



August 31, 2016 and 2015
Stanford University
Annual Financial Report





Central Energy Facility

The Central Energy Facility (CEF) includes three large water tanks for thermal energy storage, a high-voltage substation that receives electricity from the grid, and an innovative heat recovery system that takes advantage of Stanford's overlap in heating and cooling needs. Unlike the previous fossil-fuel-fired combined heat and power plant, the CEF is powered completely by electricity, which Stanford has committed to procure from renewable sources. In addition to the mechanical operations, the facility also includes administrative, classroom and meeting space that contribute to the educational component of the plant. As is true throughout the facility, these spaces also feature the latest in efficient design.

Photographs:

Courtesy ZGF Architects LLP; © Robert Canfield (top)

Linda A. Cicero / Stanford News Service (bottom)

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STANFORD UNIVERSITY ANNUAL FINANCIAL REPORT

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MANAGEMENT'S DISCUSSION AND ANALYSIS

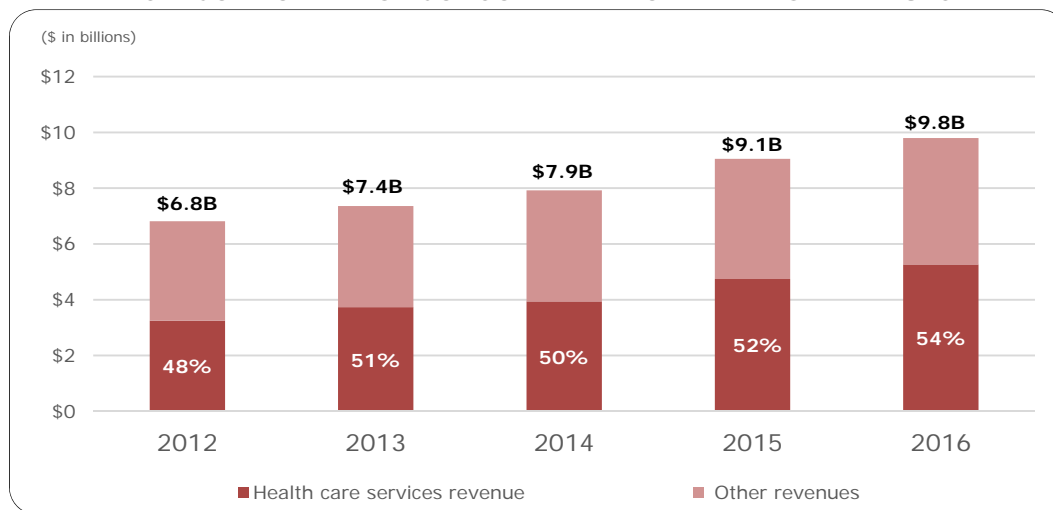
CONSOLIDATED FINANCIAL HIGHLIGHTS

Stanford's FY16 consolidated financial results reflect the combined financial position and results of the University, Stanford Health Care (SHC) and Lucile Salter Packard Children's Hospital at Stanford (LPCH), including their respective controlled affiliates. Operating revenues exceeded expenses by \$490 million, compared to \$700 million in FY15. Net assets increased \$1.4 billion to end the year at \$37.0 billion. Stanford achieved positive results through significant growth in health care services revenues, the generosity of its donors, and modest investment performance.

Investment performance. Consolidated investment returns in FY16 were \$1.3 billion. Stanford's investment returns in the Merged Pool (MP), the University's primary investment vehicle, were augmented by substantial growth in the value of income-generating properties on Stanford's lands. Total consolidated investments at August 31, 2016 were \$31.3 billion, compared to \$31.4 billion at August 31, 2015.

Significant growth in health care services revenues. Health care services represented approximately 54% of consolidated revenues in FY16, as shown in Figure 1. Health care services have been the fastest growing revenue component, with a five-year compound annual growth rate (CAGR) of approximately 13%. The partnership among Stanford's School of Medicine (SOM), SHC and LPCH (collectively known as Stanford Medicine) is synergistic. The SOM is a research intensive medical school that provides education, patient care, and interdisciplinary research. Stanford Medicine's tripartite mission is to promote fundamental, clinical, and translational discovery; train the medical leaders of tomorrow; and transform patient care. SHC and LPCH provide the settings where these clinical innovations are delivered to patients. See further discussion in the sections for *Stanford Health Care* and *Lucile Salter Packard Children's Hospital at Stanford*.

FIGURE 1
CONSOLIDATED HEALTH CARE SERVICES REVENUE
AS A COMPONENT OF CONSOLIDATED OPERATING REVENUES



Generous donor support. The University’s Office of Development reported gifts benefiting the University, SHC and LPCH of \$951 million. The dollars represent support from more than 81,000 donors including alumni, parents, friends, and others. This amount includes \$32 million and \$56 million in support of SHC and LPCH, respectively. These results are evidence of our donors’ ongoing commitment to Stanford and its mission.

In February 2016, the University announced the Knight-Hennessy Scholars Program, a graduate-level scholarship program to prepare a new generation of global leaders with the skills to address the increasingly complex challenges facing the world. Each year the program will identify a group of 100 high-achieving students from around the world with demonstrated leadership and civic commitment to receive full funding to pursue a wide-ranging graduate education at Stanford. With \$750 million in support, the Knight-Hennessy Scholars Program will be the largest fully endowed scholarship program in the world.

The sections below provide additional details about the University’s, SHC’s and LPCH’s financial position, financial results and operations.

UNIVERSITY

FY16 net assets increased 4% to \$31.7 billion compared to \$30.4 billion in the prior year. With the support of donors and modest investment performance, the University’s endowment grew by \$175 million after distributing \$1.1 billion for operations. The endowment ended the year at an all-time high of \$22.4 billion, exceeding last year’s \$22.2 billion.

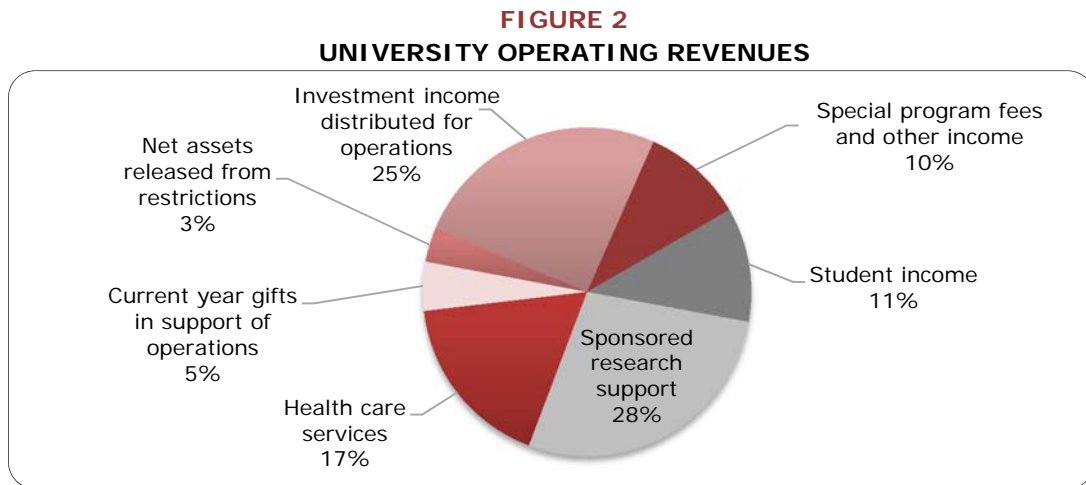
UNIVERSITY OPERATING RESULTS

The *Statements of Activities* include results from both operating and non-operating activities 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, research and other University priorities, including patient care.

The University ended the year with a surplus from operating activities of \$303 million. The results were essentially flat compared to the FY15 surplus of \$313 million. FY16 operating revenues increased \$260 million or 5%; operating expenses increased \$269 million or 6%. Non-operating activities are discussed in the *University Financial Position* section of this analysis.

UNIVERSITY OPERATING REVENUES

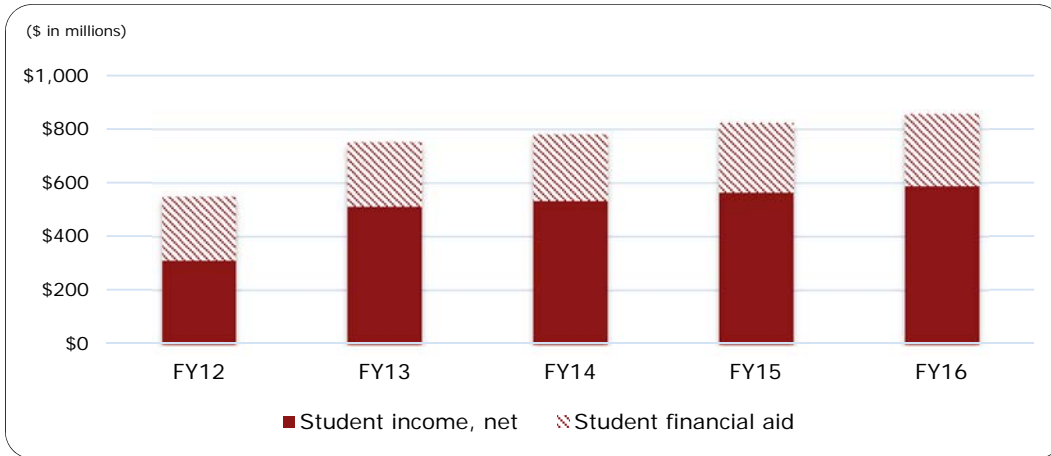
FY16 operating revenues of \$5.2 billion were derived from diverse sources, as shown in Figure 2.



Student Income

Total student income, which represents 11% of University operating revenues, increased 4% to \$587 million in FY16. Total student income includes tuition and fees from undergraduate and graduate programs and room and board; this amount is partially offset by financial aid consisting of assistance in the form of scholarship and fellowship grants that cover a portion of tuition, living and other costs.

FIGURE 3
UNIVERSITY STUDENT INCOME AND FINANCIAL AID



Student Tuition

Tuition revenue provides half of unrestricted funds which the University receives annually and supports many of the University's core academic and administrative functions, including the undergraduate financial aid program, faculty and staff salaries, student services and the purchase of materials for Stanford's two dozen libraries.

Revenues from student tuition and fees before the deduction for student financial aid increased by \$23 million in FY16 primarily as a result of undergraduate and graduate tuition rate increases of 3.5%.

Student Room and Board

Revenues from room and board increased 6% in FY16 due to an increase in room and board rates of 3.5%, an increase in room capacity from opening the new Ng House at Gerhard Casper Quad, and from Stanford's off-campus graduate housing program. The University continues to actively increase its capacity to house more students on campus.

Student Financial Aid and Other Graduate Support

One of the University's highest priorities is to remain affordable and accessible to the most talented students, regardless of their financial circumstances. The University's admission process for undergraduate students from the United States is need-blind, which means that students are admitted irrespective of their ability to pay; the University provides the financial aid necessary to make Stanford affordable to every admitted student. For international students, the University is need-aware: Stanford analyzes the need for aid and aims to meet the determined need.

Since 2000, the University has continued to enhance its financial aid programs for both its undergraduate and graduate students.

- Currently, families from the U.S. with incomes below \$125,000 pay no tuition, and those with incomes below \$65,000 pay no tuition, room or board. In FY16, approximately half of undergraduates were awarded need-based financial aid from Stanford.

- Graduate student financial aid and other support is awarded based on academic merit and the availability of aid. In the face of diminishing federal support, Stanford has assumed more of the financial weight of supporting its graduate students. In FY16, approximately 82% of graduate students received financial support.
- The Knight-Hennessy Scholars Program will be an additional source of graduate student support when its first cohort begins their studies in fall 2018. The program provides full funding for three years to enable graduate students to pursue advanced degrees and develop the capacity to lead and bring about positive changes in the world.

The University provides financial assistance to students in the form of scholarships, fellowships, and stipends, as well as teaching and research assistantships. Total Student Financial Aid and Other Graduate Support for FY16 and FY15 is as follows (in millions of dollars):

| <i>(\$ in millions)</i> | FY16 | FY15 |
|---|----------------------|----------------------|
| Student Financial Aid | | |
| Undergraduate | \$ 163 | \$ 156 |
| Graduate | 107 | 105 |
| Total Student Financial Aid | <u>270</u> | <u>261</u> |
| Other Graduate Support | | |
| Stipends | 97 | 90 |
| Assistantships (research and teaching) | 103 | 95 |
| Allowance for tuition (for assistantship recipients) | 82 | 76 |
| Total Other Graduate Support | <u>282</u> | <u>261</u> |
| Total Student Financial Aid and Other Graduate Support | <u>\$ 552</u> | <u>\$ 522</u> |

FY16 undergraduate aid and graduate fellowships of \$270 million represent an increase of 3% over the prior year and is included in Student Financial Aid in the *Consolidated Financial Statements*. For FY16, the University also provided other graduate student support in the form of stipends of \$97 million (included in other operating expenses), and teaching and research assistantships and related allowances for tuition of \$185 million (included in salaries and benefits expense).

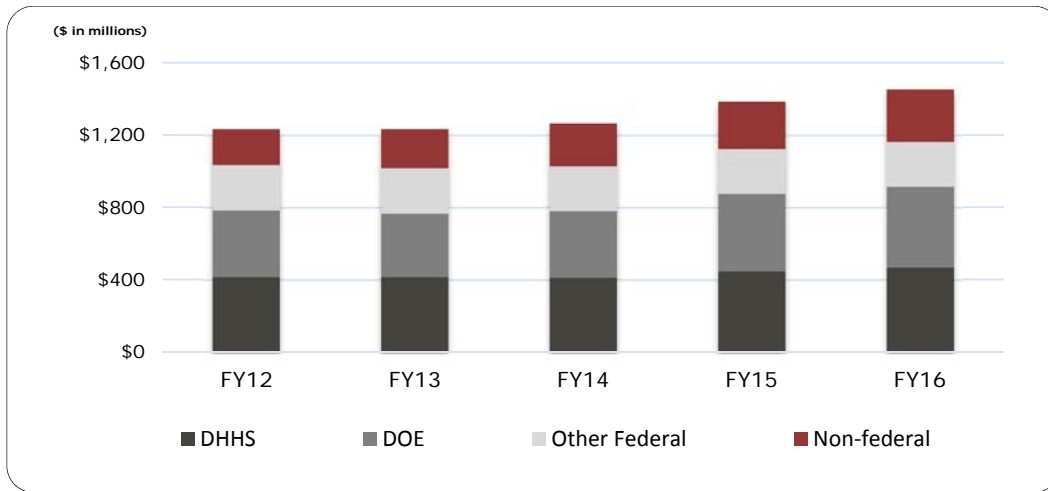
During FY16, sources of the total \$552 million of student financial aid and graduate support included approximately \$250 million in payout from restricted endowment funds, \$200 million from unrestricted University funds and approximately \$100 million from grants and contracts.

Sponsored Research Support

FY16 sponsored research support increased to \$1.5 billion, nearly 5% over FY15. Sponsored research support represents 28% of the University's operating revenues, the highest source of operating revenue for the University.

In addition to payment for the direct costs of performing research, the University receives an amount from sponsors for facilities and administrative costs, known as indirect costs. For FY16, the federal and non-federal indirect cost recovery increased by 4% to \$251 million.

FIGURE 4
UNIVERSITY SPONSORED RESEARCH SUPPORT



Approximately 80% of the University’s sponsored research support (including support for the SLAC National Accelerator Laboratory—“SLAC”) is received directly or indirectly from the federal government (See Figure 4). The largest federal sponsor, the Department of Health and Human Services (DHHS), provided support of \$468 million in FY16 compared to \$447 million in the prior year, primarily through the National Institutes of Health. Most of these funds support research within the University’s SOM.

In FY16, sponsored research support for SLAC was \$448 million, up 4% from FY15. The U.S. Department of Energy (DOE) provided substantially all of this support, consisting of funding for ongoing research operations and construction of new facilities or instruments. In FY16, SLAC received \$162 million for several construction projects, including \$135 million for the Linac Coherent Light Source (LCLS) II project expected to be completed in 2021. LCLS II is a major upgrade to increase the power and capacity of LCLS, the revolutionary X-ray free-electron laser that first became operational in October 2009.

Health Care Services

FY16 health care services revenue represented 17% of University operating revenues, increasing \$66 million (8%) to \$906 million. This increase primarily reflects increased services at higher rates performed by the University’s physicians for SHC and LPCH. SHC and the SOM revised their inter-entity agreement in June 2015.

SOM faculty serve as physicians for the Hospitals. Clinical services are billed and collected by the Hospitals, and a portion is remitted to the University as payment for these physician services. In addition, the Hospitals pay the University for other essential services such as medical direction, and various infrastructure and administrative services. Health care services revenues of \$874 million represent the net value of services provided between the University and the Hospitals; these amounts are eliminated in consolidation. The remaining \$33 million in health care services revenue is for services provided to other health care systems, primarily the VA Palo Alto Health Care System and Santa Clara Valley Medical Center.

The results of operations and financial position for SHC and LPCH are discussed in more detail in the *Stanford Health Care* and *Lucile Salter Packard Children’s Hospital at Stanford* sections.

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

Current year gifts in support of operations increased 7% to \$251 million in FY16. Net assets released from restrictions, which consisted primarily of pledge payments and gifts released from donor restrictions, increased 11% to \$175 million.

Total Investment Income Distributed for Operations

The University distributes investment income for use in operations according to policies approved by the Board of Trustees (Board). Total investment income distributed for operations represented 25% of University operating revenues in FY16, the second highest source of operating revenues for the University.

To the extent that current year returns do not adequately cover the Board approved payout, prior year earnings are used to support payout. This approach enables the University to provide a consistent payout to support operations. See the separate section, *The University's Endowment*.

Endowment income distributed for operations increased 7% to \$1.1 billion in FY16. This includes payout from the University's MP based on a Board approved formula, and income received from real estate and other investments not included in the MP. The endowment payout as a percentage of the beginning endowment value was 5.1% for FY16 and 4.9% for FY15.

Expendable funds pool and other investment income distributed for operations was \$190 million in FY16, compared to \$218 million in FY15. 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.

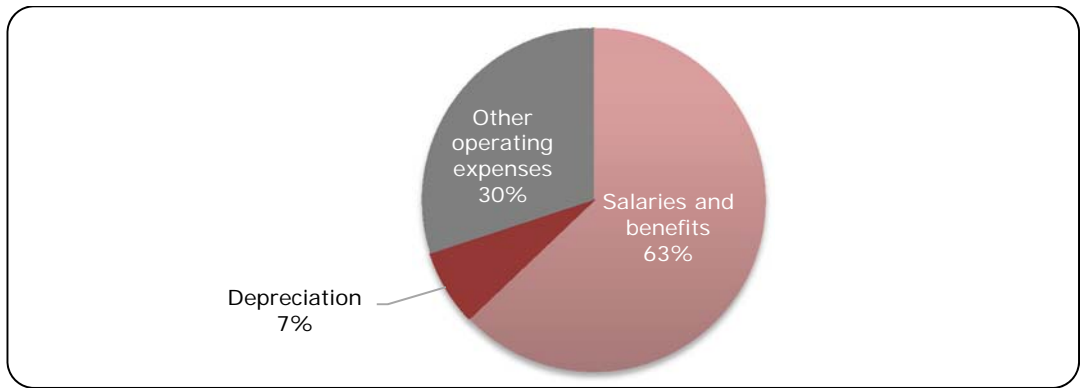
The EFP policy provides a variable payout to certain funds that support operations based on the prior year's investment returns. See *Note 7* to the *FY16 Consolidated Financial Statements*.

The EIFP holds previously distributed but unspent endowment payout. These amounts are held, for instance, until there is adequate funding to support a program, scholarship or professorship. These amounts are invested in highly liquid instruments in order to preserve the principal balance. Earnings on these investments are fully distributed to the fund holders. See *Note 7* to the *FY16 Consolidated Financial Statements*.

UNIVERSITY OPERATING EXPENSES

Total expenses increased \$269 million, or 6%, to \$4.9 billion in FY16. As shown in Figure 5, salaries and benefits comprised 63% of the University's total expenses; depreciation expense was 7% and other operating expenses represented 30%.

FIGURE 5
UNIVERSITY OPERATING EXPENSES



Salaries and benefits increased 9% in FY16 to \$3.1 billion. The increase resulted from a combination of factors including additional headcount to support new programs and sponsored research activities, particularly within the SOM, salary programs designed to maintain Stanford's competitive position, and higher benefit costs.

Depreciation expense increased by 3% to \$346 million in FY16 from \$335 million in FY15. The increase resulted from buildings recently placed in service as described in the *Capital Projects* section below.

Other operating expenses increased slightly by 1% to \$1.5 billion in FY16. Increases in expenses for sponsored research support and off-campus housing leases were offset by reduced expenses from the sale of the Stanford Blood Center.

UNIVERSITY FINANCIAL POSITION

Total University assets increased \$1.6 billion in FY16 to end the year at \$37.8 billion. Total University liabilities increased from \$5.8 billion to \$6.0 billion.

Cash and Assets Limited as to Use

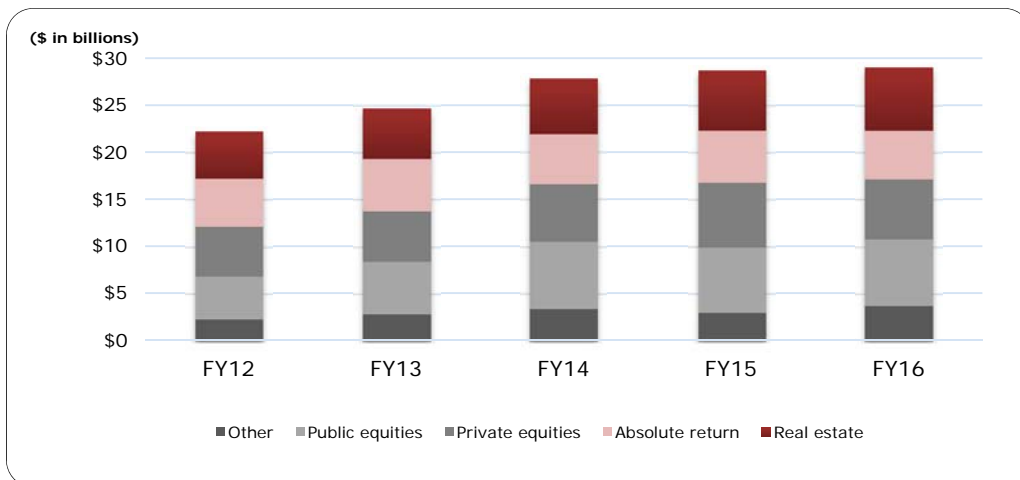
The University regularly monitors liquidity required to meet its operating needs and other contractual commitments. At the same time, the University strives to optimize the long-term total return while maintaining an appropriate level of risk of its available funds. At August 31, 2016, the University's cash and cash equivalents was \$640 million, a decrease of \$68 million compared to the prior year. In addition to cash and cash equivalents, there was \$985 million in cash and cash equivalents in the University's investments. See *Note 6* to the FY16 *Consolidated Financial Statements*.

Assets limited as to use nearly doubled to \$316 million primarily due to \$250 million in proceeds from the issuance of CEFA Series U-7 tax-exempt bonds, less spending on eligible capital projects during the year.

Investments

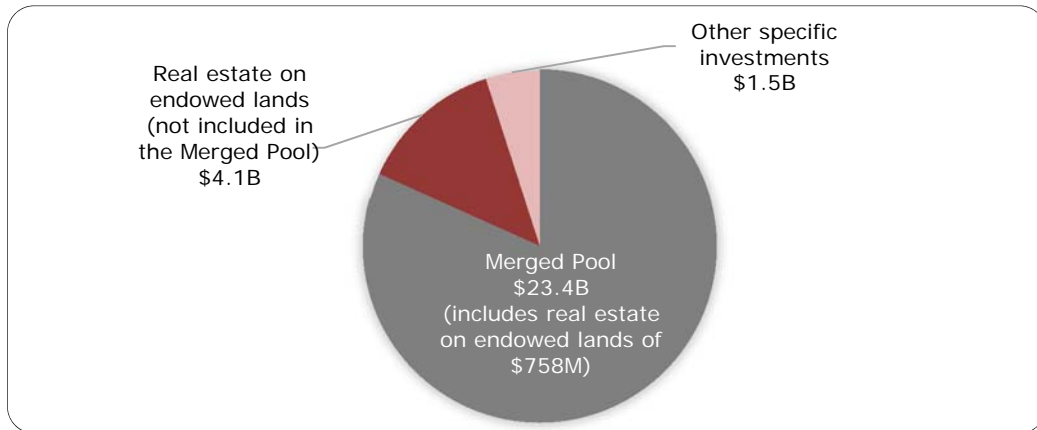
University investments at August 31, 2016 were \$29.1 billion. Investments by asset class are shown in Figure 6.

**FIGURE 6
UNIVERSITY INVESTMENTS BY ASSET CLASS**



There are three primary categories of investments as shown in Figure 7: the MP, real estate investments on endowed lands, and other specific investments.

FIGURE 7
UNIVERSITY INVESTMENTS BY CATEGORY



\$23.4 billion of the University's investments was held in the MP at August 31, 2016. The majority of the University's endowment assets are managed through the MP, a diversified portfolio of actively managed public and private equity, absolute return, natural resources and real estate assets. The portfolio is designed to optimize long-term returns, create consistent annual payouts to support the University's operations and preserve purchasing power for future generations of Stanford faculty and students. The MP is managed by the Stanford Management Company (SMC), a division of the University with oversight by a Board of Directors appointed by the University Board of Trustees.

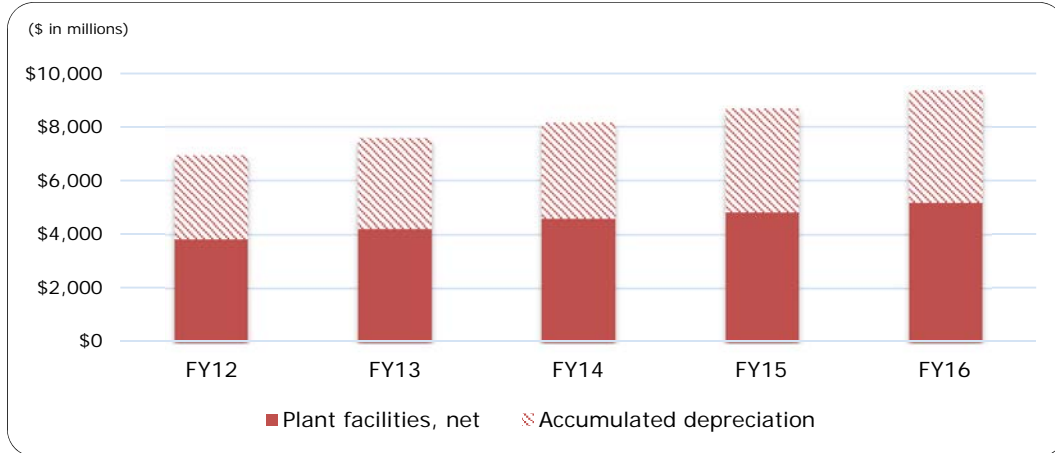
A portion of Stanford's 8,200 acres of endowed lands, including the Stanford Research Park, is designated for the production of income by the Board. As of August 31, 2016, most of Stanford's \$4.9 billion of real estate investments (including \$758 million in the MP as discussed above) are located on these lands. In FY16, these properties generated \$119 million in income, net of expenses, and appreciated in value by \$385 million. These lands have been developed for various uses, including research, medical and commercial offices, hotels, retail properties and a regional mall. The University further diversifies this portfolio by employing a variety of structures, including ground leases, direct leases and participation arrangements. In recent years, the value of these properties has benefited from strong dynamics in the regional market including rising investor demand for real estate; high office, hotel and apartment occupancy rates; increased office rents; and strong retail sales. Decreases in the capitalization and discount rates have also contributed to the positive results.

The remaining \$1.5 billion of investments are specifically invested for a variety of purposes, in accordance with donor wishes.

Capital Projects

The University continues to invest heavily in its physical facilities to support key academic initiatives, housing and infrastructure, including environmental sustainability. During FY16, the University invested \$706 million in capital projects, bringing gross plant facilities before accumulated depreciation to \$9.3 billion. Plant facilities, net of accumulated depreciation, increased \$373 million to \$5.2 billion, as shown in Figure 8.

FIGURE 8
Plant Facilities and Accumulated Depreciation



In recent years, the University’s need for housing has outpaced its ability to provide new residences on university-owned land. During FY16, the University completed construction of the new Ng House at Gerhard Casper Quad and two new residences in Lagunita Court, providing more on-campus housing to its undergraduate population. During the year, Stanford also completed construction of the Graduate School of Business (GSB)’s Highland Hall residences, enabling the GSB to offer on-campus housing to nearly all first-year MBA students. Several additional housing initiatives are in the planning phases to address the student, faculty and staff housing constraints on or near campus.

Construction continued on the Anne T. and Robert M. Bass Biology Building, a new laboratory research facility designed to support the University’s biochemistry and computational research initiative. In the fall of 2016, the Sapp Center for Science Teaching and Learning opened in the historic Old Chem building. As a center for undergraduate education and anchor for the future Biology Chemistry Quad, the Sapp Center will launch a new era for interdisciplinary science education and research at Stanford by encouraging collaboration across various disciplines, and among students, faculty and staff.

Stanford’s plan for an off-site administrative campus in Redwood City is moving forward. Phase 1 of the Stanford in Redwood City project is expected to be completed in 2019, when select administrative staff will relocate to this site in order to make additional core campus space available for the University’s academic priorities.

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, real estate investment projects, faculty and staff mortgage loans and other infrastructure projects.

The University is not an obligor or guarantor with respect to any debt obligations of SHC or LPCH, nor are SHC or LPCH obligors or guarantors with respect to debt obligations of the University, or each other.

During FY16, the University issued \$250 million in tax-exempt debt (\$170 million principal plus bond premium of \$80 million) to finance various facilities and infrastructure and to achieve long-term savings in interest costs. The debt was issued with a yield to maturity of 2.71% and matures in 2046. In addition, the University entered into a second \$250 million unsecured revolving credit facility in August 2016, bringing the total unsecured revolving credit facilities to \$500 million. As of August 31, 2016, the University has drawn down \$66 million.

Total debt increased \$251 million to \$3.3 billion as of August 31, 2016. During FY16, 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.

Net Assets

The University's net assets are classified as unrestricted, temporarily restricted or permanently restricted. See *Note 1* to the *Consolidated Financial Statements*. As previously noted, FY16 net assets increased 4% to \$31.7 billion compared to \$30.4 billion in the prior year. The increase of \$1.3 billion resulted from operating income of \$303 million and gifts and pledges of \$1.0 billion not included in operating income. A substantial portion of gifts and pledges was received in support of the Knight-Hennessy Scholars Program as previously discussed. Investment income distributed for operations of \$1.3 billion exceeded investment returns of \$1.2 billion, which reduced net assets by \$132 million.

THE UNIVERSITY'S ENDOWMENT

The University's endowment is a collection of gift funds and reserves which is invested to generate income to support the University's teaching and research missions.

The University's endowment is crucial to providing funding for its academic program activities, ensuring affordability for its students and enabling the University to increase the amount spent on student financial aid. At August 31, 2016, the endowment totaled \$22.4 billion (See Figure 9) and represented approximately 71% of the University's net assets. The endowment, which includes the University's endowed lands, is comprised of pure endowment funds, term endowment funds and funds functioning as endowment.

FIGURE 9
UNIVERSITY ENDOWMENT

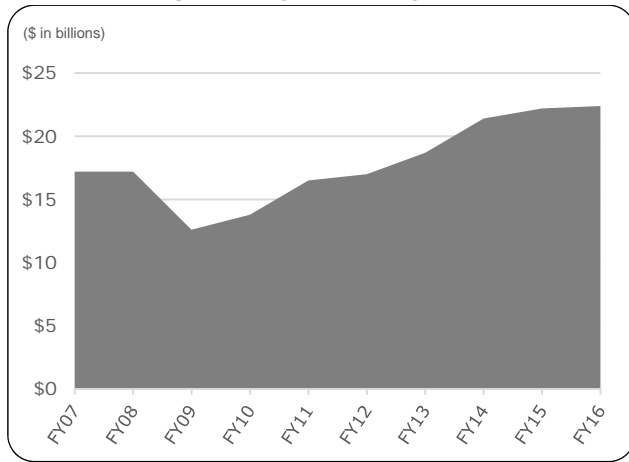
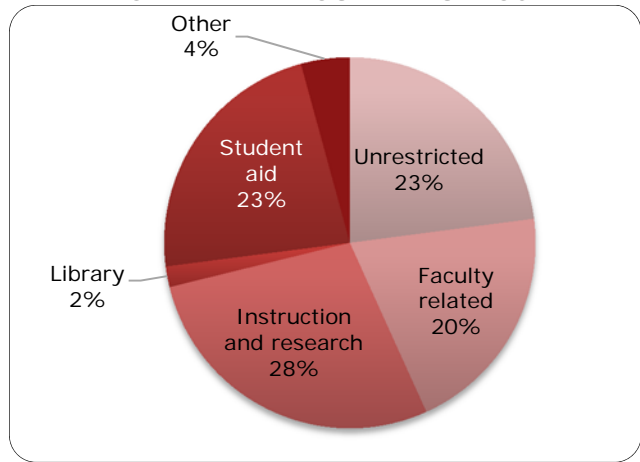


FIGURE 10
ENDOWMENT PAYOUT BY PURPOSE



Through a combination of investment strategy and payout policy, the University strives to provide a reasonably consistent payout from endowment to support operations, while preserving the purchasing power of the endowment, adjusted for cost inflation, so that the endowment can continue to support the University in perpetuity.

The Board is responsible for setting the payout rate, and continuously evaluating the payout policy to ensure that the endowment can meet the current and future needs of the University. The current Board approved targeted payout rate is 5.5%. Over time, the Board believes this payout rate maximizes the endowment's benefit to our current students and faculty while preserving intergenerational equity – the concept that payout from an endowment fund should remain constant over time, adjusted for inflation, in order to provide for future operations.

Annual payout to operations from the endowment continues to be a significant source of operating revenue for the University, covering approximately 23% of expenses in FY16. In FY16, the endowment payout to operations of \$1.1 billion exceeded the investment returns on endowment of \$930 million. Despite this, gifts and pledge payments and other funds invested in the endowment helped to increase the endowment slightly to \$22.4 billion in FY16.

The University's endowment provides funding annually for a wide variety of important purposes. As shown in Figure 10, a significant portion of the endowment payout (approximately 80%) is restricted as to purpose, and provided funding for instruction and research activities (28%), student aid (23%), and faculty salaries and support (20%), with the remaining amount providing support for the University's libraries and other purposes.

HOSPITALS

The financial results and financial position of Stanford Health Care (SHC) and Lucile Salter Packard Children's Hospital at Stanford (LPCH) and their controlled affiliates, are included in the FY16 *Consolidated Financial Statements*. The University is the sole member of both SHC and LPCH. The University's School of Medicine (SOM) and its clinical faculty, together with SHC and LPCH, constitute and are known in the marketplace as Stanford Medicine.

In FY11, SHC and LPCH received local government approval to rebuild and expand their principal facilities. Construction is projected to be completed in 2017 for LPCH and 2018 for SHC. These improvements will assure that SHC and LPCH have additional inpatient capacity in modern, technologically-advanced and patient-centered facilities, and meet state-mandated earthquake safety standards. The total estimated cost, inclusive of contingencies, is approximately \$2.0 billion for SHC. The cost of LPCH's project is expected to exceed its originally estimated amount of \$1.2 billion because of cost increases related to changes in technology, change orders, and market availability of subcontractors, among other factors. LPCH management believes that sources of funding are adequate to cover remaining costs.

To improve and expand their services, the Hospitals have established community-based ambulatory clinic organizations—SHC's University HealthCare Alliance (UHA) and LPCH's Packard Children's Health Alliance (PCHA)—that support Stanford Medicine's mission to deliver quality care to the community and conduct research and education. Working collaboratively with their respective hospitals and the SOM faculty, these organizations have acquired multi-specialty practices to form a network of coordinated care throughout the Bay Area.

SHC and LPCH continue to participate in the California Hospital Quality Assurance Fee (QAF) Program and the Hospital Fee Program. These programs are designed to provide supplemental payments to certain hospitals and support the State's effort to maintain health care coverage for children.

The discussion below provides additional detail about SHC's and LPCH's consolidated operations and financial results as derived from their separate consolidated financial statements.

STANFORD HEALTH CARE

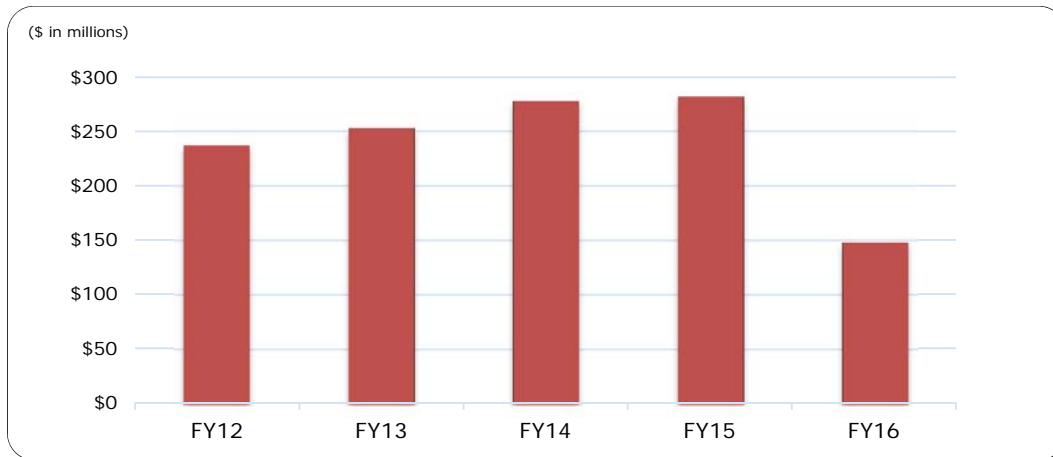
Stanford Health Care ("SHC") experienced positive financial results in FY16. SHC's FY16 financial results benefited from its operating performance and fundraising.

The consolidated results reflect the combined results of SHC and its subsidiaries (see *Note 1* to SHC's separately issued *Consolidated Financial Statements*).

SHC FINANCIAL HIGHLIGHTS

Net assets decreased \$6 million to end the year at \$3.1 billion. Operating revenues exceeded operating expenses by \$148 million, compared to \$282 million in FY15. As shown in Figure 11, the change in net assets from operating activities ("operating margin") declined as compared to prior years, primarily due to cost increases incurred to further grow and expand SHC's network of care.

FIGURE 11
SHC OPERATING MARGIN



SHC OPERATING RESULTS

SHC's *Consolidated Statements of Operations and Changes in Net Assets* include results from both operating and non-operating changes in the net assets of SHC. Operating activities include the revenues earned and expenses incurred in the current year to support patient care. FY16 operating revenues increased 15% compared to an increase in operating expenses of 20% during the same period. Expenses grew more than revenues mainly due to the inter-entity agreement with the SOM needed to recruit and retain physicians to provide high quality patient care and support SHC's continued growth. Additional expenses were also incurred for the Stanford Cancer Center South Bay, SHC's first off-campus outpatient clinic for the diagnosis and treatment of cancer, primary care clinics and affiliation with ValleyCare. In addition, SHC has increased its marketing of two new plans: SHC Advantage, a Medicare health plan offered to Santa Clara County residents, and increased membership in SHC Alliance, a benefit plan that allows University employees access to the Stanford network of care.

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

SHC OPERATING REVENUES

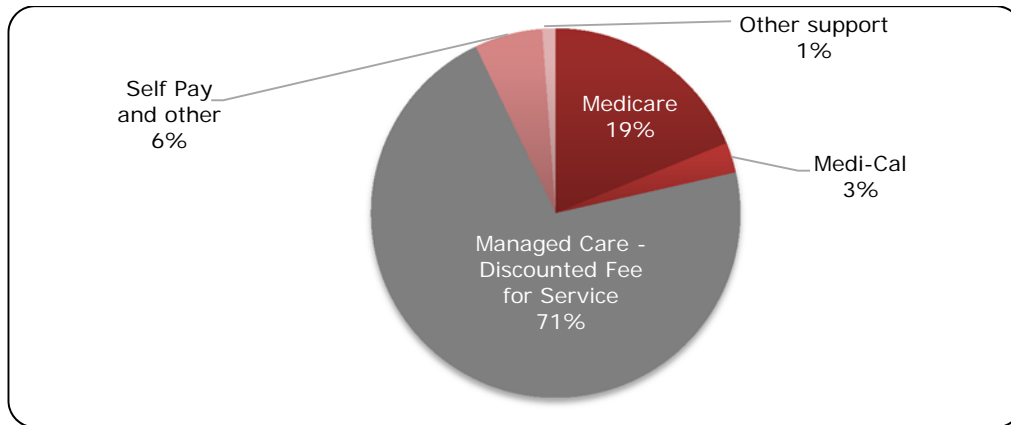
FY16 operating revenues were \$4.1 billion, a 15% increase over FY15.

Health Care Services Revenue

FY16 health care services revenue (including capitation/premium revenue) less doubtful accounts increased \$509 million, or 15%, from FY15 to \$4.0 billion and represented 97% of operating revenues.

Patient care revenue consists of revenue from patient and third-party payers and comprises nearly all of SHC's health care services revenue. Patient care revenue by major payer, net of contractual allowances (but before provision for doubtful accounts), is shown in Figure 12.

FIGURE 12
SHC PATIENT CARE REVENUE



Inpatient and outpatient, which represented 44% and 56% of net patient revenues (including capitation / premium revenue), respectively, grew significantly due to strong volume growth in multiple areas, such as operating rooms, emergency department, pharmacy, cath angio, imaging, clinical labs and other ambulatory care services.

Other Operating Revenues

Other operating revenues, which include revenues from various related entities and outreach clinical activities, increased 25% to \$123 million.

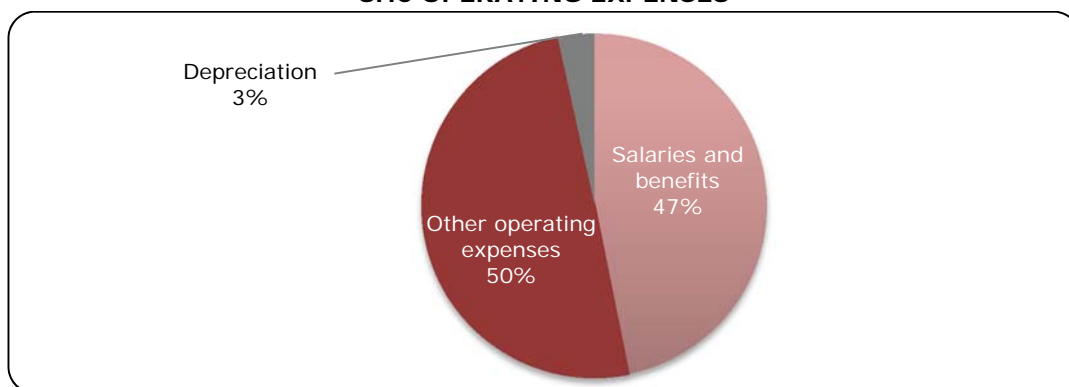
Net Assets Released from Restrictions

Net assets released from restrictions for use in operations was \$9.4 million in FY16 compared to \$15.7 million in FY15 due to lower restricted gift spending.

SHC OPERATING EXPENSES

Total expenses increased \$661 million, or 20.1%, to \$3.9 billion in FY16, which was primarily due to increased headcount, physician services, the affiliation with ValleyCare in May 2015, and acquisition of the Stanford Blood Center from the University in September 2015.

FIGURE 13
SHC OPERATING EXPENSES



As shown in Figure 13, salaries and benefits comprised 47% of SHC's total expenses, depreciation expense was 3%, and all other operating expenses represented 50%.

- Salaries and benefits increased 30% in FY16 to \$1.9 billion. The increase primarily resulted from expanded headcount to support current growth in patient volumes and for future expansion (see the *Capital Projects* section below), the acquisition of the Stanford Blood Center from the University, partial insourcing of information technology services, annual salary increases designed to maintain SHC's position in the competitive market for healthcare professionals and higher benefit costs.
- Depreciation expense increased by 24% to \$136 million in FY16 from \$110 million in FY15. The increase resulted from buildings and equipment recently placed in service, such as the Stanford Neuroscience Health Center, and a full year of service for the Stanford Cancer Center South Bay, Central Steam Plant, and Beaker Integrated Laboratory System.
- Other operating expenses increased by 12% to \$2.0 billion for FY16. The majority of this increase is purchased services related to payments to the University under a revised inter-entity agreement for clinical services provided by the SOM to provide high quality patient care and support continuous growth, and from growth in additional physicians joining the UHA network. In addition, supplies expense increased by 10% to \$531 million in response to patient volume growth and inflation.

SHC FINANCIAL POSITION

SHC's *Consolidated Statements of Financial Position* reflect strong operating results and positive investment returns. Total SHC assets increased \$239 million in FY16 to end the year at \$5.8 billion and total SHC liabilities increased from \$2.5 billion in FY15 to \$2.7 billion in FY16. As a result, net assets at the end of the year remained essentially unchanged from the previous year end.

Unrestricted Cash and Investments

Unrestricted cash and investments increased to \$2.1 billion in FY16 from \$2.0 billion at the end of FY15.

Capital Projects

SHC continues to invest in facilities and systems required to remain at the forefront of medicine and to be the provider of choice for complex and network care in the communities it serves. During FY16, SHC invested \$620 million in capital projects, bringing property and equipment, net of accumulated depreciation, to \$2.4 billion, a \$478 million increase from FY15.

The majority of the FY16 spending was for the New Stanford Hospital (to meet State-mandated earthquake safety standards, and provide modern, technologically-advanced hospital facilities), the Stanford Neuroscience Health Center (a five-story, 92,000 square foot facility on the Hoover Medical Campus which will provide comprehensive outpatient neurology, imaging, and neurosurgery services to the community) and the Stanford Health Center in Emeryville (a four-story, 80,000 square foot facility for multi-specialty clinics focused on cardio-vascular care).

Debt

Total debt, including current portions, was \$1.5 billion as of August 31, 2016.

A combination of fixed and variable rate debt, of varying maturities, is used to fund SHC's mission. Tax-exempt bonds with fixed interest rates account for 71% of the total, while the remaining 29% have variable rates.

In September and October, 2016, Standard & Poor's, Moody's Investor Service and Fitch Ratings affirmed their previous long-term ratings at AA-/Aa3/AA, respectively.

Net Assets

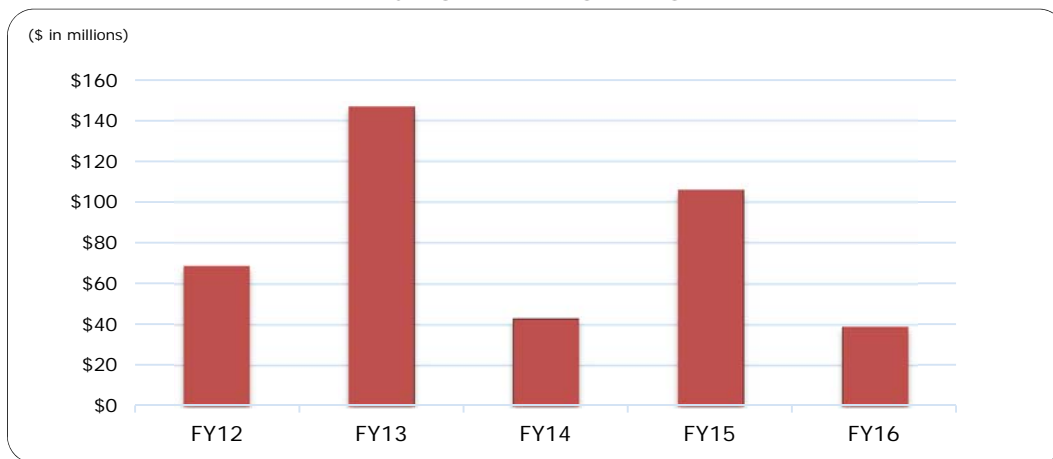
SHC's net assets are classified as unrestricted, temporarily restricted or permanently restricted. See *Note 1* to the *Consolidated Financial Statements*. As previously noted, FY16 net assets were essentially unchanged, ending the year at \$3.1 billion. SHC's operating surplus of \$148 million, plus an increase of \$38 million on investments (majority from the University MP), was offset by a decrease of \$116 million on swap valuations. Temporarily restricted net assets increased by \$15 million to \$577 million in large part due to fundraising commitments for the New Stanford Hospital, while permanently restricted net assets increased modestly by \$200 thousand in contributions. These mostly positive changes were offset by transfers to the University of \$31 million for the sale of the Stanford Blood Center and \$45 million for transfers under the inter-entity agreement with the SOM.

LUCILE SALTER PACKARD CHILDREN'S HOSPITAL AT STANFORD

LPCH FY16 FINANCIAL HIGHLIGHTS

Net assets at August 31, 2016 were \$2.2 billion, reflecting an increase of \$157 million over FY15. Operating revenues exceeded operating expenses by \$39 million in FY16, compared to \$106 million in FY15. FY16 operating results experienced pressure due to an increase of 7% in operating expenses as compared to FY15 primarily related to higher personnel costs and physician payments to the University's School of Medicine (SOM) as well as the opening of new outpatient facilities in Sunnyvale and Los Gatos. Figure 14 shows the change in net assets from operating activities ("operating margin") in the past five years.

FIGURE 14
LPCH OPERATING MARGIN



LPCH OPERATING RESULTS

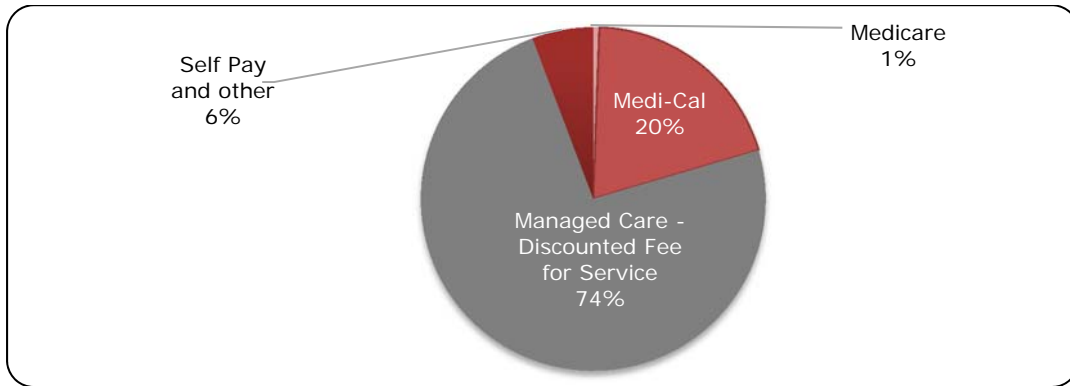
Income from operations was \$39 million in FY16, as compared to \$106 million in FY15.

LPCH OPERATING REVENUES

FY16 operating revenues increased \$22 million, or 2%, compared to the prior year. Patient care revenue increased \$9 million from the prior year, mainly due to increased reimbursement from commercial managed care payers, and an increase in outpatient visits. This increase was partially offset by a decrease in the California Hospital Quality Assurance Fee (QAF) Program and Hospital Fee program revenues from \$80 million in FY15 to \$52 million in FY16. These programs are designed to provide supplemental payments to certain hospitals and support the State's effort to maintain health care coverage for children.

Patient care revenue by major payer, net of contractual allowances (but before provision for doubtful accounts), is shown in Figure 15.

FIGURE 15
LPCH PATIENT CARE REVENUE

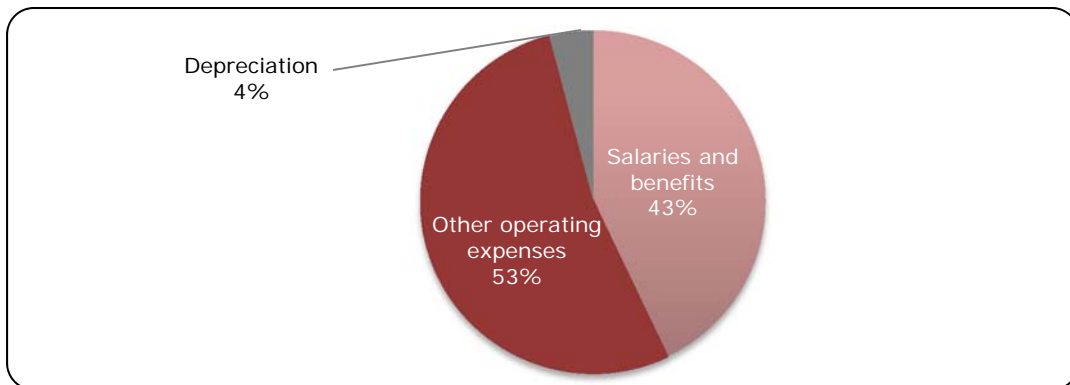


LPCH's community benefits, including services to patients under Medi-Cal and other publicly sponsored programs that reimburse at amounts less than the cost of services, were \$214 million in FY16 compared with \$222 million in FY15. These amounts also include investments LPCH makes in improving the health of children through a range of community-based programs.

LPCH OPERATING EXPENSES

Operating expenses increased \$90 million, or 7%, compared to the prior year. This increase was mainly attributable to the increase in salaries and benefits as LPCH ramps up and prepares for the launch of the new hospital in 2017. In addition, LPCH experienced increases in payments to the SOM for services provided by the physician faculty, and higher costs resulting from the usage of prosthetics and surgical supplies. New center openings in Sunnyvale and Los Gatos also contributed to one-time costs in FY16. The increases were partially offset by a decrease of \$19 million in the expense recorded from the QAF and Hospital Fee programs compared to the prior year.

FIGURE 16
LPCH OPERATING EXPENSES



As shown in Figure 16, salaries and benefits comprised 43% of LPCH's total expenses, depreciation expense was 4%, and all other operating expenses represented 53%.

LPCH FINANCIAL POSITION

Statement of Financial Position

Total assets increased by \$286 million, or 10%, driven by a combination of cash generated from operations, proceeds from the 2016 Series B Bonds and continued support from the donor community. These cash flows, combined with planned withdrawals from the Merged Pool, were used to fund the ongoing construction of the new hospital expansion. As a result, fixed assets increased \$351 million to \$1.4 billion as of August 31, 2016.

Total liabilities increased by \$129 million, or 16%, primarily due to the issuance of the 2016 Series B Bonds referenced above.

Unrestricted Cash and Investments

Unrestricted cash and investments decreased by \$55 million, or 7%, mainly due to funding for the ongoing construction of the Renewal Project.

Capital Projects

LPCH's *Statement of Financial Position* reflects significant investments in the facilities and systems required to continue to provide the highest quality children's hospital services to the community it serves. The majority of the FY16 spending was for LPCH's portion of the Renewal Project, which represented \$401 million of the increase in property and equipment.

During the year, LPCH also completed construction on two ambulatory buildings purchased in FY14 in Sunnyvale and Los Gatos, California. Both locations are currently being used for outpatient pediatric specialty services.

Debt

Total debt, including the current portion, increased by \$109 million, or 19% from the prior year. In March 2016, California Health Facilities Financing Authority issued, on behalf of LPCH, two series of revenue bonds in the aggregate par amount of \$177 million. Proceeds of the Series A bonds were used for the legal defeasance and redemption of the 2008 bonds. The proceeds of the Series B bonds were used to finance a portion of the Renewal Project, and to pay for the cost of issuance.

During FY16, S&P, Fitch and Moody's assigned ratings on the new debt of AA-, AA and Aa3, respectively. In addition, the ratings agencies affirmed their previous ratings on the existing debt with no changes in outlook.

Net Assets

Total net assets increased by \$157 million, or 8%, from August 31, 2015 to August 31, 2016, representing income from operations and restricted contributions, as offset by funding its portion of certain projects at the SOM and SHC through equity transfers.

LOOKING FORWARD

Stanford's financial position remains strong. The University's endowment is at an all-time high at the end of the fiscal year. Our donors and alumni continue to embrace Stanford's mission through their generous support of time, talent and financial resources—and this is reflected in our FY16 results. The growth in Stanford's physical infrastructure continues to support the advancement in our academic programs, investment in our students and evolving health care services.

The University begins FY17 under the leadership of a new president, Marc Tessier-Lavigne, who inherits a solid foundation from his predecessor, John Hennessy. Currently, interdisciplinary research and education programs are flourishing and focused on addressing global challenges; the undergraduate curriculum has

been redesigned; and the arts and humanities are enjoying renewed appreciation and focus. During President Hennessy's tenure, the academic campus and physical infrastructure were transformed to support new ways of learning and working while conserving natural resources and reducing energy consumption.

Health care service revenues have grown significantly in recent years and Stanford Medicine is well poised to continue on this current growth trajectory. Stanford's history of innovation is reflected in Stanford Medicine's vision of delivering proactive, preemptive and preventive health care. Stanford has created the infrastructure to deliver this vision. Both SHC and LPCH have established a strong local presence in a number of important markets. The new SHC and LPCH hospitals are on track to deliver state of the art facilities to provide exceptional patient care in the next few years. Through precision health, Stanford Medicine is within reach to change the very nature of health care to one of personalized care focused on keeping people healthy, with an emphasis on prediction and prevention as well as precise diagnosis and treatment

The current environment is not without its challenges. Pressure continues on a number of Stanford's most significant revenue sources, including tuition, federal sponsored research and health care services. Weak investment returns are limiting the growth of endowment payout. Bay Area housing costs continue to be one of Stanford's greatest hurdles in recruiting faculty and staff.

Despite these challenges, Stanford is well positioned to face the future, to educate leaders of tomorrow and to help solve the world's global issues. These challenges require us to invest selectively in high priority initiatives and to focus on identifying and implementing efficiencies. Stanford continues to foster interdisciplinary research, identify new funding sources for research and discover new ways and venues for delivering education and patient care. Applying the knowledge gained through research to solve real world problems will be a cornerstone of our future. Encouraged and inspired by the tremendous support of our donors, alumni, faculty, and staff, Stanford faces the future with cautious optimism.



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



David Connor
Interim Chief Financial Officer
Stanford Health Care



Dana Haering
Chief Financial Officer
Lucile Salter Packard Children's Hospital at Stanford

SELECTED FINANCIAL AND OTHER DATA

Fiscal Years Ended August 31

| | 2016 | 2015 | 2014 | 2013 | 2012 |
|---|-----------------------|-----------|-----------|-----------|-----------|
| | (dollars in millions) | | | | |
| CONSOLIDATED STATEMENT OF ACTIVITIES HIGHLIGHTS: | | | | | |
| Total operating revenues | \$ 9,797 | \$ 9,051 | \$ 7,924 | \$ 7,359 | \$ 6,814 |
| Student income (A) | 587 | 564 | 534 | 511 | 481 |
| Sponsored research support | 1,453 | 1,387 | 1,266 | 1,233 | 1,234 |
| Health care services | 5,264 | 4,744 | 3,942 | 3,734 | 3,245 |
| Investment income distributed for operations | 1,338 | 1,292 | 1,181 | 1,019 | 1,015 |
| Total operating expenses | 9,307 | 8,351 | 7,389 | 6,794 | 6,298 |
| Change in net assets from operating activities | 490 | 700 | 535 | 565 | 516 |
| Other changes in net assets | 947 | 1,034 | 3,582 | 2,441 | 1,043 |
| Net change in total net assets | \$ 1,437 | \$ 1,734 | \$ 4,117 | \$ 3,006 | \$ 1,559 |
| CONSOLIDATED STATEMENT OF FINANCIAL POSITION HIGHLIGHTS: | | | | | |
| Investments at fair value | \$ 31,332 | \$ 31,399 | \$ 30,464 | \$ 26,974 | \$ 24,146 |
| Plant facilities, net of accumulated depreciation | 9,000 | 7,797 | 6,832 | 5,995 | 5,320 |
| Notes and bonds payable | 5,402 | 5,125 | 5,139 | 4,782 | 4,409 |
| Total assets | 46,586 | 44,509 | 42,547 | 37,988 | 34,785 |
| Total liabilities | 9,616 | 8,976 | 8,748 | 8,306 | 8,110 |
| Total net assets | 36,970 | 35,533 | 33,799 | 29,682 | 26,675 |
| UNIVERSITY STATEMENT OF FINANCIAL POSITION HIGHLIGHTS: | | | | | |
| Investments at fair value | \$ 29,086 | \$ 28,766 | \$ 27,829 | \$ 24,703 | \$ 22,247 |
| Plant facilities, net of accumulated depreciation | 5,169 | 4,796 | 4,559 | 4,208 | 3,826 |
| Notes and bonds payable | 3,271 | 3,085 | 3,265 | 3,098 | 2,709 |
| Total assets | 37,767 | 36,214 | 35,227 | 31,540 | 28,981 |
| Total liabilities | 6,048 | 5,780 | 6,006 | 5,817 | 5,476 |
| Total net assets | 31,719 | 30,434 | 29,221 | 25,723 | 23,505 |
| OTHER FINANCIAL DATA AND METRICS: | | | | | |
| University endowment at year end | \$ 22,398 | \$ 22,223 | \$ 21,446 | \$ 18,689 | \$ 17,036 |
| University endowment payout in support of operations | 1,132 | 1,058 | 985 | 921 | 871 |
| As a % of beginning of year University endowment | 5.1% | 4.9% | 5.3% | 5.4% | 5.3% |
| As a % of University total expenses | 23.0% | 22.8% | 24.8% | 24.5% | 24.8% |
| Total gifts as reported by the Office of Development (B) | 951 | 1,625 | 976 | 1,010 | 1,077 |
| STUDENTS: | | | | | |
| ENROLLMENT: (C) | | | | | |
| Undergraduate | 7,032 | 6,994 | 7,018 | 6,980 | 6,999 |
| Graduate | 9,304 | 9,196 | 9,118 | 8,980 | 8,958 |
| DEGREES CONFERRED: | | | | | |
| Bachelor degrees | 1,744 | 1,671 | 1,651 | 1,661 | 1,715 |
| Advanced degrees | 3,370 | 3,286 | 3,292 | 3,365 | 3,305 |
| FACULTY: | | | | | |
| Total Professoriate (C) | 2,180 | 2,153 | 2,118 | 2,043 | 1,995 |
| ANNUAL UNDERGRADUATE TUITION RATE (IN DOLLARS) | \$ 45,729 | \$ 44,184 | \$ 42,690 | \$ 41,250 | \$ 40,050 |

(A) Student income is reported net of financial aid in the Consolidated Statements of Activities.

(B) Includes University, SHC and LPCH gifts. The FY15 amount includes \$626 million in works of art and special collections. In FY15, the University received a significant collection of artwork which is included with other donations reported by the Office of Development. As stated in Note 1, Stanford does not capitalize works of art and special collections.

(C) Fall quarter immediately following fiscal year end.

MANAGEMENT RESPONSIBILITY FOR FINANCIAL STATEMENTS

The Leland Stanford Junior University (“Stanford University” or the “University”) is the sole member of Stanford Health Care (SHC) and Lucile Salter Packard Children’s Hospital at Stanford (LPCH). SHC and LPCH each have their own separate management with responsibility for their own financial reporting.

Management of the University, SHC and LPCH is each responsible for the integrity and reliability of their respective portions of these financial statements. The University oversees the process of consolidating the SHC’s and LPCH’s 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 (“U.S. GAAP”).

In accumulating and controlling financial data, management of the University, SHC and LPCH maintains separate systems of internal control. Management of the respective entities believes that effective internal control has been designed, implemented and maintained to provide reasonable assurance that assets are protected and that transactions and events are recorded properly. All internal control systems, however, no matter how well designed, have inherent limitations and can provide only reasonable assurance that their objectives are met.

The accompanying consolidated financial statements have been audited by the University’s, SHC’s and LPCH’s independent auditor, PricewaterhouseCoopers LLP. Their report expresses an opinion as to whether the consolidated financial statements, considered in their entirety, present fairly, in conformity with U.S. GAAP, the consolidated financial position and changes in net assets and cash flows. The independent auditor’s opinion is based on audit procedures described in their report, which include considering internal control relevant to the preparation and fair presentation of the consolidated financial statements in order to design audit procedures to provide reasonable assurance that the financial statements are free from material misstatement.

The Board of Trustees of the University and the separate Boards of Directors of SHC and LPCH, through their respective audit committees, comprised of trustees and directors not employed by the University, SHC or LPCH, are responsible for engaging the independent auditor and meeting with management, internal auditors and the independent auditor 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 auditor have full and free access to the respective audit committees. Both meet with the respective audit committees at least annually, with and without each other, and without the presence of management representatives.



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Chief Financial Officer
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Report of Independent Auditors

To the Board of Trustees of the
Leland Stanford Junior University

We have audited the accompanying consolidated financial statements of the Leland Stanford Junior University and its subsidiaries ("Stanford"), which comprise the consolidated statements of financial position as of August 31, 2016 and 2015, and the related consolidated statements of activities and cash flows for the years then ended.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on the consolidated financial statements based on our audits. We conducted our audits 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to Stanford's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of Stanford's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Leland Stanford Junior University and its subsidiaries at August 31, 2016 and 2015, and their changes in net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

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

December 6, 2016

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

At August 31, 2016 and 2015 (in thousands of dollars)

Includes the separate legal entities of The Leland Stanford Junior University, Stanford Health Care and Lucile Salter Packard Children's Hospital at Stanford and other majority-owned or controlled entities of these organizations

| | 2016 | 2015 |
|--|----------------------|----------------------|
| ASSETS | | |
| Cash and cash equivalents | \$ 1,863,584 | \$ 1,519,782 |
| Assets limited as to use | 551,896 | 830,552 |
| Accounts receivable, net | 1,260,796 | 1,133,476 |
| Prepaid expenses and other assets | 318,177 | 276,420 |
| Pledges receivable, net | 1,570,912 | 921,519 |
| Student loans receivable, net | 78,549 | 81,492 |
| Faculty and staff mortgages and other loans receivable, net | 610,026 | 549,724 |
| Investments at fair value, including securities pledged or on loan of \$205,128 and \$106,264 for 2016 and 2015, respectively | 31,332,231 | 31,399,176 |
| Plant facilities, net of accumulated depreciation | 8,999,916 | 7,797,306 |
| Works of art and special collections | - | - |
| TOTAL ASSETS | \$ 46,586,087 | \$ 44,509,447 |
| LIABILITIES AND NET ASSETS | | |
| LIABILITIES: | | |
| Accounts payable and accrued expenses | \$ 2,034,934 | \$ 1,738,631 |
| Accrued pension and postretirement benefit obligations | 699,464 | 824,189 |
| Liabilities associated with investments | 353,848 | 212,656 |
| Deferred rental and other income | 657,378 | 652,850 |
| Income beneficiary share of split interest agreements | 414,432 | 435,426 |
| Notes and bonds payable | 5,401,768 | 5,058,743 |
| U.S. government refundable loan funds | 54,035 | 54,081 |
| TOTAL LIABILITIES | 9,615,859 | 8,976,576 |
| NET ASSETS: | | |
| Unrestricted | 21,136,422 | 20,375,039 |
| Temporarily restricted | 8,545,950 | 8,763,932 |
| Permanently restricted | 7,287,856 | 6,393,900 |
| TOTAL NET ASSETS | 36,970,228 | 35,532,871 |
| TOTAL LIABILITIES AND NET ASSETS | \$ 46,586,087 | \$ 44,509,447 |

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

CONSOLIDATED STATEMENTS OF ACTIVITIES

For the years ended August 31, 2016 and 2015 (in thousands of dollars)

Includes the separate legal entities of The Leland Stanford Junior University, Stanford Health Care and Lucile Salter Packard Children's Hospital at Stanford and other majority-owned or controlled entities of these organizations

| | 2016 | 2015 |
|---|-------------------|-------------------|
| UNRESTRICTED NET ASSETS | | |
| OPERATING REVENUES: | | |
| Student income: | | |
| Undergraduate programs | \$ 342,309 | \$ 330,851 |
| Graduate programs | 340,537 | 329,047 |
| Room and board | 174,111 | 164,304 |
| Student financial aid | (269,613) | (260,616) |
| TOTAL STUDENT INCOME | 587,344 | 563,586 |
| Sponsored research support: | | |
| Direct costs - University | 753,638 | 713,831 |
| Direct costs - SLAC National Accelerator Laboratory | 447,834 | 430,365 |
| Indirect costs | 251,395 | 242,572 |
| TOTAL SPONSORED RESEARCH SUPPORT | 1,452,867 | 1,386,768 |
| HEALTH CARE SERVICES , primarily net patient service revenue | 5,264,433 | 4,743,819 |
| CURRENT YEAR GIFTS IN SUPPORT OF OPERATIONS | 258,285 | 241,175 |
| Net assets released from restrictions: | | |
| Payments received on pledges | 107,302 | 123,210 |
| Prior year gifts released from donor restrictions | 76,978 | 51,089 |
| TOTAL NET ASSETS RELEASED FROM RESTRICTIONS | 184,280 | 174,299 |
| Investment income distributed for operations: | | |
| Endowment | 1,147,980 | 1,072,710 |
| Expendable funds pools and other investment income | 190,512 | 219,037 |
| TOTAL INVESTMENT INCOME DISTRIBUTED FOR OPERATIONS | 1,338,492 | 1,291,747 |
| SPECIAL PROGRAM FEES AND OTHER INCOME | 711,591 | 649,882 |
| TOTAL OPERATING REVENUES | 9,797,292 | 9,051,276 |
| OPERATING EXPENSES: | | |
| Salaries and benefits | 5,527,284 | 4,795,588 |
| Depreciation | 538,597 | 502,635 |
| Other operating expenses | 3,241,294 | 3,052,669 |
| TOTAL OPERATING EXPENSES | 9,307,175 | 8,350,892 |
| CHANGE IN NET ASSETS FROM OPERATING ACTIVITIES | \$ 490,117 | \$ 700,384 |

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

CONSOLIDATED STATEMENTS OF ACTIVITIES, Continued

For the years ended August 31, 2016 and 2015 (in thousands of dollars)

Includes the separate legal entities of The Leland Stanford Junior University, Stanford Health Care and Lucile Salter Packard Children's Hospital at Stanford and other majority-owned or controlled entities of these organizations

| | 2016 | 2015 |
|---|----------------------|----------------------|
| UNRESTRICTED NET ASSETS (continued) | | |
| CHANGE IN NET ASSETS FROM OPERATING ACTIVITIES | \$ 490,117 | \$ 700,384 |
| NON-OPERATING ACTIVITIES: | | |
| Increase in reinvested gains | 167,634 | 745,722 |
| Donor advised funds, net | 21,783 | 66,734 |
| Current year gifts not included in operations | 2,381 | 1,655 |
| Capital and other gifts released from restrictions | 118,490 | 100,980 |
| Pension and other postemployment benefit related changes other than net periodic benefit expense | 182,013 | (105,230) |
| Transfer to permanently restricted net assets, net | (45,651) | (49,998) |
| Transfer to temporarily restricted net assets, net | (35,082) | (26,223) |
| Swap interest and change in value of swap agreements | (135,924) | (67,979) |
| Contribution income from Stanford Health Care-ValleyCare affiliation | - | 96,758 |
| Other | (4,378) | (3,919) |
| NET CHANGE IN UNRESTRICTED NET ASSETS | 761,383 | 1,458,884 |
| TEMPORARILY RESTRICTED NET ASSETS | | |
| Gifts and pledges, net | 435,507 | 373,951 |
| Decrease in reinvested gains | (337,062) | (70,902) |
| Change in value of split interest agreements, net | 14,866 | 2,195 |
| Net assets released to operations | (208,619) | (197,186) |
| Capital and other gifts released to unrestricted net assets | (118,490) | (100,980) |
| Transfer from unrestricted net assets, net | 35,082 | 26,223 |
| Transfer to permanently restricted net assets, net | (35,551) | (27,999) |
| Other | (3,715) | (3,829) |
| NET CHANGE IN TEMPORARILY RESTRICTED NET ASSETS | (217,982) | 1,473 |
| PERMANENTLY RESTRICTED NET ASSETS | | |
| Gifts and pledges, net | 769,861 | 209,058 |
| Increase in reinvested gains | 25,566 | 1,760 |
| Change in value of split interest agreements, net | 19,308 | (15,756) |
| Transfer from unrestricted net assets, net | 45,651 | 49,998 |
| Transfer from temporarily restricted net assets, net | 35,551 | 27,999 |
| Other | (1,981) | 523 |
| NET CHANGE IN PERMANENTLY RESTRICTED NET ASSETS | 893,956 | 273,582 |
| NET CHANGE IN TOTAL NET ASSETS | 1,437,357 | 1,733,939 |
| Total net assets, beginning of year | 35,532,871 | 33,798,932 |
| TOTAL NET ASSETS, END OF YEAR | \$ 36,970,228 | \$ 35,532,871 |

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the years ended August 31, 2016 and 2015 (in thousands of dollars)

Includes the separate legal entities of The Leland Stanford Junior University, Stanford Health Care and Lucile Salter Packard Children's Hospital at Stanford and other majority-owned or controlled entities of these organizations

| | 2016 | 2015 |
|---|---------------------|---------------------|
| CASH FLOW FROM OPERATING ACTIVITIES | | |
| Change in net assets | \$ 1,437,357 | \$ 1,733,939 |
| Adjustments to reconcile change in net assets to net cash provided by operating activities: | | |
| Depreciation | 538,597 | 502,635 |
| Amortization, loss on disposal of fixed assets and other adjustments | (2,782) | 7,319 |
| Provision for doubtful accounts for health care services | 123,847 | 142,075 |
| Net gains on investments and security agreements | (930,428) | (1,691,192) |
| Changes in fair value of interest rate swaps | 132,596 | 64,519 |
| Changes in split interest agreements | 9,172 | 22,093 |
| Investment income for restricted purposes | (30,815) | (31,828) |
| Gifts restricted for long-term investments | (888,137) | (354,100) |
| Gifts of securities and properties | (15,585) | (42,330) |
| Contribution income from Stanford Health Care-ValleyCare affiliation | - | (96,820) |
| Premiums received from bond issuance | 94,098 | 5,627 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable, net | (193,954) | (338,920) |
| Pledges receivable, net | (104,867) | (372) |
| Prepaid expenses and other assets | (48,914) | (38,447) |
| Accounts payable and accrued expenses | 143,310 | 194,884 |
| Accrued pension and postretirement benefit obligations | (124,725) | 140,614 |
| Deferred rental and other income | 4,528 | 36,275 |
| Other | 5,577 | 35 |
| NET CASH PROVIDED BY OPERATING ACTIVITIES | 148,875 | 256,006 |
| CASH FLOW FROM INVESTING ACTIVITIES | | |
| Land, building and equipment purchases | (1,693,181) | (1,282,265) |
| Student, faculty and other loans: | | |
| New loans made | (117,150) | (104,509) |
| Principal collected | 50,335 | 55,444 |
| Decrease in assets limited as to use | 278,788 | 236,271 |
| Cash acquired from ValleyCare, net of cash paid as consideration | - | (52,539) |
| Purchases of investments | (14,416,420) | (28,366,613) |
| Sales and maturities of investments | 15,385,843 | 29,150,703 |
| NET CASH USED FOR INVESTING ACTIVITIES | (511,785) | (363,508) |
| CASH FLOW FROM FINANCING ACTIVITIES | | |
| Gifts and reinvested income for restricted purposes | 349,969 | 424,905 |
| Proceeds from borrowing | 586,154 | 535,311 |
| Bond issuance costs and interest rate swaps | (2,154) | (2,528) |
| Repayment of notes and bonds payable | (322,700) | (543,648) |
| Increase (decrease) in liabilities associated with investments | 98,467 | (58,586) |
| Other | (3,024) | (196) |
| NET CASH PROVIDED BY FINANCING ACTIVITIES | 706,712 | 355,258 |
| INCREASE IN CASH AND CASH EQUIVALENTS | 343,802 | 247,756 |
| Cash and cash equivalents, beginning of year | 1,519,782 | 1,272,026 |
| CASH AND CASH EQUIVALENTS, END OF YEAR | \$ 1,863,584 | \$ 1,519,782 |
| SUPPLEMENTAL DATA: | | |
| Interest paid, net of capitalized interest | \$ 173,268 | \$ 178,078 |
| Cash collateral received under security lending agreements | \$ 213,629 | \$ 110,087 |
| Increase in payables for plant facilities | \$ 31,428 | \$ 46,762 |

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 The Leland Stanford Junior University (“Stanford University” or the “University”), Stanford Health Care (SHC), Lucile Salter Packard Children’s Hospital at Stanford (LPCH) and other majority-owned or controlled entities of the University, SHC and LPCH. Collectively, all of these entities are referred to as “Stanford”. 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 information 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 U.S. 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 *Consolidated Statements of Activities*, but SLAC’s assets and liabilities are not included in the *Consolidated 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 (the “Hospitals”) are California not-for-profit public benefit corporations, each governed by a separate Board of Directors. 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, the SOM and Hospitals comprise Stanford Medicine. SHC and LPCH 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 medical foundations to support Stanford Medicine’s mission of delivering quality care to the community and conducting research and education.

In September 2014, SHC entered into an affiliation agreement with The Hospital Committee for the Livermore-Pleasanton Areas (dba Stanford Health Care – ValleyCare) (“SHC-VC”) to acquire control by becoming the sole corporate member of SHC-VC. On May 18, 2015, with all conditions of the affiliation agreement satisfied and all regulatory approvals obtained, the acquisition of control of SHC-VC by SHC was consummated and became effective. Because of the acquisition of control, for financial reporting purposes SHC is treated as having acquired assets of \$233.2 million, including “plant facilities, net of accumulated depreciation” of \$135.6 million, and assumed liabilities of \$64.3 million during the year ended August 31, 2015. The excess of net assets over consideration paid was \$96.8 million and is recorded as contribution income in “non-operating activities” in the *Consolidated Statements of Activities* for the year ended August 31, 2015.

TAX STATUS

The University, SHC and LPCH 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, except with regard to unrelated business income which is taxed at corporate income tax rates.

In accordance with the guidance on accounting for uncertainty in income taxes, management regularly evaluates its tax positions and does not believe the University, SHC or LPCH have any uncertain tax positions that require disclosure or adjustment to the consolidated financial statements. The University, SHC and LPCH are subject to routine audits by taxing jurisdictions. The respective managements of the University, SHC and LPCH believe they are no longer subject to income tax examinations for fiscal years prior to August 31, 2012.

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 Stanford for specific purposes under internal operating and administrative arrangements or be subject to contractual agreements with external parties. Donor-restricted contributions that relate to Stanford's 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 Stanford include the revenues earned and expenses incurred in the current year to support teaching, research, and patient care. The non-operating activities of Stanford include increases in reinvested gains, current year gifts not included in operations, capital and other gifts released from restrictions, pension and other postemployment benefit related changes other than net periodic benefit expense, contribution income from the SHC-VC affiliation 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 Stanford, 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 *Note 12*). Donor-restricted resources intended for capital projects are initially recorded as temporarily restricted and then released and reclassified as unrestricted net assets when the

asset is placed in service. Also included in this category is Stanford'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 split interest agreements 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, Stanford'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 *Consolidated Statements of Financial Position* consist of U.S. Treasury bills, 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 amortized cost, which approximates fair value. Cash and cash equivalents that are held for investment purposes are classified as investments (see *Note 6*).

ASSETS LIMITED AS TO USE

Assets limited as to use consist primarily of proceeds of tax-exempt bonds issued for the benefit of the University and limited by the terms of indentures to use for qualified capital projects. Assets limited as to use also include trustee-held accounts reflecting proceeds of tax-exempt bonds issued for the benefit of SHC and LPCH and limited by the terms of indentures to use for qualified 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, 2009 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, 2009 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 *Consolidated Statements of Activities* (see *Note 6*).

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 flows are subjective, requiring significant judgments such as the amount and timing of future cash flows and the selection of appropriate discount rates that reflect market and credit risks. Stanford management regularly assesses 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, 2016 and 2015 are as follows:

| | |
|-------------------------------------|-------------|
| Land improvements | 10-25 years |
| Buildings and building improvements | 4-50 years |
| Furniture, fixtures and equipment | 3-20 years |
| Utilities | 5-40 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. Purchases of collection items are recorded as operating expenses in the period in which they are acquired. Proceeds from sales of such items are used to acquire other items for the collections.

DONATED ASSETS

Donated assets, other than works of art and special collections, are recorded at fair value at the date of donation. Undeveloped land, including land acquired under the original endowment to the University 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 significant portion of the gift must be designated to the University. At August 31, 2016 and 2015, approximately \$413.7 million and \$386.0 million, respectively, of DAFs may be used to support other approved charities; the donors have advisory privileges with respect to the distribution of these funds.

Current year gifts under the DAF agreements are included in the *Consolidated 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 *Consolidated Statements of Activities* as a reduction to "donor advised funds, net" at the time the transfer is made.

SPLIT INTEREST AGREEMENTS

Split interest agreements consist of arrangements with donors where Stanford has an interest in assets held by a trustee and receives benefits that are shared with other beneficiaries. Split interest agreements where Stanford is not the trustee are recorded in the "assets held by other trustees" category of "investments" in the *Consolidated Statements of Financial Position* as described in *Note 6*.

The assets held under split interest agreements where Stanford is the trustee were \$733.9 million and \$733.8 million at August 31, 2016 and 2015, respectively, and were recorded in various "investments" categories; a liability for the discounted present value of any income beneficiary interest is reported as "income beneficiary share of split interest agreements" in the *Consolidated Statements of Financial Position*. At August 31, 2016 and 2015, discount rates of 1.8% and 2% were used, respectively, based on the Charitable Federal Midterm Rate.

During fiscal years 2016 and 2015, the discounted present value of new gifts subject to split interest agreements, and net of any income beneficiary share, was \$11.3 million and \$40.6 million, respectively, and was included in "gifts and pledges, net" in the *Consolidated Statements of Activities*. Actuarial gains or losses were included in "change in value of split interest agreements, net" in the *Consolidated 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 *Consolidated 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. SHC and LPCH 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 SHC 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 SHC 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 *Consolidated Statements of Activities* as a non-operating activity in "swap interest and change in value of swap agreements". The settlements (net cash payments less receipts) under the interest rate exchange agreements are recorded in the *Consolidated Statements of Activities* in "swap interest and change in value of swap agreements" for the University and in "other operating expenses" for SHC.

The University has also entered into interest rate exchange agreements to reduce the effect of interest rate fluctuations of certain investment positions (see *Note 8*).

STUDENT INCOME

The University provides financial assistance in the form of scholarship and fellowship grants that cover a portion of tuition, living and other costs that is reflected as a reduction of student income. Graduate student research and teaching assistantship appointments provide the recipient with salary and tuition support, which are reflected as salaries and benefits expense and other operating expense, respectively.

PATIENT CARE AND OTHER SERVICES

Health Care Services

"Patient care, net" is reported in the *Consolidated Statements of Activities* at the estimated net realizable amounts from patients, third-party payers, and others for services rendered. SHC and LPCH 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 (see *Note 3*).

The University has entered into various operating agreements with SHC and LPCH for the professional services of SOM faculty members, and for non-physician services such as telecommunications, facilities, and other services. The payments by the Hospitals to the University for professional services are eliminated in consolidation.

Charity Care

SHC and LPCH 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 (see *Note 3*).

RECENT ACCOUNTING PRONOUNCEMENTS

In November 2016, the Financial Accounting Standards Board (FASB) issued an update to the Accounting Standards Codification (ASC) which requires that the amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The new guidance is effective for fiscal year 2020. Stanford is currently evaluating the impact that this guidance will have on the consolidated financial statements.

In August 2016, the FASB issued an update to the ASC which makes several modifications to current reporting requirements for not-for-profit (NFP) entities. The ASC update changes the way NFPs classify net assets and results in significant changes to financial reporting and disclosures for NFPs. The new guidance is effective for fiscal year 2019. Stanford is currently evaluating the impact that this guidance will have on the consolidated financial statements.

In February 2016, the FASB issued an update to the ASC which requires lessees to recognize operating and financing lease liabilities and corresponding right-of use assets on the statement of financial position. The new guidance is effective for fiscal year 2020. Stanford is currently evaluating the impact that this guidance will have on the consolidated financial statements.

In May 2015, the FASB issued an update to the ASC which modifies reporting requirements for investments that are eligible to be measured at fair value using the net asset value (or its equivalent) as a practical expedient. The ASC update removes the requirement to categorize these investments within the fair value hierarchy and make certain disclosures. The new guidance is effective for fiscal year 2018 but early adoption is allowed. Stanford has early adopted this guidance in fiscal year 2016 (see *Note 6*).

In April 2015, the FASB issued an update to the ASC which requires debt issuance costs to be presented in the statement of financial position as a direct deduction from the carrying value of the associated debt liability, consistent with the presentation of a debt discount. The new guidance is effective for fiscal year 2017. In August 2015, the FASB issued a supplemental ASU which allows an entity to present debt issuance costs related to a line of credit arrangement as an asset and subsequently amortize the costs ratably over the term of the line of credit arrangement. The recognition and measurement guidance for debt issuance costs is not affected. Stanford does not expect the new guidance to have a material impact on the consolidated financial statements.

In May 2014, the FASB issued an update to the ASC to improve consistency of revenue recognition practices across industries for economically similar transactions. Subsequently, the FASB has issued several amendments and updates to the original standard. The core principle is that an entity recognizes revenue for goods or services to customers in an amount that reflects the consideration it expects to receive in return. The guidance is effective for fiscal year 2019. Stanford is currently evaluating the impact that this guidance will have on the consolidated financial statements.

2. Accounts Receivable

Accounts receivable, net of bad debt allowances, at August 31, 2016 and 2015, in thousands of dollars, are as follows:

| | UNIVERSITY | SHC | LPCH | CONSOLIDATED |
|-----------------------------------|-------------------|-------------------|-------------------|---------------------|
| 2016 | | | | |
| U.S. government sponsors | \$ 104,240 | \$ - | \$ - | \$ 104,240 |
| Non-federal sponsors and programs | 49,282 | 23,939 | 15,827 | 89,048 |
| Pending trades of securities | 94,304 | - | - | 94,304 |
| Accrued interest on investments | 10,816 | - | - | 10,816 |
| Student | 7,171 | - | - | 7,171 |
| Patient and third-party payers: | | | | |
| Blue Cross | - | 117,644 | 76,551 | 194,195 |
| Blue Shield | - | 73,561 | 32,356 | 105,917 |
| Medicare | - | 90,980 | 440 | 91,420 |
| Medi-Cal | - | 17,081 | 41,533 | 58,614 |
| Other managed care and payers | - | 421,486 | 128,964 | 550,450 |
| Other | 52,195 | 58,497 | 18,233 | 128,925 |
| | 318,008 | 803,188 | 313,904 | 1,435,100 |
| Less bad debt allowances | (1,815) | (160,819) | (11,670) | (174,304) |
| ACCOUNTS RECEIVABLE, NET | \$ 316,193 | \$ 642,369 | \$ 302,234 | \$ 1,260,796 |
| 2015 | | | | |
| U.S. government sponsors | \$ 89,809 | \$ - | \$ - | \$ 89,809 |
| Non-federal sponsors and programs | 43,245 | 30,754 | 15,279 | 89,278 |
| Pending trades of securities | 33,451 | - | - | 33,451 |
| Accrued interest on investments | 9,378 | - | - | 9,378 |
| Student | 6,592 | - | - | 6,592 |
| Patient and third-party payers: | | | | |
| Blue Cross | - | 105,199 | 76,424 | 181,623 |
| Blue Shield | - | 97,654 | 34,062 | 131,716 |
| Medicare | - | 90,184 | 1,136 | 91,320 |
| Medi-Cal | - | 14,615 | 42,405 | 57,020 |
| Other managed care and payers | - | 387,924 | 139,018 | 526,942 |
| Other | 44,663 | 26,449 | 13,065 | 84,177 |
| | 227,138 | 752,779 | 321,389 | 1,301,306 |
| Less bad debt allowances | (1,698) | (144,855) | (21,277) | (167,830) |
| ACCOUNTS RECEIVABLE, NET | \$ 225,440 | \$ 607,924 | \$ 300,112 | \$ 1,133,476 |

3. Health Care Services Revenue

SHC and LPCH derive a majority of health care services revenue from contractual agreements with Medicare, Medi-Cal and other third-party payers that provide for payments at amounts different from established rates. Payments under these agreements and programs are based on a variety of payment models, 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.

A summary of payment arrangements with major third-party payers follows:

Medicare

Inpatient acute care services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Medicare reimburses hospitals for covered outpatient services rendered to its beneficiaries by way of an outpatient prospective payment system based on ambulatory payment classifications.

Inpatient non-acute services, certain outpatient services and medical education costs related to Medicare beneficiaries are paid based, in part, on a cost reimbursement methodology subject to final settlement after submission of annual cost reports and audits thereof by the Medicare fiscal intermediary. The estimated amounts due to or from the program are reviewed and adjusted annually based on the status of such audits and any subsequent appeals. Differences between final settlements and amounts accrued in previous years are reported as adjustments to net health care services revenue in the year examination is substantially completed. Medicare cost reports have been audited by the Medicare administrative contractor through August 31, 2006 for SHC and August 31, 2014 for LPCH.

Professional services are reimbursed based on a fee schedule.

Medi-Cal

The State reimburses hospitals for inpatient services rendered to Medi-Cal program beneficiaries based on a prospectively determined rate per discharge. Hospital outpatient and professional services are reimbursed based upon prospectively determined fee schedules.

Managed Care Organizations

SHC and LPCH have entered into agreements with numerous third-party payers to provide patient care to beneficiaries under a variety of payment arrangements. These include arrangements with:

- Commercial insurance companies which reimburse at negotiated charges.
- Managed care contracts such as those with HMOs and PPOs, which reimburse at contracted or per diem rates, which are usually less than full charges.
- Counties in the State of California, which reimburse for certain indigent patients covered under county contracts.

Uninsured

For uninsured patients that do not qualify for charity care, revenue is recognized on the basis of standard rates for services less an uninsured discount applied to the patient's account that approximates the average discount for managed care payers.

The following table presents health care services revenue, net of contractual allowances (but before provision for doubtful accounts), for the years ended August 31, in thousands of dollars:

| | UNIVERSITY | SHC | LPCH | ELIMINATIONS | CONSOLIDATED |
|---|-------------------|---------------------|---------------------|---------------------|---------------------|
| 2016 | | | | | |
| Medicare | \$ - | \$ 755,658 | \$ 7,390 | \$ - | \$ 763,048 |
| Medi-Cal | - | 106,728 | 260,368 | - | 367,096 |
| Managed care | - | 2,870,437 | 967,809 | - | 3,838,246 |
| Self pay and other | - | 239,248 | 75,384 | - | 314,632 |
| Premium revenue | - | 72,292 | - | - | 72,292 |
| Physician services and support (see Note 1) | 873,520 | 47,214 | - | (920,734) | - |
| Other services and support | 32,966 | - | - | - | 32,966 |
| | 906,486 | 4,091,577 | 1,310,951 | (920,734) | 5,388,280 |
| Provision for doubtful accounts | - | (126,280) | 2,433 | - | (123,847) |
| HEALTH CARE SERVICES REVENUE | \$ 906,486 | \$ 3,965,297 | \$ 1,313,384 | \$ (920,734) | \$ 5,264,433 |
| 2015 | | | | | |
| Medicare | \$ - | \$ 732,377 | \$ 6,831 | \$ - | \$ 739,208 |
| Medi-Cal | - | 77,950 | 271,231 | - | 349,181 |
| Managed care | - | 2,421,560 | 989,394 | - | 3,410,954 |
| Self pay and other | - | 246,040 | 47,131 | - | 293,171 |
| Premium revenue | - | 62,893 | - | - | 62,893 |
| Physician services and support (see Note 1) | 810,474 | 47,087 | - | (857,561) | - |
| Other services and support | 30,487 | - | - | - | 30,487 |
| | 840,961 | 3,587,907 | 1,314,587 | (857,561) | 4,885,894 |
| Provision for doubtful accounts | - | (131,601) | (10,474) | - | (142,075) |
| HEALTH CARE SERVICES REVENUE | \$ 840,961 | \$ 3,456,306 | \$ 1,304,113 | \$ (857,561) | \$ 4,743,819 |

SHC recognized net health care services revenue adjustments of \$4.3 million and \$34.2 million as a result of prior years' favorable developments related to reimbursement and appeals for the years ended August 31, 2016 and 2015, respectively. LPCH had no significant adjustments to revenue for the years ended August 31, 2016 and 2015.

SHC's and LPCH's provisions for doubtful accounts are based upon management's assessment of expected net collections considering historical experience and other collection indicators.

Charity Care

SHC's estimated cost of providing charity care was \$19.4 million and \$9.7 million, and LPCH's estimated cost of providing charity care was \$1.6 million and \$2.8 million for the years ended August 31, 2016 and 2015, 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. SHC received \$799 thousand and \$526 thousand during the years ended August 31, 2016 and 2015, respectively, from contributions that were restricted for the care of indigent patients.

SHC and LPCH also provide services to other patients under the 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 the Medicare, Medi-Cal and other publicly sponsored programs for the years ended August 31, 2016 and 2015 were \$869.0 million and \$610.0 million for SHC, and \$212.7 million and \$219.6 million for LPCH, respectively.

Provider Fee

The State of California enacted legislation in 2009 through 2016 which established a Hospital Quality Assurance Fee (QAF) Program and a Hospital Fee Program. These programs impose a provider fee on certain California general acute care hospitals that, combined with federal matching funds, is used to provide supplemental payments to certain hospitals and support the State's effort to maintain health care coverage for children. Provider fee revenue, net of expenses, under these programs for the years ended August 31, in thousands of dollars, is as follows:

| | SHC | LPCH | CONSOLIDATED |
|--------------|------------------|------------------|------------------|
| 2016 | | | |
| Revenues | \$ 55,195 | \$ 51,793 | \$ 106,988 |
| Expenses | (45,809) | (24,196) | (70,005) |
| TOTAL | \$ 9,386 | \$ 27,597 | \$ 36,983 |
| 2015 | | | |
| Revenues | \$ 103,667 | \$ 79,775 | \$ 183,442 |
| Expenses | (73,585) | (43,156) | (116,741) |
| TOTAL | \$ 30,082 | \$ 36,619 | \$ 66,701 |

4. Pledges Receivable

Pledges are recorded at applicable risk-adjusted discount rates, ranging from 1.1% to 5.7%, commensurate with the duration of the donor's payment plan. At August 31, 2016 and 2015, pledges receivable, net of discounts and allowances, in thousands of dollars, are as follows:

| | UNIVERSITY | SHC | LPCH | CONSOLIDATED |
|---------------------------------|---------------------|-------------------|-------------------|---------------------|
| 2016 | | | | |
| One year or less | \$ 151,591 | \$ 11,531 | \$ 33,182 | \$ 196,304 |
| Between one year and five years | 997,348 | 86,428 | 55,921 | 1,139,697 |
| More than five years | 403,638 | 11,352 | 45,369 | 460,359 |
| | 1,552,577 | 109,311 | 134,472 | 1,796,360 |
| Less discounts and allowances | (195,069) | (11,558) | (18,821) | (225,448) |
| PLEDGES RECEIVABLE, NET | \$ 1,357,508 | \$ 97,753 | \$ 115,651 | \$ 1,570,912 |
| 2015 | | | | |
| One year or less | \$ 123,719 | \$ 19,371 | \$ 8,372 | \$ 151,462 |
| Between one year and five years | 710,950 | 106,733 | 3,836 | 821,519 |
| More than five years | 79,667 | 18,504 | 25,000 | 123,171 |
| | 914,336 | 144,608 | 37,208 | 1,096,152 |
| Less discounts and allowances | (153,817) | (14,151) | (6,665) | (174,633) |
| PLEDGES RECEIVABLE, NET | \$ 760,519 | \$ 130,457 | \$ 30,543 | \$ 921,519 |

Conditional pledges for the University, which depend on the occurrence of a specified future and uncertain event, were \$6.5 million and \$6.7 million at August 31, 2016 and 2015, respectively. SHC and LPCH had no conditional pledges at August 31, 2016 and 2015.

5. Loans Receivable

Loans receivable consist primarily of University student loans receivable and faculty and staff mortgages. University 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, 2016 and 2015, in thousands of dollars, are as follows:

| | 2016 | 2015 |
|--|------------------|------------------|
| Institutional loans | \$ 25,577 | \$ 24,286 |
| Federally-sponsored loans | 53,766 | 57,853 |
| | 79,343 | 82,139 |
| Less allowance for student loan losses | (794) | (647) |
| STUDENT LOANS RECEIVABLE, NET | \$ 78,549 | \$ 81,492 |

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

Federally-sponsored loans are funded by advances to the University primarily under the Federal Perkins Loan Program (the "Program"). Loans to students under the Program are subject to mandatory interest rates and significant restrictions and 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 *Consolidated 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 \$609.3 million and \$547.2 million at August 31, 2016 and 2015, respectively, from University faculty and staff are included in "faculty and staff mortgages and other loans receivable, net" in the *Consolidated Statements of Financial Position*. These loans and mortgages are collateralized by deeds of trust on properties concentrated in the region surrounding the University. Management has determined that no allowance is necessary.

6. Investments

Investments are measured and recorded at fair value. The valuation methodology, investment categories, fair value hierarchy, certain investment activities and related commitments for fiscal years 2016 and 2015 are discussed below.

Investments held by Stanford at August 31, 2016 and 2015, in thousands of dollars, are as follows:

| | UNIVERSITY | SHC | LPCH | CONSOLIDATED |
|---|----------------------|---------------------|-------------------|----------------------|
| 2016 | | | | |
| Cash and cash equivalents | \$ 984,795 | \$ 50,527 | \$ - | \$ 1,035,322 |
| Collateral held for securities loaned | 213,629 | - | - | 213,629 |
| Public equities | 7,069,873 | - | - | 7,069,873 |
| Derivatives | 43 | - | - | 43 |
| Fixed income | 1,655,649 | 163,371 | 70,642 | 1,889,662 |
| Real estate | 6,741,245 | - | - | 6,741,245 |
| Natural resources | 2,300,633 | - | - | 2,300,633 |
| Private equities | 6,363,481 | - | - | 6,363,481 |
| Absolute return | 5,155,970 | - | - | 5,155,970 |
| Assets held by other trustees | 176,310 | - | 15,048 | 191,358 |
| Other | 342,571 | 28,444 | - | 371,015 |
| Total | 31,004,199 | 242,342 | 85,690 | 31,332,231 |
| Hospitals' funds invested in the University's Merged Pool | (1,918,412) | 1,310,047 | 608,365 | - |
| INVESTMENTS AT FAIR VALUE | \$ 29,085,787 | \$ 1,552,389 | \$ 694,055 | \$ 31,332,231 |
| 2015 | | | | |
| Cash and cash equivalents | \$ 1,300,474 | \$ 59,560 | \$ - | \$ 1,360,034 |
| Collateral held for securities loaned | 110,087 | - | - | 110,087 |
| Public equities | 6,971,378 | - | - | 6,971,378 |
| Derivatives | 58,992 | - | - | 58,992 |
| Fixed income | 1,350,768 | 160,088 | 69,313 | 1,580,169 |
| Real estate | 6,439,576 | - | - | 6,439,576 |
| Natural resources | 2,018,832 | - | - | 2,018,832 |
| Private equities | 6,833,087 | - | - | 6,833,087 |
| Absolute return | 5,529,102 | - | - | 5,529,102 |
| Assets held by other trustees | 192,811 | - | 16,079 | 208,890 |
| Other | 273,674 | 15,355 | - | 289,029 |
| Total | 31,078,781 | 235,003 | 85,392 | 31,399,176 |
| Hospitals' funds invested in the University's Merged Pool | (2,312,541) | 1,434,886 | 877,655 | - |
| INVESTMENTS AT FAIR VALUE | \$ 28,766,240 | \$ 1,669,889 | \$ 963,047 | \$ 31,399,176 |

VALUATION METHODOLOGY

To the extent available, Stanford's investments are recorded at fair value based on quoted prices in active markets on a trade-date basis. Stanford'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 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, 2016 and 2015, 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.

Stanford exercises due diligence in assessing the policies, procedures, and controls implemented by its external investment managers and believes its 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 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, such as 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, Stanford considers various factors to estimate fair value, such as, but not limited to, 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, Stanford 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 and restricted cash. 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 8*).

Collateral held for securities loaned is generally received in the form of cash and cash equivalents and is reinvested for income in cash equivalent vehicles. These investments are recorded at amortized cost, which approximates fair value (see *Note 10*).

Public equities are investments valued based on quoted market prices (and exchange rates, if applicable) on the last trading date of the principal market on or before August 31. They include investments that are directly held as well as commingled funds which invest in publicly traded equities. 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 Stanford 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 total return swaps 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 primarily include investments that are actively traded fixed income securities or mutual funds.

Real estate represents directly owned real estate, interests in long-term ground leases and other real estate interests held through limited partnerships. The fair value of real estate directly owned by Stanford, 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 the NAV 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 the NAV reported by the external investment managers and is adjusted as described under *Valuation Methodology* above.

Private equities are investments primarily in venture capital and leveraged buyout strategies. Distributions from these investments are received through liquidation of the underlying assets. 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 the NAV reported by the external investment managers and is adjusted as described under *Valuation Methodology* above.

Assets held by other trustees generally represent Stanford's residual interest in split interest agreements where the University, SHC or LPCH 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.

Other investments are typically non-public investments such as preferred stocks and convertible notes. The fair value of these types of direct investments is valued as described under *Valuation Methodology* above.

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 8*).

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 U.S. government and sovereign obligations, government agency obligations, investment grade corporate bonds and certain limited marketable securities.

Privately negotiated over-the-counter (OTC) derivatives such as forward currency contracts, total return swaps, and interest rate swaps are typically classified as Level 2 (see *Note 8*). 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, or 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 Stanford's alternative investments and are classified as Level 3 as the inputs are not observable.

The following tables summarize Stanford's investment assets within the fair value hierarchy and asset categories at August 31, 2016 and 2015, in thousands of dollars:

| | LEVEL 1 | LEVEL 2 | LEVEL 3 | TOTAL |
|---|---------------------|---------------------|---|----------------------|
| 2016 | | | | |
| Cash and cash equivalents | \$ 1,010,174 | \$ 25,148 | \$ - | \$ 1,035,322 |
| Collateral held for securities loaned | - | 213,629 | - | 213,629 |
| Public equities | 2,308,666 | 189 | 3,045 | 2,311,900 |
| Derivatives | - | 43 | - | 43 |
| Fixed income | 165,292 | 1,724,370 | - | 1,889,662 |
| Real estate | 47,805 | - | 4,956,210 | 5,004,015 |
| Natural resources | 488,596 | - | 208,655 | 697,251 |
| Private equities | 603 | - | 71,875 | 72,478 |
| Absolute return | - | - | 25,587 | 25,587 |
| Assets held by other trustees | - | - | 191,358 | 191,358 |
| Other | 200 | - | 366,342 | 366,542 |
| INVESTMENTS SUBJECT TO FAIR VALUE LEVELING | \$ 4,021,336 | \$ 1,963,379 | \$ 5,823,072 | 11,807,787 |
| | | | Investments measured using Net Asset Value ¹ | 19,524,444 |
| | | | CONSOLIDATED TOTAL | \$ 31,332,231 |

| | LEVEL 1 | LEVEL 2 | LEVEL 3 | TOTAL |
|---|---------------------|---------------------|---|----------------------|
| 2015 | | | | |
| Cash and cash equivalents | \$ 1,259,787 | \$ 100,247 | \$ - | \$ 1,360,034 |
| Collateral held for securities loaned | - | 110,087 | - | 110,087 |
| Public equities | 2,901,037 | 3,208 | - | 2,904,245 |
| Derivatives | 66,601 | (7,609) | - | 58,992 |
| Fixed income | 169,129 | 1,411,040 | - | 1,580,169 |
| Real estate | 103,194 | - | 4,537,715 | 4,640,909 |
| Natural resources | 237,536 | - | 269,963 | 507,499 |
| Private equities | 10,655 | 53 | 64,025 | 74,733 |
| Absolute return | - | - | - | - |
| Assets held by other trustees | - | - | 208,890 | 208,890 |
| Other | 814 | - | 284,217 | 285,031 |
| INVESTMENTS SUBJECT TO FAIR VALUE LEVELING | \$ 4,748,753 | \$ 1,617,026 | \$ 5,364,810 | 11,730,589 |
| | | | Investments measured using Net Asset Value ¹ | 19,668,587 |
| | | | CONSOLIDATED TOTAL | \$ 31,399,176 |

¹ Entities may estimate the fair value of certain investments by using NAV as a practical expedient as of the measurement date. Investments measured under this method are not categorized in the fair value hierarchy. The fair value amounts of such investments are presented for reconciliation purposes.

The University manages the majority of SHC's and LPCH's investments, including their investments in the Merged Pool (MP). SHC's investments in the MP were \$1.3 billion and \$1.4 billion, and LPCH's investments in the MP were \$608 million and \$878 million at August 31, 2016 and 2015, respectively.

For reporting purposes, assets and liabilities of investment entities that are controlled by the University are consolidated. The following table represents the fair value of consolidated investment entity assets and liabilities at August 31, 2016 and 2015, in thousands of dollars:

| | 2016 | 2015 |
|--|-------------------|------------------|
| Consolidated investment entity assets | \$ 166,378 | \$ 121,478 |
| Consolidated investment entity liabilities | (65,550) | (65,800) |
| CONSOLIDATED INVESTMENT ENTITY NET ASSETS | \$ 100,828 | \$ 55,678 |

SUMMARY OF LEVEL 3 INVESTMENT ACTIVITIES AND TRANSFERS

The following tables present the activities for Level 3 investments for the years ended August 31, 2016 and 2015, in thousands of dollars:

| FAIR VALUE MEASUREMENTS USING SIGNIFICANT UNOBSERVABLE INPUTS (LEVEL 3) | BEGINNING BALANCE AS OF SEPTEMBER 1, 2015 | PURCHASES | SALES AND MATURITIES | NET REALIZED AND UNREALIZED | | TRANSFERS OUT* | ENDING BALANCE AS OF AUGUST 31, 2016 |
|--|--|-------------------|-------------------------|-----------------------------------|------------------|--------------------|---|
| | | | | GAINS (LOSSES) | TRANSFERS IN* | | |
| Public equities | \$ - | \$ 1,740 | \$ - | \$ 462 | \$ 843 | \$ - | \$ 3,045 |
| Real estate | 4,537,715 | 68,596 | (20,470) | 370,364 | 29 | (24) | 4,956,210 |
| Natural resources | 269,963 | 13,584 | (48,283) | (8,397) | - | (18,212) | 208,655 |
| Private equities | 64,025 | 1,629 | (1,233) | 7,483 | - | (29) | 71,875 |
| Absolute return | - | 4,938 | - | 2,437 | 18,212 | - | 25,587 |
| Assets held by other trustees | 208,890 | 3,913 | (11,477) | (7,839) | - | (2,129) | 191,358 |
| Other | 284,217 | 144,724 | (88,529) | 25,906 | 24 | - | 366,342 |
| TOTAL | \$ 5,364,810 | \$ 239,124 | \$ (169,992) | \$ 390,416 | \$ 19,108 | \$ (20,394) | \$ 5,823,072 |

| FAIR VALUE MEASUREMENTS USING SIGNIFICANT UNOBSERVABLE INPUTS (LEVEL 3) | BEGINNING BALANCE AS OF SEPTEMBER 1, 2014 | PURCHASES | SALES AND MATURITIES | NET REALIZED AND UNREALIZED | | TRANSFERS OUT* | ENDING BALANCE AS OF AUGUST 31, 2015 |
|--|--|-------------------|-------------------------|-----------------------------------|---------------|-------------------|---|
| | | | | GAINS (LOSSES) | TRANSFERS IN* | | |
| Public equities | \$ 10,127 | \$ 114 | \$ (7,239) | \$ (2,944) | \$ - | \$ (58) | \$ - |
| Fixed income | 3,960 | - | (3,955) | (5) | - | - | - |
| Real estate | 3,882,828 | 57,273 | (51,523) | 649,137 | - | - | 4,537,715 |
| Natural resources | 282,518 | 93,161 | (4,932) | (100,784) | - | - | 269,963 |
| Private equities | 40,988 | 10,087 | (2,143) | 15,093 | - | - | 64,025 |
| Absolute return | 4,594 | - | (1,698) | (2,896) | - | - | - |
| Assets held by other trustees | 202,130 | 26,468 | (14,594) | (5,114) | - | - | 208,890 |
| Other | 222,582 | 123,077 | (85,233) | 23,733 | 58 | - | 284,217 |
| TOTAL | \$ 4,649,727 | \$ 310,180 | \$ (171,317) | \$ 576,220 | \$ 58 | \$ (58) | \$ 5,364,810 |

*Transfers in (out) are primarily due to reclassification of investments between asset classes.

Net realized and unrealized gains (losses) in the tables above are included in the *Consolidated Statements of Activities* primarily as increases or decreases in reinvested gains by level of restriction. For the years ended August 31, 2016 and 2015, the change in unrealized gains (losses) for Level 3 investments still held at August 31, 2016 and 2015 was \$392 million and \$617 million, respectively.

Transfers in (out) include situations where observable inputs have changed. 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, 2016 and 2015.

LEVEL 3 INVESTMENT VALUATION TECHNIQUES AND SIGNIFICANT UNOBSERVABLE INPUTS

The following table summarizes the significant unobservable inputs and valuation methodologies for Level 3 investments as of August 31, 2016 and 2015, in thousands of dollars.

For each investment category and respective valuation technique, the range of the significant unobservable input is dependent on the nature and characteristics of the investment. The input range and weighted average values may vary at each balance sheet date.

| INVESTMENT CATEGORIES | FAIR VALUE ¹ | VALUATION TECHNIQUE | SIGNIFICANT UNOBSERVABLE INPUTS | RANGE | | IMPACT TO VALUATION FROM AN INCREASE IN INPUT ² |
|--|-------------------------|----------------------|--|-------|-------|--|
| | | | | MIN | MAX | |
| 2016 | | | | | | |
| Real estate | \$ 4,493,680 | Discounted cash flow | Discount rate | 4.8% | 20.0% | Decrease |
| | | | Capitalization rate | 4.5% | 9.0% | Decrease |
| Natural resources | 6,769 | Market comparables | Weights ascribed to market comparables | 20.0% | 50.0% | N/A |
| Other | 353,581 | Market comparables | Recent transactions | N/A | N/A | N/A |
| TOTAL AMOUNT WITH SIGNIFICANT UNOBSERVABLE INPUTS | | \$ 4,854,030 | | | | |
| 2015 | | | | | | |
| Real estate | \$ 4,065,049 | Discounted cash flow | Discount rate | 5.3% | 11.0% | Decrease |
| | | | Capitalization rate | 5.3% | 7.5% | Decrease |
| Natural resources | 84,671 | Market comparables | Weights ascribed to market comparables | 20.0% | 50.0% | N/A |
| Other | 272,860 | Market comparables | Recent transactions | N/A | N/A | N/A |
| TOTAL AMOUNT WITH SIGNIFICANT UNOBSERVABLE INPUTS | | \$ 4,422,580 | | | | |

¹ \$969.0 and \$942.2 million of Level 3 investments at August 31, 2016 and 2015, respectively, are valued using third-party valuations, other market comparables or recent transactions as an approximation of fair value.

² Unless otherwise noted, this column represents the directional change in the fair value of the Level 3 investments that would result from an increase to the corresponding unobservable input. A decrease to the unobservable input would have the opposite effect. Significant increases and decreases in these unobservable inputs in isolation could result in significantly higher or lower fair value measurements.

INVESTMENT-RELATED COMMITMENTS

Stanford is obligated under certain 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 including redemption terms, notice periods, and remaining life for all related alternative investments at August 31, 2016, in thousands of dollars:

| ASSET CLASS | FAIR VALUE | UNFUNDED COMMITMENT | REMAINING LIFE (YEARS) | REDEMPTION TERMS |
|-------------------|---------------------|---------------------|------------------------|---|
| Public equities | \$ 4,756,157 | \$ 80,000 | 0 to 5 | Generally, lock-up provisions ranging from 0 to 5 years. After initial lock up expires, redemptions are available on a rolling basis and require 30 to 120 days prior notification. |
| Real estate | 1,808,876 | 1,019,904 | 0 to 13 | Not eligible for redemption |
| Natural resources | 1,776,971 | 1,136,733 | 0 to 15 | Not eligible for redemption |
| Private equities | 6,362,821 | 3,208,213 | 0 to 16 | Not eligible for redemption |
| Absolute return | 5,155,970 | 973,401 | 0 to 9 | Generally, lock-up provisions ranging from 0 to 5 years. After initial lock up expires, redemptions are available on a rolling basis and require 30 to 90 days prior notification. |
| TOTAL | \$19,860,795 | \$ 6,418,251 | | |

OFFSETS TO INVESTMENT-RELATED ASSETS AND LIABILITIES

Financial instruments with off-balance sheet risk such as derivatives and securities lending agreements are subject to counterparty credit risk. Stanford seeks to control this risk in various ways, such as entering into transactions with quality counterparties, establishing and monitoring credit limits, and requiring collateral in certain situations.

Stanford generally maintains master netting agreements and collateral agreements with its counterparties. These agreements provide Stanford the right, in the event of default by the counterparty, such as bankruptcy or a failure to pay or perform, to net a counterparty's rights and obligations under the agreement and to liquidate and offset collateral against any net amount owed by the counterparty.

In the *Consolidated Statements of Financial Position*, derivatives are reflected on a net basis at fair value within the "derivatives" category of "investments". The fair value of assets and obligations associated with collateral under security lending agreements are presented on a gross basis within the "collateral held for securities loaned" category of "investments" as described in this note and in "liabilities associated with investments" as described in *Note 10*, respectively. The following table presents information about the offsetting of these instruments and related collateral amounts as of August 31, 2016 and 2015, in thousands of dollars:

| | GROSS AMOUNTS OF ASSETS AND LIABILITIES | GROSS AMOUNTS OFFSET IN THE CONSOLIDATED STATEMENTS OF FINANCIAL POSITION | NET AMOUNTS OF ASSETS AND LIABILITIES PRESENTED IN THE CONSOLIDATED STATEMENTS OF FINANCIAL POSITION | GROSS AMOUNTS NOT OFFSET IN CONSOLIDATED STATEMENTS OF FINANCIAL POSITION | | |
|---------------------------------|---|---|--|---|---------------------------------------|---------------|
| | | | | FINANCIAL INSTRUMENTS ³ | CASH COLLATERAL RECEIVED ³ | NET AMOUNT |
| 2016 | | | | | | |
| Assets: | | | | | | |
| Derivatives ¹ | \$ 545 | \$ (502) | \$ 43 | \$ - | \$ - | \$ 43 |
| TOTAL | 545 | (502) | 43 | - | - | 43 |
| Liabilities: | | | | | | |
| Derivatives ¹ | 502 | (502) | - | - | - | - |
| Securities lending ² | 213,629 | - | 213,629 | 213,629 | - | - |
| TOTAL | \$ 214,131 | \$ (502) | \$ 213,629 | \$ 213,629 | \$ - | \$ - |
| 2015 | | | | | | |
| Assets: | | | | | | |
| Derivatives ¹ | \$ 70,000 | \$ (11,008) | 58,992 | - | \$ 20,008 | 38,984 |
| TOTAL | 70,000 | (11,008) | 58,992 | - | 20,008 | 38,984 |
| Liabilities: | | | | | | |
| Derivatives ¹ | 11,008 | (11,008) | - | - | - | - |
| Securities lending ² | 110,087 | - | 110,087 | 110,087 | - | - |
| TOTAL | \$ 121,095 | \$ (11,008) | \$ 110,087 | \$ 110,087 | \$ - | \$ - |

¹ Gross derivative assets less gross derivative liabilities are presented as "derivatives" in the investment assets table.

² Refer to Note 10 for details.

³ These amounts are limited to the derivative asset balance and accordingly, do not include any excess collateral received.

INVESTMENT RETURNS

Total investment returns for the years ended August 31, 2016 and 2015, in thousands of dollars, are as follows:

| | UNIVERSITY | SHC | LPCH | CONSOLIDATED |
|---|---------------------|------------------|------------------|---------------------|
| 2016 | | | | |
| Investment income | \$ 250,478 | \$ 15,595 | \$ 2,351 | \$ 268,424 |
| Net realized and unrealized gains | 939,185 | 27,254 | 34,820 | 1,001,259 |
| TOTAL INVESTMENT RETURNS | \$ 1,189,663 | \$ 42,849 | \$ 37,171 | \$ 1,269,683 |
| <i>Reconciliation to Statements of Activities:</i> | | | | |
| Total investment income distributed for operations | \$ 1,321,669 | \$ 1,361 | \$ 15,462 | \$ 1,338,492 |
| Increase in reinvested gains - unrestricted | 118,270 | 39,061 | 10,303 | 167,634 |
| Increase (decrease) in reinvested gains - temporarily restricted | (349,476) | 2,427 | 9,987 | (337,062) |
| Change in value of split interest agreements, net - temporarily restricted | 14,702 | - | 164 | 14,866 |
| Increase in reinvested gains - permanently restricted | 25,566 | - | - | 25,566 |
| Change in value of split interest agreements, net - permanently restricted | 18,053 | - | 1,255 | 19,308 |
| Adjusted for: | | | | |
| Returns on split interest agreements paid to beneficiaries - temporarily restricted | 13,187 | - | - | 13,187 |
| Returns on split interest agreements paid to beneficiaries - permanently restricted | 27,692 | - | - | 27,692 |
| TOTAL INVESTMENT RETURNS | \$ 1,189,663 | \$ 42,849 | \$ 37,171 | \$ 1,269,683 |
| 2015 | | | | |
| Investment income | \$ 228,617 | \$ 18,487 | \$ 2,400 | \$ 249,504 |
| Net realized and unrealized gains | 1,633,778 | 54,279 | 59,174 | 1,747,231 |
| TOTAL INVESTMENT RETURNS | \$ 1,862,395 | \$ 72,766 | \$ 61,574 | \$ 1,996,735 |
| <i>Reconciliation to Statements of Activities:</i> | | | | |
| Total investment income distributed for operations | \$ 1,276,463 | \$ 1,018 | \$ 14,266 | \$ 1,291,747 |
| Increase in reinvested gains - unrestricted | 644,855 | 67,544 | 33,323 | 745,722 |
| Increase (decrease) in reinvested gains - temporarily restricted | (89,655) | 4,204 | 14,549 | (70,902) |
| Change in value of split interest agreements, net - temporarily restricted | 2,449 | - | (254) | 2,195 |
| Increase in reinvested gains - permanently restricted | 1,760 | - | - | 1,760 |
| Change in value of split interest agreements, net - permanently restricted | (15,446) | - | (310) | (15,756) |
| Adjusted for: | | | | |
| Returns on split interest agreements paid to beneficiaries - temporarily restricted | 14,321 | - | - | 14,321 |
| Returns on split interest agreements paid to beneficiaries - permanently restricted | 27,648 | - | - | 27,648 |
| TOTAL INVESTMENT RETURNS | \$ 1,862,395 | \$ 72,766 | \$ 61,574 | \$ 1,996,735 |

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 11).

FUTURE MINIMUM RENTAL INCOME

As part of its investment portfolio, Stanford 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, 2016, in thousands of dollars, is as follows:

| YEAR ENDING AUGUST 31 | FUTURE MINIMUM RENTAL INCOME | | | |
|-----------------------|------------------------------|------------------|-----------------|---------------------|
| | UNIVERSITY | SHC | LPCH | CONSOLIDATED |
| 2017 | \$ 111,183 | \$ 3,324 | \$ 1,426 | \$ 115,933 |
| 2018 | 111,026 | 3,010 | 1,020 | 115,056 |
| 2019 | 113,461 | 2,592 | 896 | 116,949 |
| 2020 | 112,507 | 1,699 | 629 | 114,835 |
| 2021 | 109,126 | 1,182 | 535 | 110,843 |
| Thereafter | 1,943,038 | 10,471 | 1,137 | 1,954,646 |
| TOTAL | \$ 2,500,341 | \$ 22,278 | \$ 5,643 | \$ 2,528,262 |

7. 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, 2016 and 2015, in thousands of dollars:

| | 2016 | 2015 |
|---|----------------------|----------------------|
| Merged Pool | \$ 25,337,941 | \$ 25,931,986 |
| Expendable Funds Pool | 3,752,886 | 3,666,479 |
| Endowment Income Funds Pool | 355,022 | 314,216 |
| Other investment pools | 96,643 | 100,649 |
| Specific investments | 5,569,894 | 5,046,147 |
| | <u>35,112,386</u> | <u>35,059,477</u> |
| Adjustments: | | |
| Amounts included in "cash and cash equivalents" in the <i>Statements of Financial Position</i> | (518,762) | (387,712) |
| Funds cross-invested in investment pools | (3,582,983) | (3,587,517) |
| Hospitals' funds not invested in the University's investment pools | 321,590 | 314,928 |
| TOTAL INVESTMENTS | \$ 31,332,231 | \$ 31,399,176 |

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 *Consolidated 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 *Consolidated 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, 2016 and 2015, the results of the EFP, in thousands of dollars, are as follows:

| | 2016 | 2015 |
|---|--------------------|------------------|
| Total investment return of the EFP | \$ 95,384 | \$ 159,143 |
| Less distributions to fund holders and operations | (144,158) | (143,087) |
| AMOUNTS ADDED TO (WITHDRAWN FROM) FFE | \$ (48,774) | \$ 16,056 |

8. Derivatives

Stanford, directly or through external investment managers on Stanford's behalf, 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 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, Stanford utilizes forward contracts and foreign currency options to manage exchange rate risk.

INVESTMENT-RELATED DERIVATIVES

The following table presents amounts for investment-related derivatives, including the notional amount, the fair values at August 31, 2016 and 2015, and gains and losses for the years ended August 31, 2016 and 2015, in thousands of dollars:

| | AS OF AUGUST 31, 2016 | | | YEAR ENDED AUGUST 31, 2016 |
|----------------------------|---------------------------------|--|---|---|
| | NOTIONAL AMOUNT ¹ | GROSS DERIVATIVE ASSETS ² | GROSS DERIVATIVE LIABILITIES ² | REALIZED AND UNREALIZED GAINS (LOSSES) ³ |
| Interest-rate contracts | \$ - | \$ - | \$ - | \$ (596) |
| Foreign exchange contracts | 222,815 | 545 | 502 | (1,589) |
| Equity contracts | - | - | - | 1,163 |
| TOTAL | \$ 222,815 | \$ 545 | \$ 502 | \$ (1,022) |

| | AS OF AUGUST 31, 2015 | | | YEAR ENDED AUGUST 31, 2015 |
|----------------------------|---------------------------------|--|---|---|
| | NOTIONAL AMOUNT ¹ | GROSS DERIVATIVE ASSETS ² | GROSS DERIVATIVE LIABILITIES ² | REALIZED AND UNREALIZED GAINS (LOSSES) ³ |
| Interest-rate contracts | \$ 944,114 | \$ 69,816 | \$ - | \$ (67,001) |
| Foreign exchange contracts | 35,812 | 184 | 362 | 82,656 |
| Equity contracts | 144,552 | - | 10,646 | (12,432) |
| Credit contracts | - | - | - | 563 |
| TOTAL | \$ 1,124,478 | \$ 70,000 | \$ 11,008 | \$ 3,786 |

¹ The notional amount is representative of the volume and activity of the respective derivative type during the years ended August 31, 2016 and 2015.

² Gross derivative assets less gross derivative liabilities of \$43 thousand and \$59.0 million as of August 31, 2016 and 2015, respectively, are presented as "derivatives" on the investment table in Note 6.

³ Gains (losses) on derivatives are included in the Statements of Activities as "increase in reinvested gains" in "non-operating activities".

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, 2016, the University had interest rate exchange agreements related to \$97.0 million of the outstanding balance of the CEFA Series S bonds in variable rate mode (see *Note 11*). The agreements, which have a weighted average interest rate of 3.68%, 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 \$16.7 million at August 31, 2016 and 2015, respectively, and is included in the *Consolidated 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, 2016 and 2015 (see *Note 11*).

At August 31, 2016, SHC had interest rate exchange agreements expiring through November 2051 (see *Note 11*). The agreements require SHC to 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. There was \$36.2 million and \$1.7 million cash collateral required to be posted with counterparties at August 31, 2016 and 2015, respectively.

The following table presents amounts for debt-related derivatives including the notional amount, the fair values at August 31, 2016 and 2015, and gains and losses for the years ended August 31, 2016 and 2015, in thousands of dollars:

| | AS OF AUGUST 31, 2016 | | YEAR ENDED AUGUST 31, 2016 | AS OF AUGUST 31, 2015 | | YEAR ENDED AUGUST 31, 2015 |
|---|---------------------------------|---|-----------------------------------|---------------------------------|---|-----------------------------------|
| | NOTIONAL AMOUNT ¹ | GROSS DERIVATIVE LIABILITIES ² | UNREALIZED LOSSES ³ | NOTIONAL AMOUNT ¹ | GROSS DERIVATIVE LIABILITIES ² | UNREALIZED LOSSES ³ |
| Debt-related interest- rate contracts: | | | | | | |
| University | \$ 97,000 | \$ 52,222 | \$ (16,638) | \$ 97,000 | \$ 35,584 | \$ (5,127) |
| SHC | 576,250 | 331,334 | (115,958) | 576,925 | 215,376 | (59,392) |
| TOTAL | \$ 673,250 | \$ 383,556 | \$ (132,596) | \$ 673,925 | \$ 250,960 | \$ (64,519) |

¹ The notional amount is representative of the volume and activity of the respective derivative type during the years ended August 31, 2016 and 2015.

² Fair value is measured using Level 2 inputs as defined in Note 6. Amounts are included in the Statements of Financial Position in "accounts payable and accrued expenses" and discussed more fully in Note 11.

³ Losses on derivatives are included in the Statements of Activities as "swap interest and change in value of swap agreements" in "non-operating activities".

9. Plant Facilities

Plant facilities, net of accumulated depreciation, at August 31, 2016 and 2015, in thousands of dollars, are as follows:

| | UNIVERSITY | SHC | LPCH | CONSOLIDATED |
|--|---------------------|---------------------|---------------------|---------------------|
| 2016 | | | | |
| Land and improvements | \$ 517,256 | \$ 67,816 | \$ 91,630 | \$ 676,702 |
| Buildings and building improvements | 5,817,312 | 1,321,441 | 465,945 | 7,604,698 |
| Furniture, fixtures and equipment | 1,706,663 | 944,194 | 310,498 | 2,961,355 |
| Utilities | 832,467 | - | - | 832,467 |
| Construction in progress | 475,327 | 1,383,279 | 981,974 | 2,840,580 |
| | 9,349,025 | 3,716,730 | 1,850,047 | 14,915,802 |
| Less accumulated depreciation | (4,180,305) | (1,314,850) | (420,731) | (5,915,886) |
| PLANT FACILITIES, NET OF ACCUMULATED DEPRECIATION | \$ 5,168,720 | \$ 2,401,880 | \$ 1,429,316 | \$ 8,999,916 |
| 2015 | | | | |
| Land and improvements | \$ 513,352 | \$ 67,541 | \$ 90,898 | \$ 671,791 |
| Buildings and building improvements | 5,336,952 | 1,237,008 | 410,740 | 6,984,700 |
| Furniture, fixtures and equipment | 1,617,442 | 867,053 | 294,969 | 2,779,464 |
| Utilities | 830,370 | - | - | 830,370 |
| Construction in progress | 381,745 | 937,050 | 645,953 | 1,964,748 |
| | 8,679,861 | 3,108,652 | 1,442,560 | 13,231,073 |
| Less accumulated depreciation | (3,884,297) | (1,185,187) | (364,283) | (5,433,767) |
| PLANT FACILITIES, NET OF ACCUMULATED DEPRECIATION | \$ 4,795,564 | \$ 1,923,465 | \$ 1,078,277 | \$ 7,797,306 |

At August 31, 2016, \$1.7 billion, \$811.5 million, and \$137.1 million of fully depreciated plant facilities were still in use by the University, SHC, and LPCH, respectively, and were included in plant facilities and accumulated depreciation.

10. Liabilities Associated with Investments

At August 31, 2016 and 2015, liabilities associated with investments, in thousands of dollars, are as follows:

| | LEVEL 1 | LEVEL 2 | LEVEL 3 | TOTAL |
|---|------------------|-------------------|------------------|-------------------|
| 2016 | | | | |
| Collateral deposits for certain securities loaned temporarily to brokers ¹ | \$ - | \$ 213,629 | \$ - | \$ 213,629 |
| Pending trades of securities | 57,406 | - | - | 57,406 |
| Debt of investment entity | - | 65,550 | - | 65,550 |
| Forward sale and purchase agreements | - | - | 17,263 | 17,263 |
| LIABILITIES ASSOCIATED WITH INVESTMENTS | \$ 57,406 | \$ 279,179 | \$ 17,263 | \$ 353,848 |
| 2015 | | | | |
| Collateral deposits for certain securities loaned temporarily to brokers ¹ | \$ - | \$ 110,087 | \$ - | \$ 110,087 |
| Pending trades of securities | 14,431 | - | - | 14,431 |
| Debt of investment entity | - | 65,800 | - | 65,800 |
| Forward sale and purchase agreements | - | - | 22,338 | 22,338 |
| LIABILITIES ASSOCIATED WITH INVESTMENTS | \$ 14,431 | \$ 175,887 | \$ 22,338 | \$ 212,656 |

¹ The estimated fair value of securities loaned to brokers at August 31, 2016 and 2015 was \$205.1 million and \$106.3 million, respectively.

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 equal to a minimum of 102% of the fair market value of the security loaned. The University also has obligations related to pending trades of securities purchased but not settled.

The University also holds controlling interests in several investment entities which are consolidated in the financial statements. The investment assets of these entities are included in "investments" in the *Consolidated Statements of Financial Position*. At August 31, 2016 and 2015, an investment entity held debt of \$65.6 million and \$65.8 million, respectively, where the University is ultimately liable for principal should the entity default (see *Note 6*).

In addition, the University is party to certain forward sale and purchase agreements.

11. Notes and Bonds Payable

Notes and bonds payable for the University, SHC, and LPCH at August 31, 2016 and 2015, in thousands of dollars, are presented in the table below. 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 or each other.

| | YEAR OF MATURITY | EFFECTIVE INTEREST RATE * 2016/2015 | OUTSTANDING PRINCIPAL | |
|--|------------------|--|-----------------------|---------------------|
| | | | 2016 | 2015 |
| UNIVERSITY: | | | | |
| Tax-exempt: | | | | |
| CEFA Fixed Rate Revenue Bonds: | | | | |
| Series S | 2040 | 3.18% | \$ 30,210 | \$ 30,210 |
| Series T | 2023-2039 | 3.66%-4.30% | 188,900 | 188,900 |
| Series U | 2021-2046 | 1.75%-4.25% | 1,167,205 | 996,855 |
| CEFA Variable Rate Revenue Bonds and Notes: | | | | |
| Series L | 2017-2023 | 0.62%/0.01% | 60,148 | 69,988 |
| Series S | 2040-2051 | 0.30%-0.47%/0.09%-0.20% | 141,200 | 141,200 |
| 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 | 2019 | 4.79% | 400,000 | 400,000 |
| Stanford University Series 2012 | 2042 | 4.01% | 143,235 | 143,235 |
| Stanford University Series 2013 | 2044 | 3.56% | 150,115 | 150,115 |
| Stanford University Series 2014 | 2054 | 4.25% | 150,000 | 150,000 |
| Stanford University Series 2015 | 2047 | 3.46% | 250,000 | 250,000 |
| Other | 2031 | Various | 484 | 484 |
| Variable Rate Notes: | | | | |
| Revolving Credit Facilities | 2019 | 0.72%/0.42% | 65,800 | 41,200 |
| University notes and bonds payable | | | 2,947,297 | 2,762,187 |
| Unamortized original issue premiums/discounts, net | | | 323,320 | 257,391 |
| UNIVERSITY TOTAL | | | \$ 3,270,617 | \$ 3,019,578 |
| SHC: | | | | |
| CHFFA Fixed Rate Revenue Bonds: | | | | |
| 2008 Series A-1 | 2040 | 5.14% | \$ 67,835 | \$ 68,510 |
| 2008 Series A-2 | 2040 | 5.25% | 100,350 | 101,350 |
| 2008 Series A-3 | 2040 | 5.49% | 81,140 | 81,940 |
| 2010 Series A | 2031 | 5.46% | 124,875 | 130,220 |
| 2010 Series B | 2036 | 5.20% | 146,710 | 146,710 |
| 2012 Series A | 2051 | 5.00% | 340,000 | 340,000 |
| 2012 Series B | 2023 | 4.71% | 47,445 | 52,880 |
| 2015 Series A | 2054 | 4.82% | 100,000 | 100,000 |
| CHFFA Variable Rate Revenue Bonds: | | | | |
| 2008 Series B | 2045 | 0.55%/0.07% | 168,200 | 168,200 |
| 2012 Series C | 2051 | 0.78%/0.15% | 60,000 | 60,000 |
| 2012 Series D | 2051 | 0.75%/0.53% | 100,000 | 100,000 |
| 2015 Series B | 2054 | 0.90%/0.68% | 75,000 | 75,000 |
| Other | 2024 | 4.25%/5.95% | 4,870 | 5,567 |
| SHC notes and bonds payable | | | 1,416,425 | 1,430,377 |
| Unamortized original issue premiums/discounts, net | | | 46,320 | 49,102 |
| SHC TOTAL | | | \$ 1,462,745 | \$ 1,479,479 |
| LPCH: | | | | |
| CHFFA Fixed Rate Revenue Bonds: | | | | |
| 2008 Series A | 2016 | 1.41% | \$ - | \$ 30,340 |
| 2008 Series B | 2016 | 1.41% | - | 30,340 |
| 2008 Series C | 2016 | 1.41% | - | 29,610 |
| 2012 Series A | 2044-2051 | 4.93% | 200,000 | 200,000 |
| 2012 Series B | 2016-2027 | 4.70% | 42,195 | 44,600 |
| 2014 Series A | 2025-2043 | 4.74% | 100,000 | 100,000 |
| 2016 Series A | 2016-2033 | 4.87% | 73,675 | - |
| 2016 Series B | 2052-2055 | 4.99% | 100,000 | - |
| CHFFA Variable Rate Revenue Bonds: | | | | |
| 2014 Series B | 2034-2043 | 0.66%/0.52% | 100,000 | 100,000 |
| LPCH notes and bonds payable | | | 615,870 | 534,890 |
| Unamortized original issue premiums/discounts, net | | | 52,536 | 24,796 |
| LPCH TOTAL | | | \$ 668,406 | \$ 559,686 |
| CONSOLIDATED TOTAL | | | \$ 5,401,768 | \$ 5,058,743 |

*Exclusive of interest rate exchange agreements (see Note 8).

All bonds held at August 31, 2016 and 2015 are classified as Level 2 in the fair value hierarchy as described in *Note 6*. The fair value of the University's, SHC's, and LPCH's debt instruments at August 31, 2016 and 2015, in thousands of dollars, are as follows:

| | 2016 | 2015 |
|--------------|---------------------|---------------------|
| University | \$ 3,792,935 | \$ 3,193,736 |
| SHC | 1,585,366 | 1,546,143 |
| LPCH | 711,846 | 569,300 |
| TOTAL | \$ 6,090,147 | \$ 5,309,179 |

The University borrows at tax-exempt rates through the California Educational Facilities Authority (CEFA), a conduit issuer. 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. SHC and LPCH borrow at tax-exempt rates through the California Health Facilities Financing Authority (CHFFA). CHFFA debt is a general obligation of each of the hospitals. Payments of principal and interest on SHC's and LPCH's bonds are collateralized by a pledge of their respective revenues. Although CHFFA is the issuer, each hospital is responsible for the repayment of their respective tax-exempt debt.

The University's long-term ratings of AAA/Aaa/AAA were affirmed in May and June 2016 by Standard & Poor's, Moody's Investors Service and Fitch Ratings, respectively. In September and October 2016, SHC's long-term ratings were affirmed by Standard & Poor's, Moody's Investors Service and Fitch Ratings at AA-/Aa3/AA, respectively. In March 2016, LPCH's long-term ratings were affirmed by Standard & Poor's, Moody's Investors Service and Fitch Ratings at AA-/Aa3/AA, respectively, and the 2016 Notes were assigned the same ratings.

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, SHC and LPCH may cause the redemption of the bonds, in whole or in part, prior to the stated maturities.

UNIVERSITY

Debt issuances and repayment activity

In August 2016, the University entered into a \$250.0 million unsecured revolving credit facility. Drawdowns from the revolving credit facility bear interest at a floating rate equal to the applicable LIBOR rate plus a specified margin. There were no amounts outstanding at August 31, 2016.

In June 2016, CEFA Series U-7 bonds were issued in the amount of \$170.3 million plus an original issue premium of \$79.7 million. The bonds bear interest at a coupon rate of 5.00%, mature on June 1, 2046, and have a yield of 2.71%. Proceeds will be used to finance facilities and infrastructure.

In October 2015, CEFA Series L (third tranche) in the amount of \$9.8 million matured and was repaid. In October 2014, CEFA Series L (first and second tranches) in the amounts of \$5.1 million and \$8.8 million, respectively, matured and were repaid.

In July 2015, the University called and prepaid \$250.0 million of the taxable Series 2009A bonds due in 2016.

In May 2015, the University entered into a \$250.0 million unsecured revolving credit facility. Drawdowns from the revolving credit facility bear interest at a floating rate equal to the applicable LIBOR rate plus a specified margin. At August 31, 2016 and 2015, \$65.8 million and \$41.2 million were outstanding, respectively.

In April 2015, the University issued taxable fixed rate Series 2015 bonds in the amount of \$250.0 million. The bonds bear interest at a rate of 3.46% and mature on May 1, 2047. Proceeds can be used for general corporate purposes, including financing and refinancing capital projects.

The University's taxable and tax-exempt commercial paper authorized borrowing capacity was \$500 million and \$300 million, respectively, at both August 31, 2016 and 2015. There were no amounts outstanding at August 31, 2016 and 2015.

Variable rate debt subject to remarketing or tender

The University had \$201.3 million of revenue bonds in variable rate mode outstanding at August 31, 2016. 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.

Letters of credit

In December 2010, the University entered into a credit agreement and established a letter of credit facility under which the bank agreed to issue standby letters of credit in a principal amount not to exceed \$50.0 million. In June 2016, the University increased the facility to \$65.0 million. At August 31, 2016, irrevocable standby letters of credit of \$43.9 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 8*; (2) \$28.7 million to serve as security for workers' compensation deductible insurance arrangements; and (3) \$0.2 million for other purposes. No amounts have been drawn on these letters of credit at August 31, 2016.

SHC

Debt issuances and repayment activity

In June 2015, CHFFA, for the benefit of SHC, issued two series of revenue bonds in the aggregate principal amount of \$175.0 million (the "2015 Bonds"). The 2015 Bonds were comprised of \$100.0 million of 2015 Series A bonds, and \$75.0 million of Series B bonds. Proceeds of the 2015 Series A and B bonds will be used to finance a portion of the Renewal Project (see *Note 19*).

Variable rate debt subject to remarketing or tender

At August 31, 2016, SHC had \$403.2 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 the commercial paper rate for each commercial paper period 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 and 2015 Series B bonds are also in a floating index mode with monthly interest rate resets. The 2012 Series D and 2015 Series B bonds are not subject to remarketing or tender until May 13, 2020 and June 28, 2024, respectively.

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 any 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 any remaining bonds. SHC maintains sufficient liquidity to provide for the full and timely purchase price of any bonds tendered in the event of a failed remarketing.

Letters of credit

At August 31, 2016, SHC had irrevocable standby letters of credit in the aggregate amount of \$24.1 million posted with certain beneficiaries in the following amounts and for the following respective purposes: (i) \$22.0 million to serve as security for the workers' compensation self-insurance arrangement and (ii) \$2.1 million to serve as security deposits for certain construction projects being undertaken by SHC including the Renewal Project (see *Note 19*). No amounts have been drawn on these letters of credit at August 31, 2016 and 2015.

LPCH

Debt issuances and repayment activity

In March 2016, CHFFA, on behalf of LPCH, issued two series of revenue bonds (Series A and B) in the aggregate par amount of \$177.0 million. A portion of the proceeds were used to redeem the 2008 Series A, B and C revenue bonds, and the remaining amount will be used to finance a portion of the Renewal Project and to pay for the cost of issuance.

Letters of credit

At August 31, 2016, LPCH had irrevocable standby letters of credit in the aggregate amount of \$9.0 million posted with certain beneficiaries in the following amounts and for the following respective purposes: (i) \$7.6 million to serve as security for the workers' compensation self-insurance arrangement and (ii) \$1.4 million to serve as security deposits for certain construction projects being undertaken by LPCH including the Renewal Project (see *Note 19*). No amounts have been drawn on these letters of credit at August 31, 2016 and 2015.

INTEREST

Stanford's 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:

| | UNIVERSITY | SHC | LPCH | CONSOLIDATED |
|---|------------------|------------------|------------------|-------------------|
| 2016 | | | | |
| Interest expense, gross | \$ 110,300 | \$ 63,365 | \$ 21,861 | \$ 195,526 |
| Less: | | | | |
| Interest income earned on unspent proceeds | (409) | - | - | (409) |
| Interest capitalized as a cost of construction | (3,717) | (24,190) | (10,897) | (38,804) |
| Interest expense on Series 2009A bonds which is classified as an investment expense | (13,230) | - | - | (13,230) |
| INTEREST EXPENSE, NET | \$ 92,944 | \$ 39,175 | \$ 10,964 | \$ 143,083 |
| 2015 | | | | |
| Interest expense, gross | \$ 111,806 | \$ 60,281 | \$ 18,907 | \$ 190,994 |
| Less: | | | | |
| Interest income earned on unspent proceeds | (245) | - | - | (245) |
| Interest capitalized as a cost of construction | (3,543) | (20,232) | (4,110) | (27,885) |
| Interest expense on Series 2009A bonds which is classified as an investment expense | (22,350) | - | - | (22,350) |
| INTEREST EXPENSE, NET | \$ 85,668 | \$ 40,049 | \$ 14,797 | \$ 140,514 |

The University and SHC use interest rate exchange agreements to manage the interest rate exposure of their debt portfolios. As described in *Note 1*, settlements (net cash payments less receipts) under the interest rate exchange agreements are recorded in the *Consolidated Statements of Activities* in "swap interest and change in value of swap agreements" for the University and in "other operating expenses" for SHC. University net payments on interest rate exchange agreements were \$3.3 million and \$3.5 million for the years ended August 31, 2016 and 2015, respectively. SHC net payments on interest rate exchange agreements were \$13.5 million and \$14.1 million for the years ended August 31, 2016 and 2015, respectively.

PRINCIPAL PAYMENTS

At August 31, 2016, scheduled principal payments on notes, bonds and capital lease obligations, in thousands of dollars, are as follows:

| YEAR ENDING AUGUST 31 | PRINCIPAL PAYMENTS | | | |
|---|---------------------|---------------------|-------------------|---------------------|
| | UNIVERSITY | SHC | LPCH | CONSOLIDATED |
| 2017 Variable debt subject to remarketing | \$ 201,348 | \$ 228,200 | \$ - | \$ 429,548 |
| 2017 Other | 4 | 13,756 | 5,695 | 19,455 |
| 2018 | - | 13,873 | 5,800 | 19,673 |
| 2019 | 465,800 | 15,067 | 5,845 | 486,712 |
| 2020 | - | 14,821 | 6,135 | 20,956 |
| 2021 | 124,115 | 16,656 | 6,365 | 147,136 |
| Thereafter | 2,156,030 | 1,114,052 | 586,030 | 3,856,112 |
| TOTAL | \$ 2,947,297 | \$ 1,416,425 | \$ 615,870 | \$ 4,979,592 |

12. Endowments

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, which includes endowed lands, is comprised of pure endowment funds, 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. Accordingly, term endowments 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.

Stanford 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 the fair value of the fund equals or exceeds historic value. The aggregate amount by which fair value was below historic value was \$13.6 million and \$5.4 million at August 31, 2016 and 2015, respectively.

Endowment funds by net asset classification at August 31, 2016 and 2015, in thousands of dollars, are as follows:

| | UNRESTRICTED | TEMPORARILY RESTRICTED | PERMANENTLY RESTRICTED | TOTAL |
|---------------------------------------|----------------------|---------------------------|---------------------------|----------------------|
| 2016 | | | | |
| University endowment | | | | |
| Donor-restricted endowment funds | \$ (13,597) | \$ 6,119,400 | \$ 6,067,654 | \$ 12,173,457 |
| Funds functioning as endowment | 10,224,673 | - | - | 10,224,673 |
| University endowment | 10,211,076 | 6,119,400 | 6,067,654 | 22,398,130 |
| SHC donor-restricted endowment funds | - | 10,723 | 7,894 | 18,617 |
| LPCH donor-restricted endowment funds | - | 94,936 | 211,348 | 306,284 |
| TOTAL ENDOWMENT FUNDS | \$ 10,211,076 | \$ 6,225,059 | \$ 6,286,896 | \$ 22,723,031 |
| 2015 | | | | |
| University endowment | | | | |
| Donor-restricted endowment funds | \$ (5,394) | \$ 6,466,064 | \$ 5,720,633 | \$ 12,181,303 |
| Funds functioning as endowment | 10,041,654 | - | - | 10,041,654 |
| University endowment | 10,036,260 | 6,466,064 | 5,720,633 | 22,222,957 |
| SHC donor-restricted endowment funds | - | 10,666 | 7,694 | 18,360 |
| LPCH donor-restricted endowment funds | - | 103,166 | 204,405 | 307,571 |
| TOTAL ENDOWMENT FUNDS | \$ 10,036,260 | \$ 6,579,896 | \$ 5,932,732 | \$ 22,548,888 |

Most of Stanford'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. 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 regularly by Stanford Management Company.

UNIVERSITY

Changes in the University's endowment, excluding pledges, for the years ended August 31, 2016 and 2015, in thousands of dollars, are as follows:

| | UNRESTRICTED | TEMPORARILY RESTRICTED | PERMANENTLY RESTRICTED | TOTAL |
|--|----------------------|---------------------------|---------------------------|----------------------|
| 2016 | | | | |
| Endowment, beginning of year | \$ 10,036,260 | \$ 6,466,064 | \$ 5,720,633 | \$ 22,222,957 |
| Investment returns: | | | | |
| Earned income | 170,659 | - | - | 170,659 |
| Unrealized and realized gains (losses) | 1,087,635 | (353,178) | 25,335 | 759,792 |
| Total investment returns | 1,258,294 | (353,178) | 25,335 | 930,451 |
| Amounts distributed for operations | (1,132,105) | - | - | (1,132,105) |
| Gifts, transfers and other changes in endowment: | | | | |
| Current year gifts and pledge payments | 2,487 | 15,061 | 217,248 | 234,796 |
| Transfers of prior year gifts | 21,220 | 125 | 60,347 | 81,692 |
| EFP funds withdrawn from the endowment | (48,774) | - | - | (48,774) |
| Other funds invested in (withdrawn from) the endowment, net | 73,694 | (8,672) | 44,091 | 109,113 |
| Total gifts, transfers and other changes in endowment | 48,627 | 6,514 | 321,686 | 376,827 |
| Total net increase (decrease) in endowment | 174,816 | (346,664) | 347,021 | 175,173 |
| ENDOWMENT, END OF YEAR | \$ 10,211,076 | \$ 6,119,400 | \$ 6,067,654 | \$ 22,398,130 |
| 2015 | | | | |
| Endowment, beginning of year | \$ 9,405,641 | \$ 6,574,426 | \$ 5,465,939 | \$ 21,446,006 |
| Investment returns: | | | | |
| Earned income | 197,943 | - | - | 197,943 |
| Unrealized and realized gains (losses) | 1,454,383 | (100,618) | (334) | 1,353,431 |
| Total investment returns | 1,652,326 | (100,618) | (334) | 1,551,374 |
| Amounts distributed for operations | (1,058,025) | - | - | (1,058,025) |
| Gifts, transfers and other changes in endowment: | | | | |
| Current year gifts and pledge payments | 1,712 | 1,937 | 148,683 | 152,332 |
| Transfers of prior year gifts | - | 160 | 59,742 | 59,902 |
| EFP funds invested in the endowment | 16,056 | - | - | 16,056 |
| Other funds invested in (withdrawn from) the endowment, net | 18,550 | (9,841) | 46,603 | 55,312 |
| Total gifts, transfers and other changes in endowment | 36,318 | (7,744) | 255,028 | 283,602 |
| Total net increase (decrease) in endowment | 630,619 | (108,362) | 254,694 | 776,951 |
| ENDOWMENT, END OF YEAR | \$ 10,036,260 | \$ 6,466,064 | \$ 5,720,633 | \$ 22,222,957 |

Approximately 16% of the University's endowment is invested in real estate on Stanford's lands, including the Stanford Research Park. This portion of the endowment includes the present value of ground leases, and rental properties that have been developed on Stanford lands. The net operating income from these properties is distributed each year for University operations.

Through the combination of investment strategy and payout policy, the University strives 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.

SHC AND LPCH

The endowments of SHC and LPCH are intended to generate investment income to support their current operating and strategic initiatives. The Hospitals invest the majority of their endowments in the University's MP. Their endowments are subject to the same investment and spending strategies that the University employs. The Hospitals' Boards of Directors have approved payout policies which provide for annual amounts to be distributed for current use. "Amounts distributed for operations" in the tables below represents SHC's and LPCH's current year endowment payout spent for designated purposes during fiscal years 2016 and 2015.

SHC

Changes in SHC's endowment, excluding pledges, for the years ended August 31, 2016 and 2015, in thousands of dollars, are as follows:

| | UNRESTRICTED | TEMPORARILY RESTRICTED | PERMANENTLY RESTRICTED | TOTAL |
|------------------------------------|--------------|---------------------------|---------------------------|------------------|
| 2016 | | | | |
| Endowments, beginning of year | \$ - | \$ 10,666 | \$ 7,694 | \$ 18,360 |
| Investment returns: | | | | |
| Earned income | - | 491 | - | 491 |
| Unrealized and realized losses | - | (21) | - | (21) |
| Total investment returns | - | 470 | - | 470 |
| Amounts distributed for operations | - | (413) | - | (413) |
| Gifts and pledge payments | - | - | 200 | 200 |
| Total net increase in endowments | - | 57 | 200 | 257 |
| ENDOWMENT, END OF YEAR | \$ - | \$ 10,723 | \$ 7,894 | \$ 18,617 |

2015

| | | | | |
|------------------------------------|-------------|------------------|-----------------|------------------|
| Endowments, beginning of year | \$ - | \$ 10,293 | \$ 7,692 | \$ 17,985 |
| Investment returns: | | | | |
| Earned income | - | 478 | - | 478 |
| Unrealized and realized gains | - | 314 | - | 314 |
| Total investment returns | - | 792 | - | 792 |
| Amounts distributed for operations | - | (419) | - | (419) |
| Gifts and pledge payments | - | - | 2 | 2 |
| Total net increase in endowments | - | 373 | 2 | 375 |
| ENDOWMENT, END OF YEAR | \$ - | \$ 10,666 | \$ 7,694 | \$ 18,360 |

LPCH

Changes in LPCH's endowment, excluding pledges, for the years ended August 31, 2016 and 2015, in thousands of dollars, are as follows:

| | UNRESTRICTED | TEMPORARILY RESTRICTED | PERMANENTLY RESTRICTED | TOTAL |
|---|--------------|---------------------------|---------------------------|-------------------|
| 2016 | | | | |
| Endowments, beginning of year | \$ - | \$ 103,166 | \$ 204,405 | \$ 307,571 |
| Investment returns: | | | | |
| Earned income | - | 16,134 | - | 16,134 |
| Unrealized and realized gains (losses) | - | (8,746) | 1,255 | (7,491) |
| Total investment returns | - | 7,388 | 1,255 | 8,643 |
| Amounts distributed for operations | - | (15,462) | - | (15,462) |
| Gifts and pledge payments | - | - | 5,763 | 5,763 |
| Other | - | (156) | (75) | (231) |
| Total net increase (decrease) in endowments | - | (8,230) | 6,943 | (1,287) |
| ENDOWMENT, END OF YEAR | \$ - | \$ 94,936 | \$ 211,348 | \$ 306,284 |
| 2015 | | | | |
| Endowments, beginning of year | \$ - | \$ 105,530 | \$ 203,342 | \$ 308,872 |
| Investment returns: | | | | |
| Earned income | - | 15,162 | - | 15,162 |
| Unrealized and realized losses | - | (2,202) | (310) | (2,512) |
| Total investment returns | - | 12,960 | (310) | 12,650 |
| Amounts distributed for operations | - | (14,266) | - | (14,266) |
| Gifts and pledge payments | - | 2 | 850 | 852 |
| Other | - | (1,060) | 523 | (537) |
| Total net increase (decrease) in endowments | - | (2,364) | 1,063 | (1,301) |
| ENDOWMENT, END OF YEAR | \$ - | \$ 103,166 | \$ 204,405 | \$ 307,571 |

13. Gifts and Pledges

Gifts and pledges reported for financial statement purposes are recorded on the accrual basis. The Office of Development (OOD), which is the primary fundraising agent for the University and SHC, reports total gifts based on contributions received in cash or property during the fiscal year. Lucile Packard Foundation for Children's Health (LPFCH) is the primary community fundraising agent for LPCH and the pediatric faculty and programs at the University's SOM. The following summarizes gifts and pledges reported for the years ended August 31, 2016 and 2015, per the *Consolidated Statements of Activities*, in thousands of dollars:

| | UNIVERSITY | SHC | LPCH | CONSOLIDATED |
|---|---------------------|------------------|-------------------|---------------------|
| 2016 | | | | |
| Current year gifts in support of operations | \$ 250,769 | \$ 1,776 | \$ 5,740 | \$ 258,285 |
| Donor advised funds, net | 21,783 | - | - | 21,783 |
| Current year gifts not included in operations | 2,381 | - | - | 2,381 |
| Temporarily restricted gifts and pledges, net | 284,923 | 20,716 | 129,868 | 435,507 |
| Permanently restricted gifts and pledges, net | 761,992 | 200 | 7,669 | 769,861 |
| TOTAL | \$ 1,321,848 | \$ 22,692 | \$ 143,277 | \$ 1,487,817 |
| 2015 | | | | |
| Current year gifts in support of operations | \$ 233,572 | \$ 2,049 | \$ 5,554 | \$ 241,175 |
| Donor advised funds, net | 66,734 | - | - | 66,734 |
| Current year gifts not included in operations | 1,655 | - | - | 1,655 |
| Temporarily restricted gifts and pledges, net | 250,808 | 52,333 | 70,810 | 373,951 |
| Permanently restricted gifts and pledges, net | 208,206 | 2 | 850 | 209,058 |
| TOTAL | \$ 760,975 | \$ 54,384 | \$ 77,214 | \$ 892,573 |

14. Functional Expenses

Expenses for the years ended August 31, 2016 and 2015 are categorized on a functional basis as follows, in thousands of dollars:

| | UNIVERSITY | SHC | LPCH | ELIMINATIONS | CONSOLIDATED |
|---------------------------------------|---------------------|---------------------|---------------------|---------------------|---------------------|
| 2016 | | | | | |
| Instruction and departmental research | \$ 1,733,100 | \$ - | \$ - | \$ - | \$ 1,733,100 |
| Organized research - direct costs | 1,092,696 | - | - | - | 1,092,696 |
| Patient services | - | 3,553,997 | 1,232,211 | (860,086) | 3,926,122 |
| Auxiliary activities | 1,019,270 | - | - | - | 1,019,270 |
| Administration and general | 410,659 | 384,711 | 120,601 | (50,669) | 865,302 |
| Student services | 242,693 | - | - | - | 242,693 |
| Libraries | 151,531 | - | - | - | 151,531 |
| Development | 102,528 | 10,911 | 10,868 | (9,979) | 114,328 |
| SLAC construction | 162,133 | - | - | - | 162,133 |
| TOTAL EXPENSES | \$ 4,914,610 | \$ 3,949,619 | \$ 1,363,680 | \$ (920,734) | \$ 9,307,175 |
| 2015 | | | | | |
| Instruction and departmental research | \$ 1,611,953 | \$ - | \$ - | \$ - | \$ 1,611,953 |
| Organized research - direct costs | 1,068,039 | - | - | - | 1,068,039 |
| Patient services | - | 2,973,295 | 1,141,571 | (796,944) | 3,317,922 |
| Auxiliary activities | 960,981 | - | - | - | 960,981 |
| Administration and general | 396,950 | 305,910 | 119,105 | (51,803) | 770,162 |
| Student services | 219,733 | - | - | - | 219,733 |
| Libraries | 154,323 | - | - | - | 154,323 |
| Development | 91,927 | 9,566 | 13,308 | (8,814) | 105,987 |
| SLAC construction | 141,792 | - | - | - | 141,792 |
| TOTAL EXPENSES | \$ 4,645,698 | \$ 3,288,771 | \$ 1,273,984 | \$ (857,561) | \$ 8,350,892 |

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, patient care provided by the SOM faculty, and other activities.

15. University Retirement Plans

The University provides retirement benefits through both defined benefit and defined contribution 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). Employer contributions are based on a percentage of participant annual compensation, participant contributions and years of service. 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 \$145.8 million and \$137.5 million for the years ended August 31, 2016 and 2015, respectively.

DEFINED BENEFIT PLANS

The University provides retirement and postretirement medical and other benefits through 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 *Consolidated Statements of Financial Position* as "accrued pension and postretirement benefit obligations". These plans 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. While the SRAP is closed to new participants, certain employees continue to accrue benefits. Contributions to the plan are made in accordance with the Employee Retirement Income Security Act (ERISA) based on actuarially determined amounts sufficient to meet the benefits to be paid to plan participants.

Faculty Retirement Incentive Program

The University 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, 2016 and 2015, there were no program assets. The University funds benefit payouts as they are incurred.

Postretirement Benefit Plan

The University provides 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 and meeting specific years of service and age criteria. Retiree health plans are paid for, in part, by retiree contributions, which are adjusted annually. The University's subsidy varies depending on whether the retiree is covered under the grandfathered 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:

| | SRAP | FRIP | PRBP | TOTAL |
|---|--------------------|---------------------|---------------------|---------------------|
| 2016 | | | | |
| Fair value of plan assets, beginning of year | \$ 269,969 | \$ - | \$ 194,978 | 464,947 |
| Change in plan assets: | | | | |
| Actual return on plan assets | 34,625 | - | 14,670 | 49,295 |
| Employer contributions | - | 6,014 | 17,451 | 23,465 |
| Plan participants' contributions | - | - | 12,111 | 12,111 |
| Benefits and plan expenses paid | (18,920) | (6,014) | (28,636) * | (53,570) |
| FAIR VALUE OF PLAN ASSETS, END OF YEAR | 285,674 | - | 210,574 | 496,248 |
| Benefit obligation, beginning of year | 316,835 | 207,481 | 626,467 | 1,150,783 |
| Change in projected benefit obligation: | | | | |
| Service cost | 2,794 | 12,637 | 23,677 | 39,108 |
| Interest cost | 12,124 | 7,947 | 27,538 | 47,609 |
| Plan participants' contributions | - | - | 12,111 | 12,111 |
| Actuarial loss (gain) | 33,730 | (51,362) | (127,114) | (144,746) |
| Benefits and plan expenses paid | (18,920) | (6,014) | (28,636) * | (53,570) |
| BENEFIT OBLIGATION, END OF YEAR | 346,563 | 170,689 | 534,043 | 1,051,295 |
| NET LIABILITY RECOGNIZED IN THE STATEMENTS OF FINANCIAL POSITION | \$ (60,889) | \$ (170,689) | \$ (323,469) | \$ (555,047) |

* Net of Medicare subsidy

| | | | | |
|---|--------------------|---------------------|---------------------|---------------------|
| 2015 | | | | |
| Fair value of plan assets, beginning of year | \$ 301,314 | \$ - | \$ 203,109 | \$ 504,423 |
| Change in plan assets: | | | | |
| Actual return on plan assets | (6,231) | - | (7,067) | (13,298) |
| Employer contributions | - | 4,782 | 16,205 | 20,987 |
| Plan participants' contributions | - | - | 11,173 | 11,173 |
| Benefits and plan expenses paid | (25,114) | (4,782) | (28,442) * | (58,338) |
| FAIR VALUE OF PLAN ASSETS, END OF YEAR | 269,969 | - | 194,978 | 464,947 |
| Benefit obligation, beginning of year | 316,165 | 197,596 | 556,898 | 1,070,659 |
| Change in projected benefit obligation: | | | | |
| Service cost | 3,003 | 12,326 | 20,079 | 35,408 |
| Interest cost | 11,003 | 6,923 | 22,471 | 40,397 |
| Plan amendments | 1,565 | - | - | 1,565 |
| Plan participants' contributions | - | - | 11,173 | 11,173 |
| Actuarial loss (gain) | 10,213 | (4,582) | 44,288 | 49,919 |
| Benefits and plan expenses paid | (25,114) | (4,782) | (28,442) * | (58,338) |
| BENEFIT OBLIGATION, END OF YEAR | 316,835 | 207,481 | 626,467 | 1,150,783 |
| NET LIABILITY RECOGNIZED IN THE STATEMENTS OF FINANCIAL POSITION | \$ (46,866) | \$ (207,481) | \$ (431,489) | \$ (685,836) |

* Net of Medicare subsidy

The accumulated benefit obligation for the SRAP was \$344.7 million and \$314.8 million at August 31, 2016 and 2015, respectively.

Net periodic benefit expense and non-operating activities related to the Plans for the years ended August 31, 2016 and 2015, in thousands of dollars, includes the following components:

| | SRAP | FRIP | PRBP | TOTAL |
|---|------------------|--------------------|--------------------|---------------------|
| 2016 | | | | |
| Service cost | \$ 2,794 | \$ 12,637 | \$ 23,677 | \$ 39,108 |
| Interest cost | 12,124 | 7,947 | 27,538 | 47,609 |
| Expected return on plan assets | (15,349) | - | (13,648) | (28,997) |
| Amortization of: | | | | |
| Prior service cost | 396 | - | 849 | 1,245 |
| Actuarial loss | 1,047 | 4,747 | 8,625 | 14,419 |
| NET PERIODIC BENEFIT EXPENSE | 1,012 | 25,331 | 47,041 | 73,384 |
| Net actuarial loss (gain) | 14,454 | (51,362) | (128,136) | (165,044) |
| Amortization of: | | | | |
| Prior service cost | (396) | - | (849) | (1,245) |
| Actuarial loss | (1,047) | (4,747) | (8,625) | (14,419) |
| TOTAL AMOUNTS RECOGNIZED IN NON-OPERATING ACTIVITIES | 13,011 | (56,109) | (137,610) | (180,708) |
| TOTAL AMOUNT RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE AND NON-OPERATING ACTIVITIES | \$ 14,023 | \$ (30,778) | \$ (90,569) | \$ (107,324) |
| 2015 | | | | |
| Service cost | \$ 3,003 | \$ 12,326 | \$ 20,079 | \$ 35,408 |
| Interest cost | 11,003 | 6,923 | 22,471 | 40,397 |
| Expected return on plan assets | (18,660) | - | (15,233) | (33,893) |
| Amortization of: | | | | |
| Prior service cost | 277 | - | 2,545 | 2,822 |
| Actuarial loss | - | 5,570 | 5,192 | 10,762 |
| NET PERIODIC BENEFIT EXPENSE (INCOME) | (4,377) | 24,819 | 35,054 | 55,496 |
| Net actuarial loss (gain) | 35,104 | (4,582) | 66,588 | 97,110 |
| Prior service cost | 1,565 | - | - | 1,565 |
| Amortization of: | | | | |
| Prior service cost | (277) | - | (2,545) | (2,822) |
| Actuarial loss | - | (5,570) | (5,192) | (10,762) |
| TOTAL AMOUNTS RECOGNIZED IN NON-OPERATING ACTIVITIES | 36,392 | (10,152) | 58,851 | 85,091 |
| TOTAL AMOUNT RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE AND NON-OPERATING ACTIVITIES | \$ 32,015 | \$ 14,667 | \$ 93,905 | \$ 140,587 |

Cumulative amounts recognized in non-operating activities, but not yet recognized in net periodic benefit expense in the *Consolidated Statements of Activities*, are presented in the following table for the years ended August 31, 2016 and 2015, in thousands of dollars:

| | SRAP | FRIP | PRBP | TOTAL |
|--|------------------|------------------|-------------------|-------------------|
| 2016 | | | | |
| Prior service cost | \$ 1,206 | \$ - | \$ - | \$ 1,206 |
| Net actuarial loss | 70,349 | 32,429 | 59,660 | 162,438 |
| ACCUMULATED PLAN BENEFIT COSTS NOT YET RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE | | | | |
| | \$ 71,555 | \$ 32,429 | \$ 59,660 | \$ 163,644 |
| 2015 | | | | |
| Prior service cost | \$ 1,602 | \$ - | \$ 849 | \$ 2,451 |
| Net actuarial loss | 56,942 | 88,538 | 196,421 | 341,901 |
| ACCUMULATED PLAN BENEFIT COSTS NOT YET RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE | | | | |
| | \$ 58,544 | \$ 88,538 | \$ 197,270 | \$ 344,352 |

The prior service costs and net actuarial loss expected to be amortized from non-operating activities to net periodic benefit expense in fiscal year 2017, in thousands of dollars, are as follows:

| | SRAP | FRIP | PRBP | TOTAL |
|--------------------|----------|--------|--------|----------|
| Prior service cost | \$ 390 | \$ - | \$ - | \$ 390 |
| Net actuarial loss | \$ 1,508 | \$ 870 | \$ 464 | \$ 2,842 |

ACTUARIAL ASSUMPTIONS

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

| | SRAP | | FRIP | | PRBP | |
|----------------------------------|-------|-------|-------|-------|-------|-------|
| | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 |
| BENEFIT OBLIGATIONS | | | | | | |
| Discount rate | 3.15% | 4.00% | 3.15% | 3.93% | 3.56% | 4.46% |
| Covered payroll growth rate | 3.00% | 3.00% | 4.26% | 4.45% | N/A | N/A |
| NET PERIODIC BENEFIT COST | | | | | | |
| Discount rate | 4.00% | 3.64% | 3.93% | 3.59% | 4.46% | 4.10% |
| Expected returns on plan assets | 6.00% | 6.50% | N/A | N/A | 7.00% | 7.50% |
| Covered payroll growth rate | 3.00% | 3.00% | 4.45% | 4.45% | N/A | N/A |

In 2014, the Society of Actuaries issued a new mortality table (RP-2014) and a new mortality improvement (projection) scale that recognized increases in life expectancy. In selecting its assumptions for determining the benefit obligations as of August 31, 2015, the University adopted a modified version of the RP-2014 mortality table and a projection scale based on the 2014 Trustees Report of the Social Security Administration (SSA). The use of the new mortality table and projection scale resulted in an increase of approximately \$20.5 million, \$3.9 million, and \$84.0 million to the SRAP, FRIP and PRBP benefit obligations as of August 31, 2015, respectively.

The expected long-term rate of return on asset assumptions for the SRAP and PRBP plans is 6.00% and 7.00%, respectively. The assumption is used in determining the expected returns on plan assets, a component of net periodic benefit expense (income), representing the expected return for the upcoming fiscal year on plan assets. This assumption is developed based on 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 benefit expense (income) over the service or 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, 2016, a 7.00% annual rate of increase in the per capita cost of covered health care was assumed for calendar year 2016, declining gradually to 4.50% by 2038 and remaining at this rate thereafter. Health care cost trend rate assumptions have a significant effect on the amounts reported for the health care plans.

If the assumed health care cost trend were increased or decreased by 1%, the impact on the PRBP service and interest cost and the accumulated obligation are as follows, in thousands of dollars:

| | 1% INCREASE IN HEALTH CARE COST TREND RATE | 1% DECREASE IN HEALTH CARE COST TREND RATE |
|--|--|--|
| Effect on PRBP total service and interest cost | \$ 12,339 | \$ (9,263) |
| Effect on accumulated PRBP obligation | \$ 94,641 | \$ (74,809) |

EXPECTED CONTRIBUTIONS

The University expects to contribute \$11.4 million to the FRIP, \$5.0 million to the SRAP and does not expect to contribute to the PRBP during the fiscal year ending August 31, 2017.

EXPECTED BENEFIT PAYMENTS

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

| YEAR ENDING AUGUST 31 | SRAP | FRIP | PRBP | |
|-----------------------|-----------|-----------|----------------------------------|---|
| | | | EXCLUDING MEDICARE SUBSIDY | EXPECTED MEDICARE PART D SUBSIDY |
| 2017 | \$ 27,633 | \$ 11,439 | \$ 21,177 | \$ 3,838 |
| 2018 | 25,022 | 13,621 | 22,644 | 4,171 |
| 2019 | 24,486 | 10,281 | 23,970 | 4,515 |
| 2020 | 24,940 | 10,548 | 25,367 | 4,875 |
| 2021 | 24,197 | 10,836 | 26,812 | 5,248 |
| 2022 - 2026 | 108,085 | 58,827 | 157,131 | 32,079 |

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, 2016, the University did not have concentrations of risk in any single entity, counterparty, sector, industry or country.

PLAN ASSETS AND ALLOCATIONS

Current U.S. GAAP defines a hierarchy of valuation inputs for the determination of the fair value of plan assets as described in *Note 6*. As of August 31, 2016 and 2015, all of the assets of the PRBP and substantially all of the assets of the SRAP were categorized as Level 1 investments. The fair value of plan assets by asset category, in thousands of dollars, at August 31, 2016 and 2015 and actual allocations and weighted-average target allocations at August 31, 2016 are as follows:

| | 2016 | 2015 | 2016 ACTUAL ALLOCATION | 2016 TARGET ALLOCATION |
|--|-------------------|-------------------|---------------------------|---------------------------|
| SRAP: | | | | |
| Cash and cash equivalents | \$ 1,829 | \$ 1,179 | 1% | 0% |
| Public equities | 114,544 | 105,361 | 40% | 41% |
| Fixed income | 169,171 | 163,205 | 59% | 59% |
| Private equities | 130 | 224 | <1% | 0% |
| TOTAL | 285,674 | 269,969 | 100% | 100% |
| PRBP: | | | | |
| Public equities | 157,937 | 145,070 | 75% | 75% |
| Fixed income | 52,637 | 49,908 | 25% | 25% |
| TOTAL | 210,574 | 194,978 | 100% | 100% |
| TOTAL FAIR VALUE OF PLAN ASSETS | \$ 496,248 | \$ 464,947 | | |

16. SHC and LPCH Retirement Plans

SHC and LPCH provide retirement benefits through defined benefit and defined contribution retirement plans covering substantially all of its regular employees.

DEFINED CONTRIBUTION PLAN

The Hospitals offer a defined contribution plan to eligible employees. Employer contributions to the defined contribution retirement plan are based on a percentage of participant annual compensation, participant contributions and years of service. SHC and LPCH contributions under the plan, which are vested immediately to participants, were approximately \$79.2 million and \$63.7 million, and \$29.0 million and \$27.0 million for the years ended August 31, 2016 and 2015, respectively.

DEFINED BENEFIT PLANS

The Hospitals provide retirement and postretirement medical benefits through the SHC *Staff Pension Plan*, the SHC *Postretirement Medical Benefit Plan*, and the LPCH *Frozen Pension Plan*, collectively (the "Plans"). The obligations for the Plans, net of plan assets, are recorded in the *Consolidated Statements of Financial Position* as "accrued pension and postretirement benefit obligations". These plans are described more fully below.

Staff Pension Plan

Certain employees of SHC and LPCH are covered by the SHC *Staff Pension Plan* (the "Pension Plan"), a noncontributory, defined benefit pension plan. While the Pension Plan is closed to new participants, certain employees continue to accrue benefits. Benefits are based on years of service and the employee's compensation. Contributions to the plan are made in accordance with ERISA based on actuarially determined amounts sufficient to meet the benefits to be paid to plan participants. SHC and LPCH have an arrangement whereby SHC assumes the pension liability of the LPCH employees and previously leased employees. However, LPCH is required to reimburse SHC for the annual expense incurred for these employees and previously leased employees.

During the fiscal year ending August 31, 2016, the Pension Plan was amended to allow for a temporary lump sum window for deferred vested participants. During the window, eligible participants were contacted and offered an opportunity to take the lump sum value of their benefit, resulting in a \$17.2 million lump sum payment from the plan. This large lump sum payment triggered settlement accounting which required a \$6.1 million recognition of the plan's deferred losses, and also reduced the projected benefit obligation and assets by \$17.2 million.

Postretirement Medical Benefit Plan

SHC and LPCH provide health care benefits for certain retired employees through the SHC *Postretirement 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' subsidies vary depending on whether the retiree is covered under the grandfathered design or the defined dollar benefit design. Medicare supplement options are provided for retirees over age 65. LPCH reimburses SHC for costs related to this plan on a periodic basis.

Frozen Pension Plan

The remainder of certain other LPCH employees and previously leased employees not covered by the previously described plans are covered by a frozen noncontributory defined benefit pension plan (the "LPCH Frozen Pension Plan"). Benefits are based on years of service and the employee's

compensation. Contributions to the plan are made in accordance with ERISA based on actuarially determined amounts sufficient to meet the benefits to be paid to plan participants.

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 PENSION PLAN | PRMB | LPCH FROZEN PENSION PLAN |
|---|-----------------------|--------------------|-----------------------------|
| 2016 | | | |
| Fair value of plan assets, beginning of year | \$ 197,889 | \$ - | \$ 5,664 |
| Change in plan assets: | | | |
| Actual return on plan assets | 24,034 | - | 820 |
| Employer contributions | - | 6,029 | 422 |
| Plan participants' contributions | - | 1,043 | - |
| Benefits and plan expenses paid | (13,685) | (7,072) * | (516) |
| Plan settlements | (17,217) | - | - |
| FAIR VALUE OF PLAN ASSETS, END OF YEAR | 191,021 | - | 6,390 |
| Benefit obligation, beginning of year | 249,109 | 84,751 | 8,046 |
| Change in projected benefit obligation: | | | |
| Service cost | 1,644 | 2,052 | - |
| Interest cost | 9,806 | 3,295 | 311 |
| Plan participants' contributions | - | 1,043 | - |
| Actuarial loss (gain) | 26,827 | (9,714) | 859 |
| Benefits and plan expenses paid | (13,685) | (7,072) * | (516) |
| Plan settlements | (17,217) | - | - |
| Plan amendments | - | 2,289 | - |
| BENEFIT OBLIGATION, END OF YEAR | 256,484 | 76,644 | 8,700 |
| NET LIABILITY RECOGNIZED IN THE STATEMENTS OF FINANCIAL POSITION | \$ (65,463) | \$ (76,644) | \$ (2,310) |
| <i>* Net of Medicare subsidy</i> | | | |
| 2015 | | | |
| Fair value of plan assets, beginning of year | \$ 214,575 | \$ - | \$ 5,853 |
| Change in plan assets: | | | |
| Actual return on plan assets | (4,727) | - | (108) |
| Employer contributions | - | 4,914 | 300 |
| Plan participants' contributions | - | 1,038 | - |
| Benefits and plan expenses paid | (11,959) | (5,952) * | (381) |
| FAIR VALUE OF PLAN ASSETS, END OF YEAR | 197,889 | - | 5,664 |
| Benefit obligation, beginning of year | 245,402 | 84,616 | 7,749 |
| Change in projected benefit obligation: | | | |
| Service cost | 2,006 | 2,068 | - |
| Interest cost | 9,182 | 2,995 | 273 |
| Plan participants' contributions | - | 1,038 | - |
| Actuarial loss (gain) | 4,478 | (14) | 405 |
| Benefits and plan expenses paid | (11,959) | (5,952) * | (381) |
| BENEFIT OBLIGATION, END OF YEAR | 249,109 | 84,751 | 8,046 |
| NET LIABILITY RECOGNIZED IN THE STATEMENTS OF FINANCIAL POSITION | \$ (51,220) | \$ (84,751) | \$ (2,382) |
| <i>* Net of Medicare subsidy</i> | | | |

The net liability for the PRMB includes amounts for both SHC and LPCH employees and is recognized on the Hospitals' respective *Statements of Financial Position*. The table below presents the plan obligations for each entity as of August 31, 2016 and 2015, in thousands of dollars:

| | 2016 | | 2015 | |
|--------------|-----------|---------------|-----------|---------------|
| SHC | \$ | 59,895 | \$ | 66,547 |
| LPCH | | 16,749 | | 18,204 |
| TOTAL | \$ | 76,644 | \$ | 84,751 |

The accumulated benefit obligation for the Pension Plan and LPCH Frozen Pension Plan was \$254.1 million and \$247.0 million, and \$8.7 million and \$8.0 million at August 31, 2016 and 2015, respectively.

Net periodic benefit expense and non-operating activities related to the Plans for the years ended August 31, 2016 and 2015, in thousands of dollars, includes the following components:

| | STAFF PENSION PLAN | | PRMB | LPCH FROZEN PENSION PLAN |
|--|-----------------------|---------------|-----------|-----------------------------|
| 2016 | | | | |
| Service cost | \$ | 1,644 | \$ | 2,052 |
| Interest cost | | 9,806 | | 3,295 |
| Expected return on plan assets | | (11,909) | | - |
| Amortization of: | | | | |
| Prior service cost | | - | | 773 |
| Actuarial loss (gain) | | 2,272 | | (313) |
| Settlement loss | | 6,079 | | - |
| NET PERIODIC BENEFIT EXPENSE | | 7,892 | | 5,807 |
| Net actuarial loss (gain) | | 14,702 | | (9,714) |
| New prior service cost | | - | | 2,289 |
| Amortization of: | | | | |
| Prior service cost | | - | | (773) |
| Actuarial gain (loss) | | (2,272) | | 313 |
| Settlement loss | | (6,079) | | - |
| TOTAL AMOUNTS RECOGNIZED IN NON-OPERATING ACTIVITIES | | 6,351 | | (7,885) |
| TOTAL AMOUNT RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE AND NON- OPERATING ACTIVITIES | \$ | 14,243 | \$ | (2,078) |
| 2015 | | | | |
| Service cost | \$ | 2,006 | \$ | 2,068 |
| Interest cost | | 9,182 | | 2,995 |
| Expected return on plan assets | | (13,195) | | - |
| Amortization of: | | | | |
| Prior service cost | | - | | 815 |
| Actuarial loss (gain) | | 2,556 | | (338) |
| NET PERIODIC BENEFIT EXPENSE | | 549 | | 5,540 |
| Net actuarial loss (gain) | | 22,400 | | (14) |
| Amortization of: | | | | |
| Prior service cost | | - | | (815) |
| Actuarial gain (loss) | | (2,556) | | 338 |
| TOTAL AMOUNTS RECOGNIZED IN NON-OPERATING ACTIVITIES | | 19,844 | | (491) |
| TOTAL AMOUNT RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE AND NON- OPERATING ACTIVITIES | \$ | 20,393 | \$ | 5,049 |
| | | | | \$ |
| | | | | 786 |

The net periodic benefit expense and amounts recognized in non-operating activities for the PRMB include amounts for both SHC and LPCH employees and is recognized on the Hospitals' respective *Statements of Activities*. The table below presents the amount for each entity as of August 31, 2016 and 2015, in thousands of dollars:

| | SHC | LPCH | TOTAL |
|--|-------------------|-----------------|-------------------|
| 2016 | | | |
| Net periodic benefit expense | \$ 4,272 | \$ 1,535 | \$ 5,807 |
| Amounts recognized in non-operating activities | (6,271) | (1,614) | (7,885) |
| TOTAL AMOUNT RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE AND NON- OPERATING ACTIVITIES | \$ (1,999) | \$ (79) | \$ (2,078) |
| 2015 | | | |
| Net periodic benefit expense | \$ 4,189 | \$ 1,351 | \$ 5,540 |
| Amounts recognized in non-operating activities | (383) | (108) | (491) |
| TOTAL AMOUNT RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE AND NON- OPERATING ACTIVITIES | \$ 3,806 | \$ 1,243 | \$ 5,049 |

Cumulative amounts recognized in non-operating activities, but not yet recognized in net periodic benefit expense in the *Consolidated Statements of Activities*, are presented in the following table for the years ended August 31, 2016 and 2015, in thousands of dollars:

| | STAFF PENSION PLAN | PRMB | LPCH FROZEN PENSION PLAN |
|--|-----------------------|--------------------|-----------------------------|
| 2016 | | | |
| Prior service cost | \$ - | \$ 4,102 | \$ - |
| Net actuarial loss (gain) | 91,341 | (14,131) | 2,686 |
| ACCUMULATED PLAN BENEFIT COSTS NOT YET RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE | \$ 91,341 | \$ (10,029) | \$ 2,686 |
| 2015 | | | |
| Prior service cost | \$ - | \$ 2,586 | \$ - |
| Net actuarial loss (gain) | 84,990 | (4,730) | 2,457 |
| ACCUMULATED PLAN BENEFIT COSTS NOT YET RECOGNIZED IN NET PERIODIC BENEFIT EXPENSE | \$ 84,990 | \$ (2,144) | \$ 2,457 |

The prior service cost and net actuarial loss expected to be amortized from non-operating activities to net periodic benefit expense in fiscal year 2017, in thousands of dollars, are as follows:

| | STAFF PENSION PLAN | PRMB | LPCH FROZEN PENSION PLAN |
|---------------------------|-----------------------|----------|-----------------------------|
| Prior service cost | \$ - | \$ 674 | \$ - |
| Net actuarial loss (gain) | \$ 3,012 | \$ (915) | \$ 118 |

ACTUARIAL ASSUMPTIONS

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

| | STAFF PENSION PLAN | | PRMB | | LPCH FROZEN PENSION PLAN | |
|----------------------------------|--------------------|-------|-------|-------|--------------------------|-------|
| | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 |
| BENEFIT OBLIGATIONS | | | | | | |
| Discount rate | 3.32% | 4.20% | 3.07% | 4.01% | 3.18% | 4.03% |
| Covered payroll growth rate | 3.00% | 3.00% | N/A | N/A | N/A | N/A |
| NET PERIODIC BENEFIT COST | | | | | | |
| Discount rate | 4.20% | 3.84% | 4.01% | 3.65% | 4.03% | 3.66% |
| Expected return on plan assets | 6.50% | 7.00% | N/A | N/A | 5.50% | 6.25% |
| Covered payroll growth rate | 3.00% | 3.00% | N/A | N/A | N/A | N/A |

In 2014, the Society of Actuaries issued a new mortality table (RP-2014) and a new mortality improvement (projection) scale that recognized increases in life expectancy. In selecting its assumptions for determining the benefit obligations as of August 31, 2015, SHC and LPCH adopted a modified version of the RP-2014 mortality table and a projection scale based on the 2014 Trustees Report of the Social Security Administration (SSA). The use of the new mortality table and projection scale resulted in an increase of approximately \$18.4 million, \$6.4 million, and \$570 thousand to the Pension Plan, PRMB, and LPCH Frozen Pension Plan benefit obligations, as of August 31, 2015, respectively.

The expected long-term rate of return on asset assumptions for the Pension Plan and LPCH Frozen Pension Plan are 6.50% and 5.50%, respectively. The assumption is used in determining the expected returns on plan assets, a component of net periodic benefit expense (income), representing the expected return for the upcoming fiscal year on plan assets based on the calculated market-related value of plan assets. This assumption is developed based on 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 benefit expense (income) over the service or life expectancy of the plan participants, depending on the plan, provided such amounts exceed the accounting standards threshold.

To determine the accumulated PRMB obligation at August 31, 2016, a 7.00% annual rate of increase in the per capita cost of covered health care was assumed for calendar year 2016, declining gradually to 4.50% by 2038 and remaining at this rate thereafter. Health care cost trend rate assumptions have a significant effect on the amounts reported for the health care plan.

If the assumed health care cost trend were increased or decreased by 1%, the impact on PRMB service and interest cost and accumulated obligation are as follows, in thousands of dollars:

| | 1% INCREASE IN HEALTH CARE COST TREND RATE | 1% DECREASE IN HEALTH CARE COST TREND RATE |
|--|---|---|
| Effect on PRMB total service and interest cost | \$ 130 | \$ (119) |
| Effect on accumulated PRMB obligation | \$ 1,939 | \$ (1,789) |

EXPECTED CONTRIBUTIONS

SHC expects to contribute \$4.5 million to the PRMB during the fiscal year ending August 31, 2017. SHC and LPCH do not expect to contribute to the Pension Plan and LPCH Frozen Pension Plan during the fiscal year ending August 31, 2017.

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 | PRMB | | LPCH FROZEN PENSION PLAN |
|-----------------------|-----------------------|----------------------------------|--|-----------------------------|
| | | EXCLUDING MEDICARE SUBSIDY | EXPECTED MEDICARE PART D SUBSIDY | |
| 2017 | \$ 13,198 | \$ 5,760 | \$ 275 | \$ 668 |
| 2018 | 13,601 | 5,882 | 272 | 660 |
| 2019 | 13,976 | 6,040 | 268 | 656 |
| 2020 | 14,352 | 6,189 | 262 | 620 |
| 2021 | 14,663 | 6,300 | 254 | 581 |
| 2022 - 2026 | 75,142 | 30,301 | 1,111 | 2,594 |

INVESTMENT STRATEGY

SHC's and LPCH's investment strategies for the Pension Plan and LPCH Frozen 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. 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

SHC and LPCH 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, 2016, the Hospitals did not have concentrations of risk in any single entity, counterparty, sector, industry or country.

PLAN ASSETS AND ALLOCATIONS

Current U.S. GAAP defines a hierarchy of valuation inputs for the determination of the fair value of plan assets as described in *Note 6*. The Plans' assets measured at fair value at August 31, 2016 and 2015, are all categorized as Level 1 investments. The fair value of plan assets by asset category, in thousands of dollars, at August 31, 2016 and 2015 and actual allocations and weighted-average target allocations at August 31, 2016 are as follows:

| | 2016 | 2015 | 2016 ACTUAL ALLOCATION | 2016 TARGET ALLOCATION |
|----------------------------------|-------------------|-------------------|---------------------------|---------------------------|
| STAFF PENSION PLAN: | | | | |
| Cash and cash equivalents | \$ 1,075 | \$ 1,288 | 1% | 0% |
| Public equities | 94,079 | 95,829 | 49% | 50% |
| Fixed income | 95,867 | 100,772 | 50% | 50% |
| TOTAL | \$ 191,021 | \$ 197,889 | 100% | 100% |
| LPCH FROZEN PENSION PLAN: | | | | |
| Cash and cash equivalents | \$ 65 | \$ 40 | 1% | 0% |
| Public equities | 1,894 | 1,628 | 30% | 30% |
| Fixed income | 4,431 | 3,996 | 69% | 70% |
| TOTAL | \$ 6,390 | \$ 5,664 | 100% | 100% |

17. Operating Leases

Stanford leases certain equipment and facilities under operating leases expiring at various dates. Total rental expense under these leases for the years ended August 31, 2016 and 2015 was \$68.6 million and \$51.1 million, respectively, for the University, \$90.0 million and \$65.4 million, respectively, for SHC, and \$27.5 million and \$26.5 million, respectively, for LPCH.

Net minimum future operating lease payments for periods subsequent to August 31, 2016, in thousands of dollars, are as follows:

| YEAR ENDING AUGUST 31 | MINIMUM LEASE PAYMENTS | | | |
|-----------------------|------------------------|-------------------|------------------|-------------------|
| | UNIVERSITY | SHC | LPCH | CONSOLIDATED |
| 2017 | \$ 53,683 | \$ 78,325 | \$ 23,541 | \$ 155,549 |
| 2018 | 33,931 | 73,742 | 21,534 | 129,207 |
| 2019 | 26,867 | 68,716 | 19,001 | 114,584 |
| 2020 | 19,008 | 57,213 | 13,156 | 89,377 |
| 2021 | 17,670 | 49,483 | 3,920 | 71,073 |
| Thereafter | 83,488 | 128,962 | 7,200 | 219,650 |
| TOTAL | \$ 234,647 | \$ 456,441 | \$ 88,352 | \$ 779,440 |

18. Related Party Transactions

Members of the University, SHC, and LPCH boards and senior management may, from time to time, be associated, either directly or indirectly, with companies doing business with Stanford. For senior management, each entity requires annual disclosure of significant financial interests in, or employment or consulting relationships with, entities doing business with its relevant entity. These annual disclosures cover both senior management and their immediate family members. When such relationships exist, measures are taken to manage appropriately the actual or perceived conflict in the best interests of the relevant entity. No such associations are considered to be significant.

The University, SHC and LPCH have separate written conflict of interest policies that require, among other items, that no member of their respective board can participate in any decision in which he or she (or an immediate family member) has a material financial interest. Each board member is required to certify compliance with his or her respective entity's conflict of interest policy on an annual basis and indicate whether his or her respective entity does business with any entity in which the board member 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 respective entity, and in accordance with applicable conflict of interest laws and policies. No such associations are considered to be significant.

19. Commitments and Contingencies

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

SPONSORED RESEARCH

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, 2010 to 2016 are subject to audit. The University does not anticipate any adjustments material to the consolidated financial statements.

HEALTH CARE

As described in *Note 3*, 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.

The health care 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 of regulations by health care providers could result in the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. SHC and LPCH are subject to similar regulatory reviews, and while such reviews may result in repayments and civil remedies that could have a material effect on their respective financial results of operations in a given period, SHC's and LPCH's management believes that such repayments and civil remedies would not have a material effect on its financial position.

INFORMATION SECURITY AND PRIVACY

As with many medical centers and universities across the country, information security and privacy is a growing risk area based on developments in the law and expanding mobile technology practices. The University, SHC and LPCH have policies, procedures, and training in place to safeguard protected information, but select incidents have occurred in the past and may occur in the future involving potential or actual disclosure of such information (including, for example, certain identifiable information relating to patients or research participants). In most cases, there has been no evidence of unauthorized access to, or use/disclosure of, such information, yet laws may require reporting to potentially affected individuals and federal and state governmental agencies. Governmental agencies have the authority to investigate and request further information about an incident or safeguards, to cite the University, SHC or LPCH for a deficiency or regulatory violation, and/or require payment of fines, corrective action, or both. California law also allows a private right to sue for a breach of medical information. The cost of such possible consequences has not been material to date to the University, SHC or LPCH, and management does not believe that any future consequences of these incidents will be material to the consolidated financial statements.

LABOR AGREEMENTS

Approximately 7% of the University's, 31% of SHC's and 40% 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. The University's agreements with the Stanford Deputy Sheriffs' Association and the Service Employees International Union (SEIU) will expire in 2020 and 2019, respectively. SHC's and LPCH's agreements with SEIU and the Committee for Recognition of Nursing Achievement (CRONA) will expire in 2017 and 2019, respectively.

GUARANTEES AND INDEMNIFICATIONS

Stanford enters into indemnification agreements with third parties in the normal course of business. The impact of these agreements, individually or in the aggregate, is not expected to be material to the consolidated financial statements. As a result, no liabilities related to guarantees and indemnifications have been recorded at August 31, 2016.

LITIGATION

The University, SHC and LPCH 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.

MEDICAL CENTER RENEWAL PROJECT

In July 2011, Stanford 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 share of the estimated total cost of the Renewal Project is \$2 billion. The cost of LPCH's share, originally estimated to be approximately \$1.2 billion, is likely to be exceeded because of cost increases related to changes in technology, change orders, and market availability of subcontractors, among other factors. The sources of funding for the Renewal Project include operating surpluses, gifts, government grants, and bond proceeds. Through August 2016, SHC has recorded \$1.2 billion in construction in progress, inclusive of \$98.0 million in capitalized interest and LPCH has recorded \$966.8 million in construction in progress, inclusive of \$15.6 million in capitalized interest, related to this project. Construction of the Renewal Project is currently scheduled to be completed in 2017 for LPCH and 2018 for SHC.

CONTRACTUAL COMMITMENTS

At August 31, 2016, the University had contractual obligations of approximately \$332.8 million in connection with major construction projects. Remaining expenditures on construction in progress are estimated to be \$902.9 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 \$511.9 million for SHC and \$188.6 million for LPCH at August 31, 2016.

The University executed an agreement with a solar electricity developer and operator in 2015 to purchase the output from its solar photovoltaic facility, which is expected to be placed in service by January 1, 2017. The minimum energy purchase requirements are well within the University's current consumption. The University's total payment under the agreement over 25 years, undiscounted, is \$198.6 million.

In addition, as described in *Note 6*, the University is obligated under certain alternative investment agreements to advance additional funding up to specified levels over a period of years.

20. Subsequent Events

Stanford has evaluated subsequent events for the period from August 31, 2016 through December 6, 2016, the date the consolidated financial statements were issued.

The Board of Directors of LPFCH and the Board of Directors of LPCH approved a binding memorandum of understanding pursuant to which LPCH would become the sole member of LPFCH, effective September 1, 2016. The bylaws of LPFCH afford control of LPFCH to LPCH and therefore, the activities of LPFCH will be included in the consolidated financial statements of LPCH starting September 1, 2016.

21. Consolidating Entity Statements

The pages which follow present consolidating statements of financial position as of August 31, 2016 and 2015, and consolidating statements of activities and cash flows for the years then ended, in thousands of dollars.

CONSOLIDATING STATEMENTS OF FINANCIAL POSITION

At August 31, 2016 (in thousands of dollars)

| | UNIVERSITY | SHC | LPCH | ELIMINATIONS | CONSOLIDATED |
|--|----------------------|---------------------|--------------------|--------------------|----------------------|
| ASSETS | | | | | |
| Cash and cash equivalents | \$ 640,224 | \$ 690,460 | \$ 532,900 | \$ - | \$ 1,863,584 |
| Assets limited as to use | 315,889 | 235,788 | 219 | - | 551,896 |
| Accounts receivable, net | 316,193 | 642,369 | 302,234 | - | 1,260,796 |
| Receivables (payables) from SHC and LPCH, net | 91,468 | - | - | (91,468) | - |
| Prepaid expenses and other assets | 103,043 | 136,698 | 82,354 | (3,918) | 318,177 |
| Pledges receivable, net | 1,357,508 | 97,753 | 115,651 | - | 1,570,912 |
| Student loans receivable, net | 78,549 | - | - | - | 78,549 |
| Faculty and staff mortgages and other loans receivable, net | 610,026 | - | - | - | 610,026 |
| Investments at fair value, including securities pledged or on loan of \$205,128 | 29,085,787 | 1,552,389 | 694,055 | - | 31,332,231 |
| Plant facilities, net of accumulated depreciation | 5,168,720 | 2,401,880 | 1,429,316 | - | 8,999,916 |
| Works of art and special collections | - | - | - | - | - |
| TOTAL ASSETS | \$ 37,767,407 | \$ 5,757,337 | \$3,156,729 | \$ (95,386) | \$ 46,586,087 |
| LIABILITIES AND NET ASSETS | | | | | |
| LIABILITIES: | | | | | |
| Accounts payable and accrued expenses | \$ 742,872 | \$ 1,115,084 | \$ 272,364 | \$ (95,386) | \$ 2,034,934 |
| Accrued pension and postretirement benefit obligations | 555,047 | 125,358 | 19,059 | - | 699,464 |
| Liabilities associated with investments | 353,848 | - | - | - | 353,848 |
| Deferred rental and other income | 657,378 | - | - | - | 657,378 |
| Income beneficiary share of split interest agreements | 414,432 | - | - | - | 414,432 |
| Notes and bonds payable | 3,270,617 | 1,462,745 | 668,406 | - | 5,401,768 |
| U.S. government refundable loan funds | 54,035 | - | - | - | 54,035 |
| TOTAL LIABILITIES | 6,048,229 | 2,703,187 | 959,829 | (95,386) | 9,615,859 |
| NET ASSETS: | | | | | |
| Unrestricted | 17,255,819 | 2,469,170 | 1,411,433 | - | 21,136,422 |
| Temporarily restricted | 7,394,745 | 577,086 | 574,119 | - | 8,545,950 |
| Permanently restricted | 7,068,614 | 7,894 | 211,348 | - | 7,287,856 |
| TOTAL NET ASSETS | 31,719,178 | 3,054,150 | 2,196,900 | - | 36,970,228 |
| TOTAL LIABILITIES AND NET ASSETS | \$ 37,767,407 | \$ 5,757,337 | \$3,156,729 | \$ (95,386) | \$ 46,586,087 |

CONSOLIDATING STATEMENTS OF FINANCIAL POSITION

At August 31, 2015 (in thousands of dollars)

| | UNIVERSITY | SHC | LPCH | ELIMINATIONS | CONSOLIDATED |
|--|----------------------|---------------------|---------------------|--------------------|----------------------|
| ASSETS | | | | | |
| Cash and cash equivalents | \$ 708,204 | \$ 475,677 | \$ 335,901 | \$ - | \$ 1,519,782 |
| Assets limited as to use | 160,351 | 580,701 | 89,500 | - | 830,552 |
| Accounts receivable, net | 225,440 | 607,924 | 300,112 | - | 1,133,476 |
| Receivables (payables) from SHC and LPCH, net | 89,045 | - | - | (89,045) | - |
| Prepaid expenses and other assets | 77,303 | 129,766 | 73,376 | (4,025) | 276,420 |
| Pledges receivable, net | 760,519 | 130,457 | 30,543 | - | 921,519 |
| Student loans receivable, net | 81,492 | - | - | - | 81,492 |
| Faculty and staff mortgages and other loans receivable, net | 549,724 | - | - | - | 549,724 |
| Investments at fair value, including securities pledged or on loan of \$106,264 | 28,766,240 | 1,669,889 | 963,047 | - | 31,399,176 |
| Plant facilities, net of accumulated depreciation | 4,795,564 | 1,923,465 | 1,078,277 | - | 7,797,306 |
| Works of art and special collections | - | - | - | - | - |
| TOTAL ASSETS | \$ 36,213,882 | \$ 5,517,879 | \$ 2,870,756 | \$ (93,070) | \$ 44,509,447 |
| LIABILITIES AND NET ASSETS | | | | | |
| LIABILITIES: | | | | | |
| Accounts payable and accrued expenses | \$ 719,979 | \$ 860,925 | \$ 250,797 | \$ (93,070) | \$ 1,738,631 |
| Accrued pension and postretirement benefit obligations | 685,836 | 117,767 | 20,586 | - | 824,189 |
| Liabilities associated with investments | 212,656 | - | - | - | 212,656 |
| Deferred rental and other income | 652,850 | - | - | - | 652,850 |
| Income beneficiary share of split interest agreements | 435,426 | - | - | - | 435,426 |
| Notes and bonds payable | 3,019,578 | 1,479,479 | 559,686 | - | 5,058,743 |
| U.S. government refundable loan funds | 54,081 | - | - | - | 54,081 |
| TOTAL LIABILITIES | 5,780,406 | 2,458,171 | 831,069 | (93,070) | 8,976,576 |
| NET ASSETS: | | | | | |
| Unrestricted | 16,507,624 | 2,490,372 | 1,377,043 | - | 20,375,039 |
| Temporarily restricted | 7,744,051 | 561,642 | 458,239 | - | 8,763,932 |
| Permanently restricted | 6,181,801 | 7,694 | 204,405 | - | 6,393,900 |
| TOTAL NET ASSETS | 30,433,476 | 3,059,708 | 2,039,687 | - | 35,532,871 |
| TOTAL LIABILITIES AND NET ASSETS | \$ 36,213,882 | \$ 5,517,879 | \$ 2,870,756 | \$ (93,070) | \$ 44,509,447 |

CONSOLIDATING STATEMENTS OF ACTIVITIES

For the year ended August 31, 2016 (in thousands of dollars)

| | UNIVERSITY | SHC | LPCH | ELIMINATIONS | CONSOLIDATED |
|---|-------------------|-------------------|------------------|------------------|-------------------|
| UNRESTRICTED NET ASSETS | | | | | |
| OPERATING REVENUES: | | | | | |
| Student income: | | | | | |
| Undergraduate programs | \$ 342,309 | \$ - | \$ - | \$ - | \$ 342,309 |
| Graduate programs | 340,537 | - | - | - | 340,537 |
| Room and board | 174,111 | - | - | - | 174,111 |
| Student financial aid | (269,613) | - | - | - | (269,613) |
| TOTAL STUDENT INCOME | 587,344 | - | - | - | 587,344 |
| Sponsored research support: | | | | | |
| Direct costs - University | 753,638 | - | - | - | 753,638 |
| Direct costs - SLAC National Accelerator Laboratory | 447,834 | - | - | - | 447,834 |
| Indirect costs | 251,395 | - | - | - | 251,395 |
| TOTAL SPONSORED RESEARCH SUPPORT | 1,452,867 | - | - | - | 1,452,867 |
| Health care services: | | | | | |
| Net patient service revenue | - | 3,893,005 | 1,313,384 | (47,214) | 5,159,175 |
| Premium revenue | - | 72,292 | - | - | 72,292 |
| Physicians' services and support - SHC and LPCH, net | 873,520 | - | - | (873,520) | - |
| Physicians' services and support - other facilities, net | 32,966 | - | - | - | 32,966 |
| TOTAL HEALTH CARE SERVICES | 906,486 | 3,965,297 | 1,313,384 | (920,734) | 5,264,433 |
| CURRENT YEAR GIFTS IN SUPPORT OF OPERATIONS | 250,769 | 1,776 | 5,740 | - | 258,285 |
| Net assets released from restrictions: | | | | | |
| Payments received on pledges | 104,599 | 2,703 | - | - | 107,302 |
| Prior year gifts released from donor restrictions | 70,819 | 3,532 | 2,627 | - | 76,978 |
| TOTAL NET ASSETS RELEASED FROM RESTRICTIONS | 175,418 | 6,235 | 2,627 | - | 184,280 |
| Investment income distributed for operations: | | | | | |
| Endowment | 1,132,105 | 413 | 15,462 | - | 1,147,980 |
| Expendable funds pools and other investment income | 189,564 | 948 | - | - | 190,512 |
| TOTAL INVESTMENT INCOME DISTRIBUTED FOR OPERATIONS | 1,321,669 | 1,361 | 15,462 | - | 1,338,492 |
| SPECIAL PROGRAM FEES AND OTHER INCOME | 523,506 | 122,996 | 65,089 | - | 711,591 |
| TOTAL OPERATING REVENUES | 5,218,059 | 4,097,665 | 1,402,302 | (920,734) | 9,797,292 |
| OPERATING EXPENSES: | | | | | |
| Salaries and benefits | 3,091,657 | 1,850,124 | 585,503 | - | 5,527,284 |
| Depreciation | 345,977 | 136,166 | 56,454 | - | 538,597 |
| Other operating expenses | 1,476,976 | 1,963,329 | 721,723 | (920,734) | 3,241,294 |
| TOTAL OPERATING EXPENSES | 4,914,610 | 3,949,619 | 1,363,680 | (920,734) | 9,307,175 |
| CHANGE IN NET ASSETS FROM OPERATING ACTIVITIES | \$ 303,449 | \$ 148,046 | \$ 38,622 | \$ - | \$ 490,117 |

CONSOLIDATING STATEMENTS OF ACTIVITIES, Continued
For the year ended August 31, 2016 (in thousands of dollars)

| | UNIVERSITY | SHC | LPCH | ELIMINATIONS | CONSOLIDATED |
|---|----------------------|---------------------|---------------------|--------------|----------------------|
| UNRESTRICTED NET ASSETS (continued) | | | | | |
| CHANGE IN NET ASSETS FROM OPERATING ACTIVITIES | \$ 303,449 | \$ 148,046 | \$ 38,622 | \$ - | \$ 490,117 |
| NON-OPERATING ACTIVITIES: | | | | | |
| Increase in reinvested gains | 118,270 | 39,061 | 10,303 | - | 167,634 |
| Donor advised funds, net | 21,783 | - | - | - | 21,783 |
| Current year gifts not included in operations | 2,381 | - | - | - | 2,381 |
| Equity and fund transfers from Hospitals, net | 104,944 | (92,242) | (12,702) | - | - |
| Capital and other gifts released from restrictions | 117,490 | 973 | 27 | - | 118,490 |
| Pension and other postemployment benefit related changes other than net periodic benefit expense | 180,708 | (80) | 1,385 | - | 182,013 |
| Transfer to permanently restricted net assets, net | (45,651) | - | - | - | (45,651) |
| Transfer to temporarily restricted net assets, net | (35,082) | - | - | - | (35,082) |
| Swap interest and change in value of swap agreements | (19,966) | (115,958) | - | - | (135,924) |
| Other | (131) | (1,002) | (3,245) | - | (4,378) |
| NET CHANGE IN UNRESTRICTED NET ASSETS | 748,195 | (21,202) | 34,390 | - | 761,383 |
| TEMPORARILY RESTRICTED NET ASSETS | | | | | |
| Gifts and pledges, net | 284,923 | 20,716 | 129,868 | - | 435,507 |
| Increase (decrease) in reinvested gains | (349,476) | 2,427 | 9,987 | - | (337,062) |
| Change in value of split interest agreements, net | 14,702 | - | 164 | - | 14,866 |
| Net assets released to operations | (175,418) | (9,372) | (23,829) | - | (208,619) |
| Capital and other gifts released to unrestricted net assets | (117,490) | (973) | (27) | - | (118,490) |
| Gift transfers to Hospitals, net | (2,927) | 2,646 | 281 | - | - |
| Transfer from unrestricted net assets, net | 35,082 | - | - | - | 35,082 |
| Transfer to permanently restricted net assets, net | (35,551) | - | - | - | (35,551) |
| Other | (3,151) | - | (564) | - | (3,715) |
| NET CHANGE IN TEMPORARILY RESTRICTED NET ASSETS | (349,306) | 15,444 | 115,880 | - | (217,982) |
| PERMANENTLY RESTRICTED NET ASSETS | | | | | |
| Gifts and pledges, net | 761,992 | 200 | 7,669 | - | 769,861 |
| Increase in reinvested gains | 25,566 | - | - | - | 25,566 |
| Change in value of split interest agreements, net | 18,053 | - | 1,255 | - | 19,308 |
| Transfer from unrestricted net assets, net | 45,651 | - | - | - | 45,651 |
| Transfer from temporarily restricted net assets, net | 35,551 | - | - | - | 35,551 |
| Other | - | - | (1,981) | - | (1,981) |
| NET CHANGE IN PERMANENTLY RESTRICTED NET ASSETS | 886,813 | 200 | 6,943 | - | 893,956 |
| NET CHANGE IN TOTAL NET ASSETS | 1,285,702 | (5,558) | 157,213 | - | 1,437,357 |
| Total net assets, beginning of year | 30,433,476 | 3,059,708 | 2,039,687 | - | 35,532,871 |
| TOTAL NET ASSETS, END OF YEAR | \$ 31,719,178 | \$ 3,054,150 | \$ 2,196,900 | \$ - | \$ 36,970,228 |

CONSOLIDATING STATEMENTS OF ACTIVITIES

For the year ended August 31, 2015 (in thousands of dollars)

| | UNIVERSITY | SHC | LPCH | ELIMINATIONS | CONSOLIDATED |
|---|-------------------|-------------------|-------------------|------------------|-------------------|
| UNRESTRICTED NET ASSETS | | | | | |
| OPERATING REVENUES: | | | | | |
| Student income: | | | | | |
| Undergraduate programs | \$ 330,851 | \$ - | \$ - | \$ - | \$ 330,851 |
| Graduate programs | 329,047 | - | - | - | 329,047 |
| Room and board | 164,304 | - | - | - | 164,304 |
| Student financial aid | (260,616) | - | - | - | (260,616) |
| TOTAL STUDENT INCOME | 563,586 | - | - | - | 563,586 |
| Sponsored research support: | | | | | |
| Direct costs - University | 713,831 | - | - | - | 713,831 |
| Direct costs - SLAC National Accelerator Laboratory | 430,365 | - | - | - | 430,365 |
| Indirect costs | 242,572 | - | - | - | 242,572 |
| TOTAL SPONSORED RESEARCH SUPPORT | 1,386,768 | - | - | - | 1,386,768 |
| Health care services: | | | | | |
| Net patient service revenue | - | 3,393,413 | 1,304,113 | (47,087) | 4,650,439 |
| Premium revenue | - | 62,893 | - | - | 62,893 |
| Physicians' services and support - SHC and LPCH, net | 810,474 | - | - | (810,474) | - |
| Physicians' services and support - other facilities, net | 30,487 | - | - | - | 30,487 |
| TOTAL HEALTH CARE SERVICES | 840,961 | 3,456,306 | 1,304,113 | (857,561) | 4,743,819 |
| CURRENT YEAR GIFTS IN SUPPORT OF OPERATIONS | 233,572 | 2,049 | 5,554 | - | 241,175 |
| Net assets released from restrictions: | | | | | |
| Payments received on pledges | 120,653 | 2,557 | - | - | 123,210 |
| Prior year gifts released from donor restrictions | 37,518 | 10,039 | 3,532 | - | 51,089 |
| TOTAL NET ASSETS RELEASED FROM RESTRICTIONS | 158,171 | 12,596 | 3,532 | - | 174,299 |
| Investment income distributed for operations: | | | | | |
| Endowment | 1,058,025 | 419 | 14,266 | - | 1,072,710 |
| Expendable funds pools and other investment income | 218,438 | 599 | - | - | 219,037 |
| TOTAL INVESTMENT INCOME DISTRIBUTED FOR OPERATIONS | 1,276,463 | 1,018 | 14,266 | - | 1,291,747 |
| SPECIAL PROGRAM FEES AND OTHER INCOME | 498,804 | 98,718 | 52,360 | - | 649,882 |
| TOTAL OPERATING REVENUES | 4,958,325 | 3,570,687 | 1,379,825 | (857,561) | 9,051,276 |
| OPERATING EXPENSES: | | | | | |
| Salaries and benefits | 2,848,708 | 1,428,100 | 518,780 | - | 4,795,588 |
| Depreciation | 334,592 | 109,511 | 58,532 | - | 502,635 |
| Other operating expenses | 1,462,398 | 1,751,160 | 696,672 | (857,561) | 3,052,669 |
| TOTAL OPERATING EXPENSES | 4,645,698 | 3,288,771 | 1,273,984 | (857,561) | 8,350,892 |
| CHANGE IN NET ASSETS FROM OPERATING ACTIVITIES | \$ 312,627 | \$ 281,916 | \$ 105,841 | \$ - | \$ 700,384 |

CONSOLIDATING STATEMENTS OF ACTIVITIES, Continued
For the year ended August 31, 2015 (in thousands of dollars)

| | UNIVERSITY | SHC | LPCH | ELIMINATIONS | CONSOLIDATED |
|---|----------------------|---------------------|---------------------|--------------|----------------------|
| UNRESTRICTED NET ASSETS (continued) | | | | | |
| CHANGE IN NET ASSETS FROM OPERATING ACTIVITIES | \$ 312,627 | \$ 281,916 | \$ 105,841 | \$ - | \$ 700,384 |
| NON-OPERATING ACTIVITIES: | | | | | |
| Increase in reinvested gains | 644,855 | 67,544 | 33,323 | - | 745,722 |
| Donor advised funds, net | 66,734 | - | - | - | 66,734 |
| Current year gifts not included in operations | 1,655 | - | - | - | 1,655 |
| Equity and fund transfers from Hospitals, net | 89,963 | (39,858) | (50,105) | - | - |
| Capital and other gifts released from restrictions | 96,693 | 2,288 | 1,999 | - | 100,980 |
| Pension and other postemployment benefit related changes other than net periodic benefit expense | (85,091) | (19,461) | (678) | - | (105,230) |
| Transfer to permanently restricted net assets, net | (49,998) | - | - | - | (49,998) |
| Transfer to temporarily restricted net assets, net | (26,223) | - | - | - | (26,223) |
| Swap interest and change in value of swap agreements | (8,587) | (59,392) | - | - | (67,979) |
| Contribution income from Stanford Health Care-ValleyCare affiliation | - | 96,758 | - | - | 96,758 |
| Other | (2,693) | (116) | (1,110) | - | (3,919) |
| NET CHANGE IN UNRESTRICTED NET ASSETS | 1,039,935 | 329,679 | 89,270 | - | 1,458,884 |
| TEMPORARILY RESTRICTED NET ASSETS | | | | | |
| Gifts and pledges, net | 250,808 | 52,333 | 70,810 | - | 373,951 |
| Increase (decrease) in reinvested gains | (89,655) | 4,204 | 14,549 | - | (70,902) |
| Change in value of split interest agreements, net | 2,449 | - | (254) | - | 2,195 |
| Net assets released to operations | (158,171) | (15,663) | (23,352) | - | (197,186) |
| Capital and other gifts released to unrestricted net assets | (96,693) | (2,288) | (1,999) | - | (100,980) |
| Gift transfers to Hospitals, net | (4,073) | 4,043 | 30 | - | - |
| Transfer from unrestricted net assets, net | 26,223 | - | - | - | 26,223 |
| Transfer to permanently restricted net assets, net | (27,999) | - | - | - | (27,999) |
| Other | (3,002) | 81 | (908) | - | (3,829) |
| NET CHANGE IN TEMPORARILY RESTRICTED NET ASSETS | (100,113) | 42,710 | 58,876 | - | 1,473 |
| PERMANENTLY RESTRICTED NET ASSETS | | | | | |
| Gifts and pledges, net | 208,206 | 2 | 850 | - | 209,058 |
| Increase in reinvested gains | 1,760 | - | - | - | 1,760 |
| Change in value of split interest agreements, net | (15,446) | - | (310) | - | (15,756) |
| Transfer from unrestricted net assets, net | 49,998 | - | - | - | 49,998 |
| Transfer from temporarily restricted net assets, net | 27,999 | - | - | - | 27,999 |
| Other | - | - | 523 | - | 523 |
| NET CHANGE IN PERMANENTLY RESTRICTED NET ASSETS | 272,517 | 2 | 1,063 | - | 273,582 |
| NET CHANGE IN TOTAL NET ASSETS | 1,212,339 | 372,391 | 149,209 | - | 1,733,939 |
| Total net assets, beginning of year | 29,221,137 | 2,687,317 | 1,890,478 | - | 33,798,932 |
| TOTAL NET ASSETS, END OF YEAR | \$ 30,433,476 | \$ 3,059,708 | \$ 2,039,687 | \$ - | \$ 35,532,871 |

CONSOLIDATING STATEMENTS OF CASH FLOWS

For the year ended August 31, 2016 (in thousands of dollars)

| | UNIVERSITY | SHC | LPCH | CONSOLIDATED |
|--|-------------------|-------------------|-------------------|---------------------|
| CASH FLOW FROM OPERATING ACTIVITIES | | | | |
| Change in net assets | \$ 1,285,702 | \$ (5,558) | \$ 157,213 | \$ 1,437,357 |
| Adjustments to reconcile change in net assets to net cash provided by (used for) operating activities: | | | | |
| Depreciation | 345,977 | 136,166 | 56,454 | 538,597 |
| Amortization, loss on disposal of fixed assets and other adjustments | 335 | (1,664) | (1,453) | (2,782) |
| Provision for doubtful accounts for health care services | - | 126,280 | (2,433) | 123,847 |
| Net losses (gains) on investments and security agreements | (908,896) | (25,346) | 3,814 | (930,428) |
| Changes in fair value of interest rate swaps | 16,638 | 115,958 | - | 132,596 |
| Changes in split interest agreements | 10,591 | - | (1,419) | 9,172 |
| Investment income for restricted purposes | (30,815) | - | - | (30,815) |
| Gifts restricted for long-term investments | (848,262) | (9,832) | (30,043) | (888,137) |
| Equity and fund transfers from Hospitals | (102,017) | 89,599 | 12,418 | - |
| Gifts of securities and properties | (15,585) | - | - | (15,585) |
| Premiums received from bond issuance | 79,651 | - | 14,447 | 94,098 |
| Changes in operating assets and liabilities: | | | | |
| Accounts receivable, net | (41,134) | (160,251) | 7,431 | (193,954) |
| Pledges receivable, net | (21,036) | (951) | (82,880) | (104,867) |
| Prepaid expenses and other assets | (28,154) | (6,021) | (14,739) | (48,914) |
| Accounts payable and accrued expenses | 6,123 | 129,967 | 7,220 | 143,310 |
| Accrued pension and postretirement benefit obligations | (130,789) | 7,591 | (1,527) | (124,725) |
| Deferred rental and other income | 4,528 | - | - | 4,528 |
| Other | - | - | 5,577 | 5,577 |
| NET CASH PROVIDED BY (USED FOR) OPERATING ACTIVITIES | (377,143) | 395,938 | 130,080 | 148,875 |
| CASH FLOW FROM INVESTING ACTIVITIES | | | | |
| Land, building and equipment purchases | (699,868) | (619,570) | (373,743) | (1,693,181) |
| Student, faculty and other loans: | | | | |
| New loans made | (117,150) | - | - | (117,150) |
| Principal collected | 50,335 | - | - | 50,335 |
| Decrease (increase) in assets limited as to use | (155,538) | 344,913 | 89,413 | 278,788 |
| Purchases of investments | (14,341,974) | (74,446) | - | (14,416,420) |
| Sales and maturities of investments | 14,898,551 | 217,292 | 270,000 | 15,385,843 |
| NET CASH USED FOR INVESTING ACTIVITIES | (365,644) | (131,811) | (14,330) | (511,785) |
| CASH FLOW FROM FINANCING ACTIVITIES | | | | |
| Gifts and reinvested income for restricted purposes | 281,663 | 44,026 | 24,280 | 349,969 |
| Equity and fund transfers from Hospitals | 110,829 | (77,419) | (33,410) | - |
| Proceeds from borrowing | 486,154 | - | 100,000 | 586,154 |
| Bond issuance costs and interest rate swaps | (966) | - | (1,188) | (2,154) |
| Repayment of notes and bonds payable | (301,044) | (15,951) | (5,705) | (322,700) |
| Increase in liabilities associated with investments | 98,467 | - | - | 98,467 |
| Other | (296) | - | (2,728) | (3,024) |
| NET CASH PROVIDED BY (USED FOR) FINANCING ACTIVITIES | 674,807 | (49,344) | 81,249 | 706,712 |
| INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | (67,980) | 214,783 | 196,999 | 343,802 |
| Cash and cash equivalents, beginning of year | 708,204 | 475,677 | 335,901 | 1,519,782 |
| CASH AND CASH EQUIVALENTS, END OF YEAR | \$ 640,224 | \$ 690,460 | \$ 532,900 | \$ 1,863,584 |
| SUPPLEMENTAL DATA: | | | | |
| Interest paid, net of capitalized interest | \$ 120,891 | \$ 41,427 | \$ 10,950 | \$ 173,268 |
| Cash collateral received under security lending agreements | \$ 213,629 | \$ - | \$ - | \$ 213,629 |
| Increase (decrease) in payables for plant facilities | \$ 6,485 | \$ (8,128) | \$ 33,071 | \$ 31,428 |

CONSOLIDATING STATEMENTS OF CASH FLOWS

For the year ended August 31, 2015 (in thousands of dollars)

| | UNIVERSITY | SHC | LPCH | CONSOLIDATED |
|--|-------------------|-------------------|-------------------|---------------------|
| CASH FLOW FROM OPERATING ACTIVITIES | | | | |
| Change in net assets | \$ 1,212,339 | \$ 372,391 | \$ 149,209 | \$ 1,733,939 |
| Adjustments to reconcile change in net assets to net cash provided by (used for) operating activities: | | | | |
| Depreciation | 334,592 | 109,511 | 58,532 | 502,635 |
| Amortization, loss on disposal of fixed assets and other adjustments | 9,950 | (1,702) | (929) | 7,319 |
| Provision for doubtful accounts for health care services | - | 131,601 | 10,474 | 142,075 |
| Net gains on investments and security agreements | (1,613,337) | (52,858) | (24,997) | (1,691,192) |
| Changes in fair value of interest rate swaps | 5,127 | 59,392 | - | 64,519 |
| Changes in split interest agreements | 21,529 | - | 564 | 22,093 |
| Investment expense (income) for restricted purposes | (34,034) | - | 2,206 | (31,828) |
| Gifts restricted for long-term investments | (252,404) | (40,014) | (61,682) | (354,100) |
| Equity and fund transfers from Hospitals | (85,890) | 35,815 | 50,075 | - |
| Gifts of securities and properties | (42,330) | - | - | (42,330) |
| Contribution income from Stanford Health Care- ValleyCare affiliation | - | (96,820) | - | (96,820) |
| Premiums received from bond issuance | - | 5,627 | - | 5,627 |
| Changes in operating assets and liabilities: | | | | |
| Accounts receivable, net | (26,145) | (233,049) | (79,726) | (338,920) |
| Pledges receivable, net | (1,324) | (2,111) | 3,063 | (372) |
| Prepaid expenses and other assets | (9,761) | (17,931) | (10,755) | (38,447) |
| Accounts payable and accrued expenses | 85,525 | 60,951 | 48,408 | 194,884 |
| Accrued pension and postretirement benefit obligations | 119,600 | 20,528 | 486 | 140,614 |
| Deferred rental and other income | 36,275 | - | - | 36,275 |
| Other | - | 35 | - | 35 |
| NET CASH PROVIDED BY (USED FOR) OPERATING ACTIVITIES | (240,288) | 351,366 | 144,928 | 256,006 |
| CASH FLOW FROM INVESTING ACTIVITIES | | | | |
| Land, building and equipment purchases | (583,531) | (447,635) | (251,099) | (1,282,265) |
| Student, faculty and other loans: | | | | |
| New loans made | (104,509) | - | - | (104,509) |
| Principal collected | 55,444 | - | - | 55,444 |
| Decrease (increase) in assets limited as to use | 140,215 | (74,101) | 170,157 | 236,271 |
| Cash acquired from ValleyCare, net of cash paid as consideration | - | (52,539) | - | (52,539) |
| Purchases of investments | (28,157,549) | (208,307) | (757) | (28,366,613) |
| Sales and maturities of investments | 28,864,206 | 196,497 | 90,000 | 29,150,703 |
| NET CASH PROVIDED BY (USED FOR) INVESTING ACTIVITIES | 214,276 | (586,085) | 8,301 | (363,508) |
| CASH FLOW FROM FINANCING ACTIVITIES | | | | |
| Gifts and reinvested income for restricted purposes | 229,727 | 153,464 | 41,714 | 424,905 |
| Equity and fund transfers from Hospitals | 99,656 | (72,109) | (27,547) | - |
| Proceeds from borrowing | 291,200 | 244,111 | - | 535,311 |
| Bond issuance costs and interest rate swaps | (957) | (1,571) | - | (2,528) |
| Repayment of notes and bonds payable | (457,119) | (81,154) | (5,375) | (543,648) |
| Decrease in liabilities associated with investments | (58,586) | - | - | (58,586) |
| Other | 81 | - | (277) | (196) |
| NET CASH PROVIDED BY FINANCING ACTIVITIES | 104,002 | 242,741 | 8,515 | 355,258 |
| INCREASE IN CASH AND CASH EQUIVALENTS | 77,990 | 8,022 | 161,744 | 247,756 |
| Cash and cash equivalents, beginning of year | 630,214 | 467,655 | 174,157 | 1,272,026 |
| CASH AND CASH EQUIVALENTS, END OF YEAR | \$ 708,204 | \$ 475,677 | \$ 335,901 | \$ 1,519,782 |
| SUPPLEMENTAL DATA: | | | | |
| Interest paid, net of capitalized interest | \$ 120,743 | \$ 42,481 | \$ 14,854 | \$ 178,078 |
| Cash collateral received under security lending agreements | \$ 110,087 | \$ - | \$ - | \$ 110,087 |
| Increase (decrease) in payables for plant facilities | \$ (15,493) | \$ 43,861 | \$ 18,394 | \$ 46,762 |