIT PLAN (PRMB)	TOTAL
Prior service cost	\$ -	\$ 312	\$ 312
Net actuarial loss (gain)	\$ 10,677	\$ (71)	\$ 10,606

ACTUARIAL ASSUMPTIONS

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

	STAFF PENSION PLAN		POST RETIREMENT MEDICAL BENEFIT PLAN (PRMB)	
	2012	2011	2012	2011
Discount rate	3.42% - 3.62%	4.83% - 5.03%	3.43%	4.79%
Covered payroll growth	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:

	STAFF PENSION PLAN		POST RETIREMENT MEDICAL BENEFIT PLAN (PRMB)	
	2012	2011	2012	2011
Discount rate	4.83% - 5.03%	4.79% - 4.99%	4.79%	4.70%
Expected return on plan	6.25% - 8.00%	6.25% - 8.00%	N/A	N/A
Covered payroll growth	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, 2012, an 8.0% annual rate of increase in the pre-65 per capita costs, an 8.0% annual rate of increase in the post-65 prescription drug per capita costs, and a 6.8% rate of increase in the post-65 per capita cost of all other medical benefits was assumed for 2012, 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 \$218 thousand. Decreasing the health care cost trend rate by 1% in each future year would decrease the accumulated PRMB obligation by \$2.7 million and the aggregate annual service and interest cost by \$197 thousand.

EXPECTED CONTRIBUTIONS

The Hospitals expect to contribute \$10.4 million to their Pension Plan and \$4.5 million to their PRMB during the fiscal year ending August 31, 2013.

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	STAFF PENSION PLAN	POST RETIREMENT MEDICAL BENEFIT PLAN (PRMB)	
		EXCLUDING MEDICARE SUBSIDY	EXPECTED MEDICARE PART D SUBSIDY
2013	\$ 10,989	\$ 5,052	\$ 503
2014	11,699	5,347	543
2015	12,495	5,642	586
2016	13,183	5,917	627
2017	13,770	6,211	666
2018 - 2022	75,295	34,218	1,675

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 ERISA. 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, 2012, 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, 2012 and 2011 are as follows:

ASSET CATEGORY	STAFF PENSION PLAN	
	2012	2011
Cash equivalents	0%	0%
Public equities	48%	44%
Fixed income	52%	56%
Real estate	0%	0%
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 2012 and 2011, the weighted-average target allocations by asset category are as follows:

ASSET CATEGORY	STAFF PENSION PLAN	
	2012	2011
Cash equivalents	0% to 4%	<1%
Public equities	28% to 60%	46%
Fixed income	36% to 60%	44%
Real estate	0% to 12%	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, 2012 and 2011, in thousands of dollars, are as follows:

	AS OF			
	AUGUST 31, 2012	LEVEL 1	LEVEL 2	LEVEL 3
Cash and cash equivalents	\$ 902	\$ 902	\$ -	\$ -
Public equities	91,411	91,411	-	-
Fixed income	98,378	98,378	-	-
Other	13	13	-	-
TOTAL FAIR VALUE OF PENSION PLAN ASSETS	\$ 190,704	\$ 190,704	\$ -	\$ -

	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	\$ -	\$ -

There were no Level 3 investments in the Pension Plan during the year ended August 31, 2012. The following table presents a reconciliation of beginning and ending balances for Level 3 investments in the Pension Plan for the year ended August 31, 2011, in thousands of dollars:

FAIR VALUE MEASUREMENTS USING SIGNIFICANT UNOBSERVABLE INPUTS (LEVEL 3)	BEGINNING BALANCE AS OF SEPTEMBER 1, 2010		SALES AND MATURITIES	NET REALIZED AND UNREALIZED GAINS		ENDING BALANCE AS OF AUGUST 31, 2011	
		PURCHASES			TRANSFERS IN (OUT)		
Real estate	\$ 7,458	\$ -	\$ (8,256)	\$ 798	\$ -	\$ -	\$ -
TOTAL	\$ 7,458	\$ -	\$ (8,256)	\$ 798	\$ -	\$ -	\$ -

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, 2012 and 2011 was \$36.4 million and \$32.8 million, respectively, for the University and \$63.6 million and \$50.0 million, respectively, for the Hospitals.

Net minimum future operating lease payments and related present value, assuming a 3.82% discount rate for periods subsequent to August 31, 2012, in thousands of dollars, are as follows:

YEAR ENDING AUGUST 31	MINIMUM LEASE PAYMENTS		PRESENT VALUE OF MINIMUM LEASE PAYMENTS	
	UNIVERSITY	HOSPITALS	UNIVERSITY	HOSPITALS
2013	\$ 23,091	\$ 45,783	\$ 22,242	\$ 44,098
2014	18,548	36,649	17,208	34,002
2015	15,232	29,702	13,612	26,543
2016	14,135	27,473	12,166	23,647
2017	11,500	26,085	9,534	21,626
Thereafter	31,335	101,316	20,620	75,064
TOTAL	\$ 113,841	\$ 267,008	\$ 95,382	\$ 224,980

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 2012 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, 2010 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 SoM 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 2012, the Hospitals have recorded \$392 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, 35% of SHC's and 45% 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, 2012, the University had contractual obligations of approximately \$358.2 million in connection with major construction projects. Remaining expenditures on construction in progress are estimated to be \$584.7 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 \$651.9 million at August 31, 2012.

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, 2012.

21. Subsequent Events

The University and the Hospitals have evaluated subsequent events for the period from August 31, 2012 through December 12, 2012, the date the consolidated financial statements were available to be issued.

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 oversees management of 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 \$19.7 billion as of June 30, 2012. 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, 2012. The following discussion of endowment performance relates solely to investments in the MP. The MP realized a 1.0% investment gain for the 12 months ending June 30, 2012. Over the past 10 years, the MP achieved an annualized rate of return of 9.7%, growing from \$7.5 billion to \$19.7 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, 2012 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%

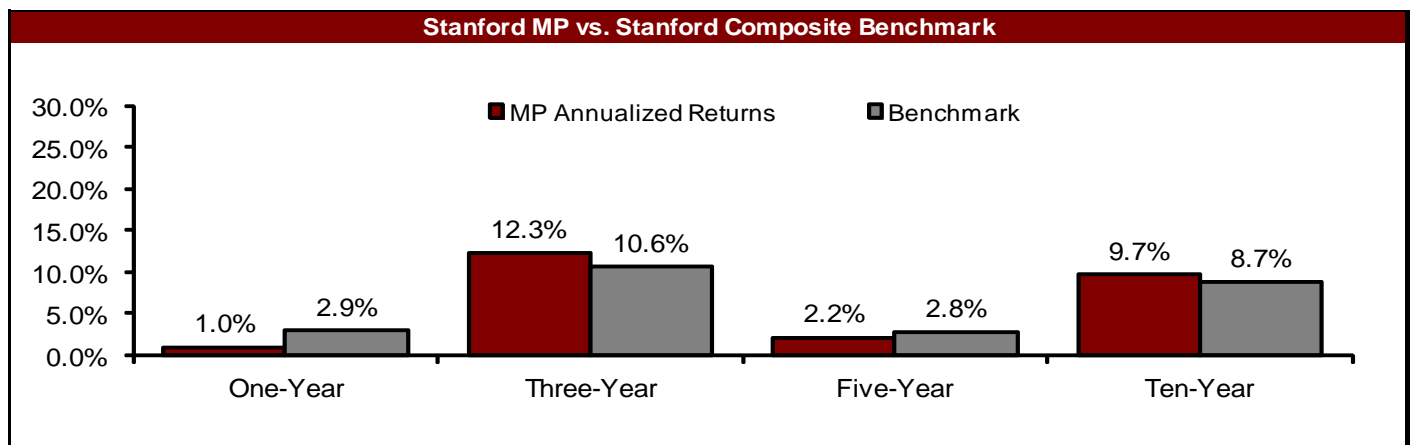
STANFORD MP PERFORMANCE COMPARED TO INFLATION The table below outlines annualized returns for various periods ending June 30, 2012.

MP PERFORMANCE COMPARED TO INFLATION

MP Performance Compared to Inflation				
	One-Year	Three-Year	Five-Year	Ten-Year
Nominal Endowment Return	1.0%	12.3%	2.2%	9.7%
GDP Deflator	1.7%	1.7%	1.6%	2.3%
Real Endowment Return	-0.7%	10.6%	0.6%	7.4%

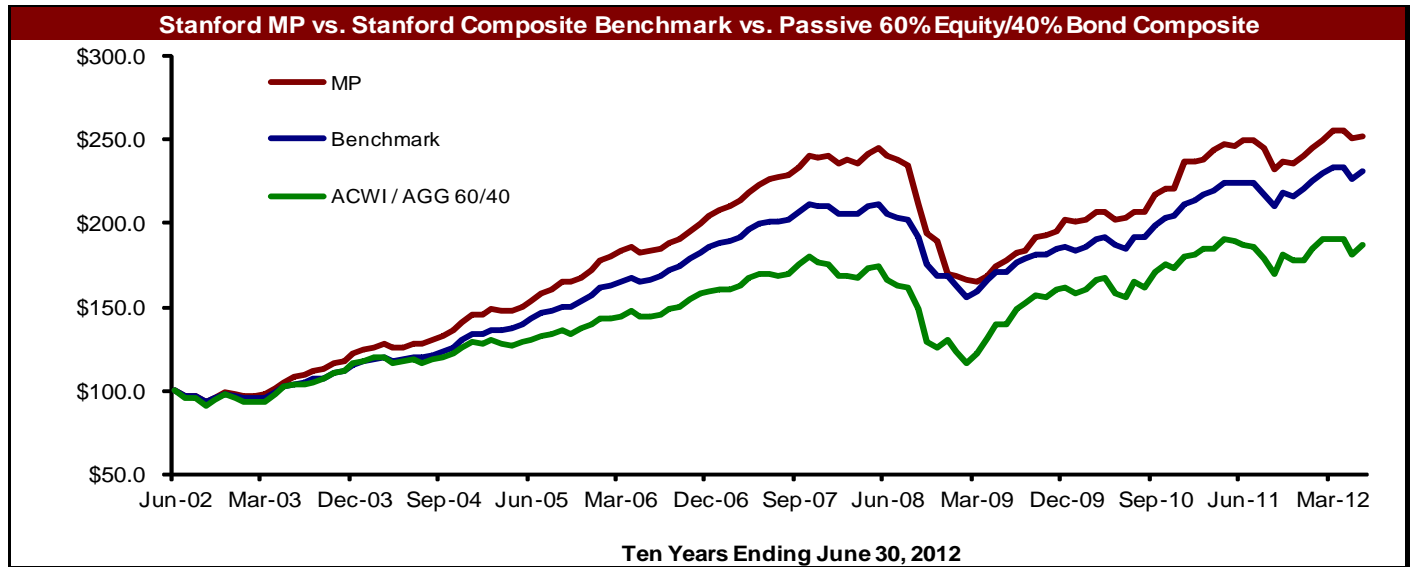
STANFORD MP PERFORMANCE COMPARED TO BENCHMARKS SMC evaluates the performance of investment managers by comparing their returns to benchmarks that are appropriate for each individual asset class. The SMC Board reviews asset class benchmarks on an annual basis to ensure comparability. SMC reviews overall 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, 2012.

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 \$1.6 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:

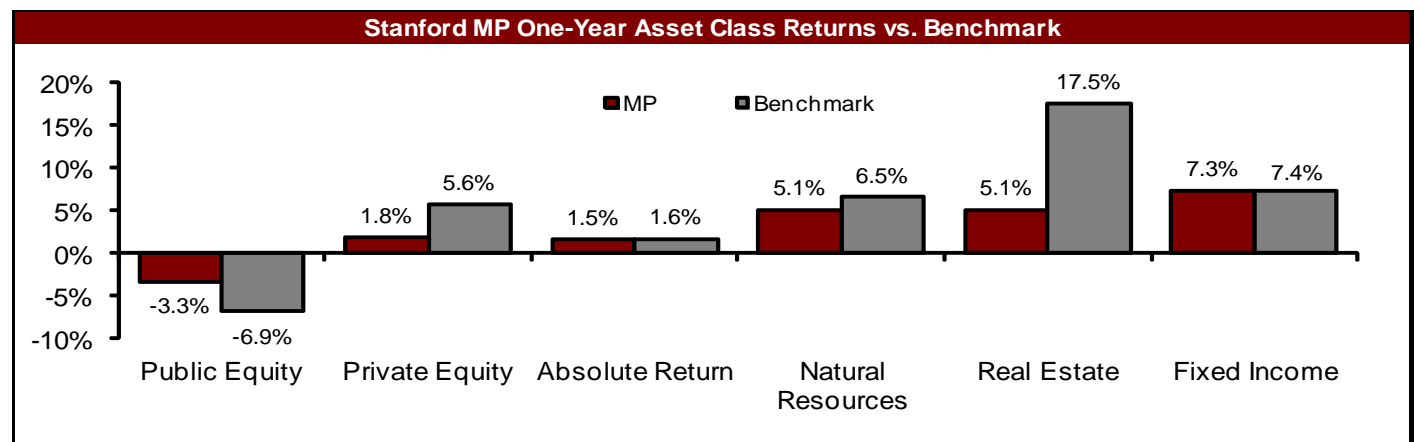
STANFORD MP VS. STANFORD COMPOSITE BENCHMARK & PASSIVE 60%EQUITY/40%BOND COMPOSITE



The relative one-year performance of the MP versus the benchmark was -1.9%.

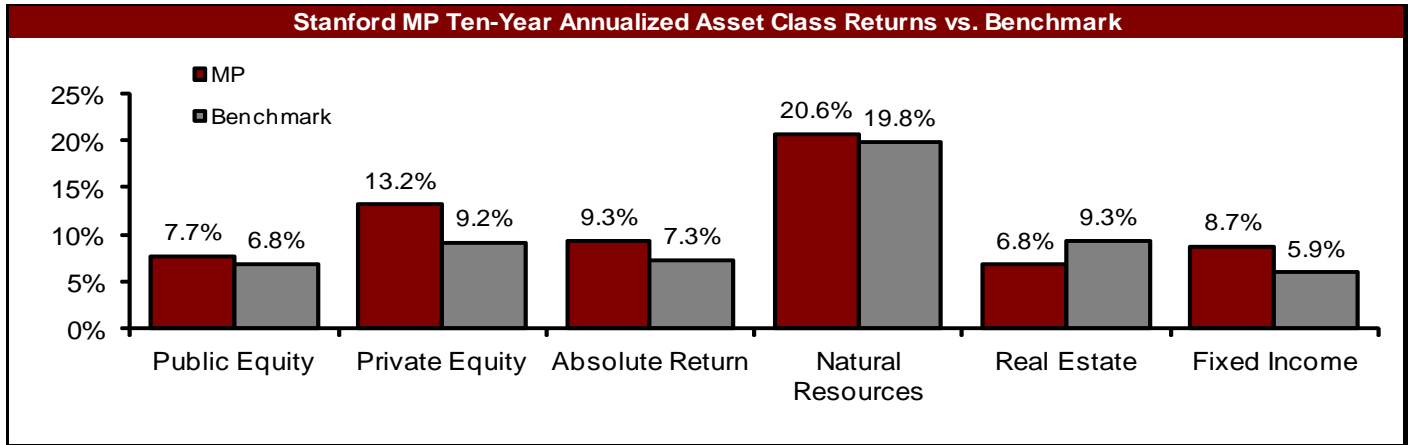
INDIVIDUAL ASSET CLASS PERFORMANCE The performance of individual asset classes for the 12 months ended June 30, 2012, relative to each asset class benchmark, is illustrated in the graph below:

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, 2012, the Merged Pool returns were 1.0%. During the same period, the MSCI ACWI Index returned -6.0%, the Barclays Aggregate returned 7.5%, and a 60/40 equity/fixed income mix would have returned -0.6%. We continue to exist in an environment where powerful drivers of financial asset returns are central bank actions. Even in this low interest rate environment, with its mix of excess liquidity and deleveraging we remain cautious. We believe there is a good chance for significant continued volatility (triggered by European banking crisis, China hard landing, or geopolitical flare-up), and have positioned the portfolio to preserve flexibility and optionality to respond with strength in a crisis.

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