Alabama Retired Education Employees' Health Care Trust

(A Component Unit of the State of Alabama)

FINANCIAL STATEMENTS

For the Fiscal Year Ended September 30, 2012

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INDEPENDENT AUDITORS' REPORT

The Public Education Employees'
Health Insurance Board

We have audited the accompanying statement of plan net assets of the Alabama Retired Education Employees' Health Care Trust (a component unit of the State of Alabama) as of September 30, 2012, and the related statement of changes in plan net assets for the year then ended. These financial statements are the responsibility of the Alabama Retired Education Employees' Health Care Trust. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year partial comparative information has been derived from the Alabama Retired Education Employees' Health Care Trust's 2011 financial statements and, in our report dated January 31, 2012, we expressed an unqualified opinion on such financial statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 2012 financial statements referred to above present fairly, in all material respects, the financial position of the Alabama Retired Education Employees' Health Care Trust (a component unit of the State of Alabama) as of September 30, 2012, and its changes in plan net assets for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 5 and the schedules of funding progress and contributions made from the employers and other contributing entities on page 23 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information on page 24 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The supplementary information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplementary information is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Carr, Riggs & Ingram, L.L.C.

January 28, 2013
Montgomery, Alabama

ALABAMA RETIRED EDUCATION EMPLOYEES' HEALTH CARE TRUST
Management's Discussion and Analysis
September 30, 2012

The Alabama Retired Education Employees' Health Care Trust (Trust) is a multiple-employer cost-sharing defined benefit postemployment healthcare plan. The Trust was established in 2007 to provide healthcare benefits to retirees of state and local educational institutions. The contributions and benefit payments related to retirees that are processed through the Public Education Employees' Health Insurance Fund (PEEHIF) are segregated from the PEEHIF and reported as part of the Trust.

The following discussion provides an overview of the financial position and results of operation for the Trust as of and for the fiscal year ended September 30, 2012. For more detailed information, please refer to the financial statements, including the *Notes to the Financial Statements*, the *Required Supplementary Information*, and the *Supplementary Information*.

Overview of the Financial Statements

The financial statements include the *Statement of Plan Net Assets* and the *Statement of Changes in Plan Net Assets*. The *Notes to the Financial Statements* are considered an integral part of the financial statements and should be read in conjunction with the financial statements. The financial statements are prepared under the accrual basis of accounting using the economic resources measurement focus. Revenues are recognized when earned and expenses are recognized when incurred, regardless of when cash is received or expended. Investments are reported at fair value.

The *Statement of Plan Net Assets* includes the assets and liabilities of the Trust and provides a snapshot of the Trust's financial position as of the end of the fiscal year. The Trust's assets primarily consist of investments and receivables. Liabilities are primarily made up of claims-related payables.

The *Statement of Changes in Plan Net Assets* includes the additions and deductions of the Trust for the fiscal year. Additions primarily consist of employer contributions, employee contributions, Federal Government subsidies, and investment income. Deductions are primarily made up of claims.

The *Notes to the Financial Statements* include a description of the Trust, a summary of significant accounting policies, a description of contract administrators and their respective fees, credit risk disclosures for cash and investments, concentration of investments disclosures, securities lending disclosures, funded status, actuarial valuation information, and disclosures related to unpaid claim liabilities.

The *Required Supplementary Information* following the *Notes to the Financial Statements* includes a Schedule of Funding Progress and a Schedule of Employer Contributions. The Schedule of Funding Progress provides trend data on the level of funding for the Trust. The Schedule of Employer Contributions provides trend data on the annual required employer contributions and the percentage contributed during the fiscal year.

The *Supplementary Information* following the *Required Supplementary Information* provides a claims development table illustrating historical trend information on how the Trust's earned revenues and interest income compare to the related costs of claims and other expenses assumed by the Trust as of the end of the fiscal year.

Comparative Financial Statements

Summary Comparative Statement of Plan Net Assets
As of September 30, 2012 and 2011
(Amounts in Thousands)

	2012	2011	Variance	% Increase (Decrease)
Assets				
Receivables	$ 14,471	$ 10,555	$ 3,916	37.10
Investments	953,268	802,688	150,580	18.76
Invested Securities Lending Collateral	65,311	70,207	(4,896)	(6.97)
Deposit with Claims-Paying Agent	200	667	(467)	(70.01)
Total Assets	$ 1,033,250	$ 884,117	$ 149,133	16.87
Liabilities				
Payables	$ 17,621	$ 17,715	$ (94)	(0.53)
Securities Lending Collateral	65,311	70,207	(4,896)	(6.97)
Claims Incurred but Not Reported	20,040	18,262	1,778	9.74
Total Liabilities	102,972	106,184	(3,212)	(3.02)
Net Assets Held in Trust for Other Postemployment Benefits	**$ 930,278**	**$ 777,933**	**$ 152,345**	**19.58**

Summary Comparative Statement of Changes in Plan Net Assets
For the Fiscal Years Ended September 30, 2012 and 2011
(Amounts in Thousands)

	2012	2011	Variance	% Increase (Decrease)
Additions				
Contributions	$ 432,575	$ 392,332	$ 40,243	10.26
Interest and Dividend Income	22,882	19,739	3,143	15.92
Net Increase (Decrease) in Fair Value of Investments	101,185	(12,814)	113,999	889.64
Securities Lending Income, Net	583	533	50	9.38
Total Additions	557,225	399,790	157,435	39.38
Deductions				
Benefits	404,880	372,241	32,639	8.77
Net Increase	152,345	27,549	124,796	453.00
Net Assets Held in Trust for Other Postemployment Benefits				
Beginning of Year	777,933	750,384	27,549	3.67
End of Year	**$ 930,278**	**$ 777,933**	**$ 152,345**	**19.58**

Financial Highlights

- Investment sales receivable and investment purchases payable occur as a result of trade date accounting. The increase in the receivable and payable for fiscal year 2012 was due to the value of securities traded in the current fiscal year and settling in the following fiscal year being larger than the value of the securities accounted for using trade date accounting in the previous fiscal year.

- The Trust's annual rate of return on investments as calculated by State Street Bank and Trust Company, the Trust's investment custodian, was 15.26% for fiscal year 2012.

- Contributions to the Trust increased by 10.26% during the fiscal year as a result of increases in employer contributions, employee contributions, and subsidies from the Federal Government. For the 2012 fiscal year, the Trust received $27.98 million from its participation in the Retiree Drug Subsidy program (RDS). The Trust will continue to receive subsidies from the RDS program until December 31, 2012. The Employer Group Waiver Plan (EGWP) will replace the RDS program beginning January 1, 2013.

- Total investment income increased by 1,571.36% as a result of the significant increases in the fair value of investments experienced during the 2012 fiscal year.

- The Trust's benefit expenses increased by 8.77% during the fiscal year, primarily as a result of increases in the number of retirees participating in the healthcare plan.

ALABAMA RETIRED EDUCATION EMPLOYEES' HEALTH CARE TRUST

STATEMENT OF PLAN NET ASSETS

September 30, 2012 with comparative amounts shown for 2011

(Amounts in Thousands)

	2012	2011
Assets		
Receivables		
Rebates - Prescription Drug Plan Manufacturer Rebates	**$ 3,968**	$ 3,474
Medicare Part D Subsidy	**5,350**	3,429
Interest and Dividends	**3,810**	3,644
Investment Sales Receivable	**1,343**	8
Total Receivables	**14,471**	10,555
Deposit with Claims-Paying Agent	**200**	667
Investments, at Fair Value (Note 7)		
Commercial Paper	**99,997**	112,996
Money Market Funds	**41,173**	35,339
U.S. Government Guaranteed Bonds	**96,914**	87,124
U.S. Agency Securities	**33,382**	31,077
Mortgage-backed Securities	**46,862**	37,762
Corporate Bonds	**120,910**	103,426
International Securities	**97,602**	89,275
Common Stocks	**416,428**	305,689
Total Investments	**953,268**	802,688
Invested Securities Lending Collateral (Note 7)	**65,311**	70,207
Total Assets	**1,033,250**	884,117
Liabilities		
Reported Claims Payable	**14,679**	16,148
Investment Purchases Payable	**2,942**	1,567
Claims Incurred but Not Reported	**20,040**	18,262
Securities Lending Collateral (Note 7)	**65,311**	70,207
Total Liabilities	**102,972**	106,184
Net Assets Held in Trust for Other Postemployment Benefits	**$ 930,278**	$ 777,933

See accompanying Notes to the Financial Statements.

ALABAMA RETIRED EDUCATION EMPLOYEES' HEALTH CARE TRUST
STATEMENT OF CHANGES IN PLAN NET ASSETS

For the Fiscal Year Ended September 30, 2012 with comparative amounts shown for 2011

(Amounts in Thousands)

	2012	2011
Additions		
Contributions		
Employee (Note 3)	**$ 97,392**	$ 91,351
Employer (Note 3)	**307,206**	265,062
Early Retiree Reinsurance Program	**-**	10,844
Medicare Part D Retiree Drug Subsidy	**27,977**	25,075
Total Contributions	**432,575**	392,332
Investment Income (Note 7)		
From Investing Activities		
Net Increase (Decrease) in Fair Value of Investments	**101,185**	(12,814)
Interest and Dividends	**22,882**	19,739
Total Investment Income from Investing Activities	**124,067**	6,925
From Securities Lending Activities		
Securities Lending Income	**814**	743
Less Securities Lending Expenses:		
Borrower Rebates	**22**	36
Management Fees	**209**	174
Total Securities Lending Expenses	**231**	210
Income from Securities Lending Activities, Net	**583**	533
Total Investment Income	**124,650**	7,458
Total Additions	**557,225**	399,790
Deductions		
Benefits	**404,880**	372,241
Total Deductions	**404,880**	372,241
Net Increase	**152,345**	27,549
Net Assets Held in Trust for Other Postemployment Benefits		
Beginning of Year	**777,933**	750,384
End of Year	**$ 930,278**	$ 777,933

See accompanying Notes to the Financial Statements.

ALABAMA RETIRED EDUCATION EMPLOYEES' HEALTH CARE TRUST
Notes to the Financial Statements
For the Fiscal Year Ended September 30, 2012

1) Plan Description

The Alabama Retired Education Employees' Health Care Trust (Trust) is a cost-sharing multiple-employer defined benefit postemployment healthcare plan that administers healthcare benefits to the retirees of participating state and local educational institutions. The Trust was established under the Alabama Retiree Health Care Funding Act of 2007 which authorized and directed the Public Education Employees' Health Insurance Board (Board) to create an irrevocable trust to fund postemployment healthcare benefits to retirees. Active and retiree health insurance benefits are paid through the Public Education Employees' Health Insurance Fund (PEEHIF). In order to comply with the reporting requirements of GASB Statement 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, the contributions (employer, plan member, and Medicare Part D Retiree Drug Subsidy) and retiree benefit payments that are processed through the PEEHIF are segregated from the PEEHIF and reported as part of the Trust. In accordance with the Governmental Accounting Standards Board (GASB), the Trust is considered a component unit of the State of Alabama (State) and is included in the State's *Comprehensive Annual Financial Report*.

The PEEHIF was established in 1983 by the Alabama Legislature under the provisions of Act 83-455 to provide a uniform plan of health insurance for active and retired employees of state and local educational institutions which provide instruction at any combination of grades K-14 (collectively, eligible employees), and to provide a method for funding the benefits related to the plan. The four-year universities are eligible and may elect to participate in the plan. At this time, Jacksonville State is the only university with active and retired members that has elected to participate in the plan. Responsibility for the establishment of the health insurance plan and its general administration and operations is vested in the Board. The Board is a corporate body for purposes of management of the health insurance plan. The *Code of Alabama 1975, Section 16-25A-4* provides the Board with the authority to amend the benefit provisions in order to provide reasonable assurance of stability in future years for the plan. All assets of the PEEHIF are held in trust for the payment of health insurance benefits. The Teachers' Retirement System of Alabama (TRS) has been appointed as the administrator of the PEEHIF and, consequently, serves as the administrator of the Trust.

The assets of the Trust may not be used for any purpose other than to acquire permitted investments, pay administrative expenses, and provide postemployment healthcare benefits to or for retired employees and their dependents. The Alabama Legislature has no authority or power to appropriate the assets of the Trust. The Board periodically reviews the funds available in the PEEHIF and determines if excess funds are available. If excess funds are determined to be available in the PEEHIF, the Board authorizes a transfer of funds from the PEEHIF to the Trust.

As of September 30, 2012, there were 188 participating employers and 12 participating universities, and as of the latest actuarial valuation, there were 211,051 active and retired members.

The Public Education Employees' Health Insurance Plan (PEEHIP) offers a basic hospital medical plan to active members and non-Medicare eligible retirees. Benefits include inpatient hospitalization for a maximum of 365 days without a dollar limit, inpatient rehabilitation, outpatient care, physician services, and prescription drugs.

1) Plan Description, Continued

Active employees and non-Medicare eligible retirees who do not have Medicare eligible dependents can enroll in a health maintenance organization (HMO) in lieu of the basic hospital medical plan. The HMO includes hospital medical benefits, dental benefits, vision benefits, and an extensive formulary. However, participants in the HMO are required to receive care from a participating physician in the HMO plan.

The PEEHIP offers four optional plans (Hospital Indemnity, Cancer, Dental, and Vision) that may be selected in addition to or in lieu of the basic hospital medical plan or HMO. The Hospital Indemnity Plan provides a per-day benefit for hospital confinement, maternity, intensive care, cancer, and convalescent care. The Cancer Plan covers cancer disease only and benefits are provided regardless of other insurance. Coverage includes a per-day benefit for each hospital confinement related to cancer. The Dental Plan covers diagnostic and preventative services, as well as basic and major dental services. Diagnostic and preventative services include oral examinations, teeth cleaning, x-rays, and emergency office visits. Basic and major services include fillings, general aesthetics, oral surgery not covered under a Group Medical Program, periodontics, endodontics, dentures, bridgework, and crowns. Dental services are subject to a maximum of $1,250 per year for individual coverage and $1,000 per person per year for family coverage. The Vision Plan covers annual eye examinations, eye glasses, and contact lens prescriptions.

PEEHIP members may opt to elect the PEEHIP Supplemental Plan as their hospital medical coverage in lieu of the PEEHIP Hospital Medical Plan. The PEEHIP Supplemental Plan provides secondary benefits to the member's primary plan provided by another employer. Only active and non-Medicare retiree members and dependents are eligible for the PEEHIP Supplemental Plan. There is no premium required for this plan, and the plan covers most out-of-pocket expenses not covered by the primary plan. The plan cannot be used as a supplement to Medicare, the PEEHIP Hospital Medical Plan, or the State or Local Governmental Plans administered by the State Employees' Insurance Board (SEIB).

2) Summary of Significant Accounting Policies

A. Basis of Accounting

The Trust's financial statements are prepared under the accrual basis of accounting using the economic resources measurement focus. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions are recognized when due pursuant to plan requirements. Benefits are recognized when due and payable in accordance with the terms of the plan. Subsequent events were evaluated by management through the date the financial statements were issued.

B. Cash

Cash consists of deposits held by the State Treasurer in the Trust's name. Deposits are entirely insured by federal depository insurance or protected under the Security for Alabama Funds Enhancement (SAFE) Program. The *Code of Alabama 1975* requires all State organizations to participate in the SAFE Program. The SAFE Program is a multiple financial institution collateral pool. The SAFE Program requires all public funds to be deposited in a financial institution designated by the State Treasurer as a qualified public depository. Each qualified public depository is required to pledge collateral in accordance with the

B. Cash, Continued

rules established by the SAFE Board of Directors. In the event that a qualified public depository defaults or becomes insolvent and the pledged collateral is insufficient to satisfy the claims of public depositors, the *Code of Alabama 1975, Section 41-14A-9(3)* authorizes the State Treasurer to make assessments against the other qualified public depositories in the pool so that there will be no loss of public funds.

C. Investments

The Board has elected to have the Trust's assets invested by the Investment Staff of the TRS under the direction of the Secretary-Treasurer of the TRS. The Board has the responsibility and authority to invest and reinvest available funds, through the Secretary-Treasurer and Investment Committee, in bonds, mortgage-backed securities, common and preferred stock, and other investment vehicles with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use. All plan assets are carried at fair value. Securities traded on national or international exchanges are valued at the last reported sales price at current exchange rates. Short-term investments are reported at cost, which approximates fair value. Mortgage-backed securities are reported based on future principal and interest payments discounted at the prevailing interest rate for similar instruments. The fair value of real estate investments is based on independent appraisals or cost, when cost approximates fair value. Generally, private placements are valued based on the selling price of similar investments sold in the open market. In those instances where there are no similar investments sold in the open market, an independent appraisal is performed to determine the fair value of the private placements.

D. Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts and disclosures in the financial statements. Actual results may differ from these estimates.

E. Medicare Part D Retiree Drug Subsidy

Medicare Part D reimbursements are the result of the PEEHIF continuing prescription drug coverage for Medicare beneficiaries and qualifying for the Medicare Part D Retiree Drug Subsidy.

F. Early Retiree Reinsurance Program Reimbursement

The PEEHIF received funds during fiscal year 2011 from its participation in the Early Retiree Reinsurance Program (ERRP), which was established as part of the Patient Protection and Affordable Care Act. ERRP is a temporary program whereby Congress appropriated $5 billion to provide reimbursements to sponsors for 80% of the claims costs associated with providing health coverage to qualifying early retirees under the age of 65 (and their eligible dependents). While funds can only be received for the claims of qualifying early retirees (and dependents), reimbursements can be used for all plan participants, therefore, a portion of the reimbursements has been allocated to retired members and reported in the Alabama Retired Education Employees' Health Care Trust.

G. Unpaid Claims Liabilities

Claims liabilities are established based on the actual cost of claims reported but not settled and estimates of claims that have been incurred but not reported. Actual claims costs ultimately incurred may vary from estimated claims liabilities should the nature and frequency of actual claims vary from historical claims experience on which the estimates are based. Adjustments to claims liabilities are charged to expense in the periods in which they are made.

Unpaid claims liabilities are material estimates that are particularly susceptible to changes in the near term. Management believes the liabilities established for unpaid claims at September 30, 2012 are adequate to cover the ultimate net cost of claims, but the liabilities are necessarily based on estimates and accordingly, the amount ultimately paid will be more or less than such estimates.

H. Comparative Statements

The basic financial statements include the prior fiscal year *Statement of Plan Net Assets* and the *Statement of Changes in Plan Net Assets* for comparative purposes only. Prior fiscal year note disclosures are not included. Therefore, the prior fiscal year basic financial statement presentation does not meet the minimum level of detail required for a presentation in conformity with generally accepted accounting principles. Accordingly, the prior fiscal year statements should be read in conjunction with the Trust's prior fiscal year financial report from which the prior fiscal year statements were derived.

3) Contributions

The *Code of Alabama, Section 16-25A-8* provides the Board with the authority to set the contribution requirements for plan employers and members. On or before January 1 preceding each regular meeting of the Alabama Legislature, the Board is required to certify to the Governor and the Legislature, the amount, as a monthly premium per active employee, necessary to fund the coverage of active and retired member benefits for the following fiscal year. The Legislature then sets the premium rate in the annual appropriation bill.

The *Code of Alabama, Section, 16-25A-8.1* also provides the Board with the authority to set the employer contribution requirements for each retiree class.

For employees who retired after September 30, 2005, but before January 1, 2012, the employer contribution of the health insurance premium set forth by the Board for each retiree class is reduced by 2% for each year of service less than 25 and increased by 2% percent for each year of service over 25 subject to adjustment by the Board for changes in Medicare premium costs required to be paid by a retiree. In no case does the employer contribution of the health insurance premium exceed 100% of the total health insurance premium cost for the retiree.

3) Contributions, Continued

For employees who retired after December 31, 2011, the employer contribution to the health insurance premium set forth by the Board for each retiree class is reduced by 4% for each year of service less than 25 and increased by 2% for each year over 25, subject to adjustment by the Board for changes in Medicare premium costs required to be paid by a retiree. In no case does the employer contribution of the health insurance premium exceed 100% of the total health insurance premium cost for the retiree.

For employees who retired after December 31, 2011, who are not covered by Medicare, regardless of years of service, the employer contribution to the health insurance premium set forth by the Board for each retiree class is reduced by a percentage equal to 1% multiplied by the difference between the Medicare entitlement age and the age of the employee at the time of retirement as determined by the Board. This reduction in the employer contribution ceases upon notification to the Board of the attainment of Medicare coverage.

Each year, the State specifies the monthly employer rate that participating school systems must contribute for each active employee. The monthly employer rate for fiscal year 2012 was $714 per active participant. In accordance with the 2012 budget established by the Alabama Legislature, participating school systems paid the required monthly employer rate of $714 on behalf of each active employee. Approximately, 32.05% of the employer contributions were used to assist in funding retiree benefit payments in 2012. Act 2003-473 requires universities who do not participate in the PEEHIP to pay the required monthly rate for each university retiree who participates in the plan. The required monthly employer rate for fiscal year 2012 was $370 per university retiree.

In addition to the employer payments each month, retirees are required to pay certain premium amounts. The required monthly contribution rates for fiscal year 2012 are as follows:

Retired Member Rates

-Individual Coverage/Non-Medicare Eligible - $151.00
-Family Coverage/Non-Medicare Eligible Retired Member and Non-Medicare Eligible Dependent(s) - $391.00
-Family Coverage/Non-Medicare Eligible Retired Member and Dependent Medicare Eligible - $250.00
-Individual Coverage/Medicare Eligible Retired Member - $10.00
-Family Coverage/Medicare Eligible Retired Member and Non-Medicare Eligible Dependent(s) - $250.00
-Family Coverage/Medicare Eligible Retired Member and Dependent Medicare Eligible - $109.00
-Tobacco surcharge - $28.00 per month
-PEEHIP Supplemental Plan - $0
-Optional Plans (Hospital Indemnity, Cancer, Dental, Vision) – up to two optional plans can be taken by retirees at no cost if the retiree is not also taking one of the Hospital Medical Plans. The combining allocation program is being phased out over three years beginning October 1, 2010. While a couple combines allocations, they are required to use both allocations to pay for the PEEHIP Hospital Medical Plan and cannot use one of the allocations towards the Optional Plans. They can purchase the Optional Plans at the normal monthly rate of $38.00 or $45.00 for family dental.
-Members who retired on or after October 1, 2005, and before January 1, 2012, pay two percent of the employer premium for each year under 25 years of service, and for each year over 25 years of service, the retiree premium is reduced by two percent.

3) Contributions, Continued

-Employees who retire on or after January 1, 2012, with less than 25 years of service, are required to pay 4% for each year under 25 years of service. Additionally, non-Medicare eligible employees who retire on or after January 1, 2012 are required to pay 1% more for each year less than age 65 (age premium) and to pay the net difference between the active employee subsidy and the non-Medicare eligible retiree subsidy (subsidy premium). When the retiree becomes Medicare eligible, the age and subsidy premium no longer applies. However, the years of service premium (if applicable to the retiree) will continue to be applied throughout retirement. These changes are being phased in over a five year period.

Surviving Spouse Rates
-Surviving Spouse Non-Medicare Eligible - $658.00
-Surviving Spouse Non-Medicare Eligible and Dependent Non-Medicare Eligible - $847.00
-Surviving Spouse Non-Medicare Eligible and Dependent Medicare Eligible - $816.00
-Surviving Spouse Medicare Eligible - $328.00
-Surviving Spouse Medicare Eligible and Dependent Non-Medicare Eligible - $517.00
-Surviving Spouse Medicare Eligible and Dependent Medicare Eligible - $486.00

4) Funding Status and Funding Progress

As of the most recent actuarial valuation, the funded status of the plan was as follows:

FUNDED STATUS
(Amounts in Thousands)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b) §	Unfunded AAL (UAAL) (b-a)	Funded Ratio (%) (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
09/30/2011	$ 777,933	$ 9,081,335	$ 8,303,402	8.6%	$ 6,159,562	134.8%

§ Projected Unit Credit

The required schedule of funding progress immediately following the *Notes to the Financial Statements* presents multi-year trend information related to the changes in the actuarial value of plan assets over time relative to the actuarial accrued liability for benefits.

5) Actuarial Method and Assumptions

The projection of future benefit payments for an ongoing plan involves estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Therefore, the actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. The actuarial calculations are based on the benefits provided under the terms of the plan in effect at the time of each valuation and on the pattern of sharing of costs between the employer and plan members to that point. The valuation does not anticipate future changes in the pattern of sharing of costs between employers and plan members. The methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities, consistent with the long-term perspective of the calculations. Information related to the most recent actuarial valuation, including the actuarial method and assumptions is as follows:

Valuation Date	9/30/2011
Actuarial Cost Method	Projected Unit Credit
Amortization Method	Level percent of pay, open
Remaining Amortization Period	30 years, closed
Asset Valuation Method	Market Value of Assets
Actuarial Assumptions:	
Investment Rate of Return*	5.00%
Medical Cost Trend Rate*	
Pre-Medicare	9.50%
Medicare Eligible	7.50%
Ultimate Trend Rate	
Pre-Medicare	5.00%
Medicare Eligible	5.00%
Year of Ultimate Trend Rate	2017
Dental Trend Rate	5.00%

* Includes inflation at 3.25%

6) Contract Administrators

Blue Cross and Blue Shield of Alabama (BCBS), under contract with the Board, administered medical claims incurred in accordance with the plan. The BCBS administrative fee was $10.45 per month per contract.

MedImpact, under contract with the Board, administered claims under the prescription drug plan. The MedImpact administrative fee was $0.75 per prescription.

Southland Benefit Solutions, LLC (Southland) under contract with the Board, administered claims under the optional plans. The PEEHIF paid Southland an amount equal to covered charges plus processing fees. The processing fees per month per contract were $0.75 for Group Hospital Indemnity, $0.61 for Group Cancer, $1.08 for Group Vision, and $1.40 for Group Dental.

7) Investments

A. Investment Risks

Investments are subject to certain types of risks, including interest rate risk, custodial credit risk, credit quality risk, and foreign currency risk. The following describes those risks and the Trust's policies regarding those risks:

Interest Rate Risk – The fair value of fixed-maturity investments fluctuate in response to changes in market interest rates. Increases in prevailing interest rates generally translate into decreases in the fair value of those instruments. The fair value of interest sensitive instruments may also be affected by the creditworthiness of the issuer, prepayment options, relative values of alternative investments, and other general market conditions. Certain fixed maturity investments have call provisions that could result in shorter maturity periods.

Custodial Credit Risk – Custodial credit risk is the risk that an entity will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party if the counterparty fails. The Trust's custodial credit risk policy requires the custodial agent to hold or direct its agents or sub custodians to hold, for the account of the Trust, all securities and other non-cash property other than securities in the Federal Reserve book-entry system, in a clearing agency which acts as a securities depository, or in another book-entry system. The Trust's safekeeping agent holds all investments of the Trust in the Trust's name with the exception of securities purchased with securities lending cash collateral.

Credit Quality – Nationally recognized statistical rating organizations provide ratings of debt securities quality based on a variety of factors, such as the financial condition of the issuers, which provide investors with some idea of the issuer's ability to meet its obligations. Domestic fixed-maturity investments may consist of rated or non-rated securities. The Trust may hedge against the possible adverse effects of currency fluctuations on its portfolio of international fixed income obligations when it is considered appropriate. Short-term investments may consist of commercial paper rated at least A-2 and/or P-2, repurchase agreements, short-term U.S. securities, and other money market investments.

A. Investment Risks, Continued

Foreign Currency Risk – Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. In order for an international security to be eligible for purchase by the Trust, the issuing company must be incorporated in a country whose debt securities are eligible for purchase as discussed above, and the fair value of the aggregate outstanding equity of the issuing company must be at least $100 million.

Concentration of Credit Risk – The investment policies limit the aggregate amount that can be invested in each class of investments. The policy limits are as follows:

- Domestic Fixed Income – Limited to 50% of the fair value of the Trust's aggregate portfolio.
- International Fixed Income – Limited to 10% of the fair value of the Trust's total portfolio.
- Domestic Equity – Limited to 65% of the fair value the Trust's aggregate portfolio.
- International Equity – Limited to 25% of the aggregate fair value of the Trust's total portfolio. The Trust may not purchase or hold more than 5% of any class of the outstanding stock of a company.
- Real Estate – Limited to 15% of the book value of the Trust's portfolio.
- Alternative Investments (mezzanine financing, LBO's, venture capital, limited partnerships, futures, commodities and derivative investments) - Limited to 10% of the book value of the Trust's aggregate portfolio.
- Short-term Investments – Limited to 20% of the fair value of the Trust's aggregate portfolio.

A. Investment Risks, Continued

The following table provides information concerning the fair value and interest rate risk of the Trust's investments as of September 30, 2012.

INVESTMENTS
Maturity in Years at Fair Value
(Amounts in Thousands)

Type of Investment	Less Than 1	1-5	6-10	More Than 10	Total Fair Value	Cost
Fixed Maturity						
Money Market Funds	$ 41,173	$ -	$ -	$ -	$ 41,173	$ 41,173
Commercial Paper	99,997	-	-	-	99,997	99,997
U.S Agency	-	19,420	12,113	1,849	33,382	30,676
U.S. Government Guaranteed	-	33,560	58,471	4,883	96,914	91,858
Corporate Bonds	30,924	35,723	36,200	18,063	120,910	110,667
GNMAs	-	-	-	7,900	7,900	7,656
Collateralized Mortgage Obligations	-	-	1,506	37,456	38,962	37,896
Total Fixed Maturity	$ 172,094	$ 88,703	$ 108,290	$ 70,151	439,238	419,923
Equities						
Domestic					416,428	342,805
International						
Emerging Markets						
United Kingdom - Pound Sterling					22,772	23,691
Japan - Yen					19,672	23,990
France - Euro					8,968	11,816
Germany - Euro					8,355	9,547
Switzerland - Franc					8,590	8,057
Netherlands - Euro					2,495	3,173
Italy - Euro					2,127	3,741
Spain - Euro					2,745	4,726
Australia - Dollar					8,775	8,165
Singapore - Dollar					1,871	1,555
Belgium - Euro					1,163	1,161
Finland - Euro					701	1,647
Hong Kong - Dollar					3,065	2,785
Sweden - Krona					3,171	2,626
Denmark - Krone					1,206	883
Israel - Shekel					570	720
Norway - Krone					995	911
Austria - Euro					276	417
New Zealand - Dollar					85	87
Total International Equities					97,602	109,698
Total Equities					514,030	452,503
Total Investments					**$ 953,268**	**$ 872,426**

A. Investment Risks, Continued

The following table provides information concerning the credit risk of the Trust's investments as of September 30, 2012.

RATINGS OF FIXED MATURITIES

Moody's Ratings	Cost	Fair Value	Fair Value as a Percent of Total Fixed Maturity Fair Value (%)
Aaa [1]	$ 158,258	$ 166,107	37.82
Aa1	28,451	29,971	6.82
Aa2	751	877	0.20
Aa3	2,762	3,585	0.82
P-1	41,173	41,173	9.37
P-2	99,998	99,998	22.77
A1	7,920	9,159	2.09
A2	10,146	11,512	2.62
A3	14,161	15,047	3.43
Baa1	16,122	18,579	4.23
Baa2	21,591	23,476	5.34
Baa3	9,242	9,560	2.18
Ba1	2,511	2,853	0.65
Ba3	485	473	0.10
B1	788	934	0.21
Not Rated [2]	5,564	5,934	1.35
Total Fixed Maturity	**$ 419,923**	**$ 439,238**	**100.00**

Standard & Poor's Ratings	Cost	Fair Value	Fair Value as a Percent of Total Fixed Maturity Fair Value (%)
AA+ [1]	$ 163,317	$ 172,051	39.17
AA	24,082	24,858	5.66
AA-	2,477	3,174	0.72
A-1+	41,173	41,173	9.37
A-1	9,999	9,999	2.28
A-2	89,998	89,998	20.49
A+	4,971	5,600	1.27
A	8,804	10,047	2.29
A-	19,405	20,734	4.72
BBB+	13,746	15,032	3.42
BBB	26,263	29,286	6.67
BBB-	1,547	1,734	0.39
BB+	2,586	2,704	0.62
B+	1,445	1,476	0.34
Not Rated [2]	10,110	11,372	2.59
Total Fixed Maturity	**$ 419,923**	**$ 439,238**	**100.00**

[1] Includes securities guaranteed by the US Gov't

[2] Primarily consists of private placements

B. Concentration of Investments

As of September 30, 2012, the Trust had no securities that constituted more than 5% of the total fair value of investments.

C. Securities Lending Program

The Trust is authorized to participate in a securities lending program. The Trust's custodian, State Street Bank and Trust Company (State Street), administers the program. Certain securities from the Trust are loaned to borrowers approved by the Trust for collateral that will be returned for the same security in the future. Approved borrowers provide acceptable collateral in the form of cash (U.S. dollar and foreign currency), U.S. and non U.S. equities, assets permissible under Rule 15c3-3 under the Exchange Act of 1934, and other collateral as the parties may agree to in writing from time to time. All security loans are open loans and can be terminated on demand by the Trust or borrower. The initial collateral received shall have (depending on the nature of the loaned securities and the collateral received), a value of 102% or 105% of the fair value of the loaned securities, or such other value, not less than 102% of the fair value of the loaned securities, as may be applicable in the jurisdiction in which such loaned securities are customarily traded. Pursuant to the terms of the applicable securities loan agreement, State Street shall, in accordance with State Street's reasonable and customary practices, mark loaned securities and collateral to their fair value each business day based upon the fair value of the collateral and the loaned securities at the close of business, employing the most recently available pricing information and shall receive and deliver collateral in order to maintain the value of the collateral at no less than 100% of the fair value of the loaned securities.

The Trust cannot pledge or sell collateral securities received unless the borrower defaults. Cash collateral is invested in the State Street Global Securities Lending Trust (GSLT). The collateral fund is separated into two pools, a liquidity pool and a duration pool. The split allows greater flexibility in managing the available liquidity of the investment in the fund and the outstanding balance of securities on loan.

The following describes the GSLT's guidelines for the liquidity pool: The GSLT's Investment Manager shall maintain the dollar-weighted average maturity of GSLT in a manner that the Investment Manager believes is appropriate to the objective of the GSLT, provided that (i) in no event shall any eligible security be acquired with a remaining legal final maturity (i.e. the date on which principal must be repaid) of greater than 18 months, (ii) the Investment Manager shall endeavor to maintain a dollar-weighted average maturity of the GSLT not to exceed 75 calendar days, and (iii) the Investment Manager shall endeavor to maintain a dollar-weighted average maturity to final of GSLT not to exceed 180 calendar days. Additionally, at the time of purchase, all eligible securities with maturities of 13 months or less shall be rated at least A1, P1, or F1 by at least two of the following nationally recognized statistical rating organizations: Standard & Poor's Corp. ("S&P"), Moody's Investor Services, Inc. ("Moody's"), or Fitch, Inc. ("Fitch"), or be determined by the Investment Manager to be of comparable quality. Additionally, all eligible securities with maturities in excess of 13 months shall be rated at least A-, A3, or A- by at least two of the following nationally recognized statistical rating organizations: S & P, Moody's, or Fitch, or be determined by the Investment Manager to be of comparable quality. The GSLT may invest up to 10% of its assets at the time of purchase in commingled vehicles managed by the Trustee or its affiliates that conform to the Investment Policy Guidelines.

C. Securities Lending Program, Continued

The following describes the GSLT's guidelines for the duration pool: The GSLT duration pool includes all GSLT asset-backed securities (regardless of maturity) and securities of any type with a remaining maturity of 91 days or greater. Each GSLT investor owns a specified percentage interest in the duration pool which is redeemable only in kind, not in cash. The GSLT duration pool will not make additional investments.

As of September 30, 2012, the average loan term was 57 days. Cash collateral investments in the GSLT are matured as needed to fulfill loan obligations. There is no direct matching of the maturities of the loans with the investments made with cash collateral.

The fair value of the securities on loan was $139,183,770 and the fair value of the collateral pledged by the borrowers was $146,046,506, as of September 30, 2012. Since the amounts owed by the Trust exceeded the amounts the borrowers owed to the Trust, there was no credit risk exposure as of September 30, 2012. Additionally, there were no significant violations of legal or contractual provisions, no borrower or lending agent default losses, and no recoveries of prior period losses during the fiscal year.

Investments purchased with cash collateral are held by the custodial agent, but not in the name of the Trust. Securities pledged as collateral are held by the custodial agent, but not in the name of the Trust. Letters of credit pledged as collateral are issued by the borrower's bank and are irrevocable. Tri party collateral is held by a third party bank in the name of the custodial agent. State Street, as custodial agent, is authorized to request a third party bank to undertake certain custodial functions in connection with holding of the collateral provided by a borrower.

C. Securities Lending Program, Continued

The following table provides information as of September 30, 2012, concerning securities lent:

SECURITIES LENDING - INVESTMENTS LENT AND COLLATERAL RECEIVED
(Fair Value - Amount in Thousands)

Type of Investment Lent		**Amounts**
For Cash Collateral		
Domestic Fixed Maturities	$	24,581
Domestic Equity		35,940
International Equity		3,084
Total Lent for Cash Collateral		63,605
For Non-cash Collateral		
Domestic Fixed Maturities		54,110
Domestic Equity		7,858
International Equity		13,611
Total Lent for Non-cash Collateral		75,579
Total Securities Lent	**$**	**139,184**
Type of Collateral Received		
Cash Collateral - Invested in State Street Global Securities Lending Trust	$	65,311
Non-cash Collateral		
For Lent Domestic Fixed Securities		56,140
For Lent Domestic Equity Securities		
US Dollar		9,515
For Lent International Equity Securities		
Securities Collateral		
EURO		1,650
GBP		1,136
US Dollar		12,295
Total Non-cash Collateral		80,736
Total Collateral Received	**$**	**146,047**

8) Unpaid Claims Liabilities

As discussed in Note 1, the Trust establishes a liability for both reported and unreported insured claims. This liability includes provisions for the future payment of losses and related claim adjustment expenses. The following represents changes in those aggregate liabilities for the Trust during fiscal year 2012.

UNPAID CLAIMS LIABILITIES
(Amounts in Thousands)

Unpaid Claims and Claim Adjustment Expenses at Beginning of Year	$ 34,410
Incurred Claims and Claim Adjustment Expenses:	
Provision for Insured Events of the Current Year	405,257
Decrease in Provision for Insured Events for Prior Years	(377)
Total Incurred Claims and Claim Adjustment Expenses	404,880
Payments:	
Claims and Claim Adjustment Expenses Attributable to Insured Events of the Current Year	370,538
Claims and Claim Adjustment Expenses Attributable to Insured Events of the Prior Years	34,033
Total Payments	404,571
Total Unpaid Claims and Claim Adjustment Expenses at the End of the Year	$ 34,719

ALABAMA RETIRED EDUCATION EMPLOYEES' HEALTH CARE TRUST
Required Supplementary Information
For the Fiscal Year Ended September 30, 2012

SCHEDULE OF FUNDING PROGRESS
(Amounts in Thousands)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (%) (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
9/30/2011	$ 777,933	$ 9,081,335	$ 8,303,402	8.6%	$ 6,159,562	134.8%
9/30/2010	750,384	11,584,965	10,834,581	6.5%	6,183,204	175.2%
9/30/2009	670,004	11,915,692	11,245,688	5.6%	6,236,922	180.3%
9/30/2008	579,813	13,224,411	12,644,598	4.4%	6,294,341	200.9%
9/30/2007	400,783	12,965,398	12,564,615	3.1%	5,897,772	213.0%
9/30/2006	-	12,532,330	12,532,330	-	5,458,443	229.6%

SCHEDULE OF CONTRIBUTIONS FROM THE EMPLOYERS AND OTHER CONTRIBUTING ENTITIES
(Amounts in Thousands)

Fiscal Year Ended	Annual Required Contribution	Percentage Contributed (%)
2012	864,503	38.6
2011	1,006,034	29.9
2010	970,330	37.0

ALABAMA RETIRED EDUCATION EMPLOYEES' HEALTH CARE TRUST
Supplementary Information
For the Fiscal Year Ended September 30, 2012

Claims Development Information

(Amounts in Thousands)

The table below illustrates the historical trend information designed to provide information on how the Trust's earned revenues and interest income compare to the related claims costs and other expenses assumed by the Trust as of the end of the fiscal year. (1) This line shows the total earned contribution and investment revenues for each fiscal year. (2) This line shows the other operating costs of the Trust including overhead and claims expenses not allocable to individual claims for each fiscal year. (3) This line shows the Trust's incurred claims and allocated claims adjustment expenses (both paid and accrued) as originally reported at the end of the first year in which the event that triggered coverage under the contract occurred (policy year). (4) This line shows the cumulative amounts paid as of the end of successive years for each policy year. (5) This line shows how the incurred claims for each policy year increased or decreased as of the end of successive years. The annual re-estimated amount results from new information received on known claims, the re-evaluation of existing information on known claims as well as the emergence of previously unknown claims. (6) This line compares the latest re-estimated incurred claims amount to the amount originally established (line 3) and shows whether it is greater or less than originally thought. As data for each policy year matures, the correlation between original estimates and re-estimated amounts is commonly used to evaluate the accuracy of estimated incurred claims currently recognized.

	Fiscal & Policy Year Ended					
	2012	2011	2010	2009	2008	2007
1) Net Earned Required Contribution & Investment Revenue	557,225	399,790	486,599	445,826	506,402	729,253
2) Unallocated Expenses	-	-	-	-	-	-
3) Estimated Incurred Claims & Expense, End of Policy Year	405,257	371,964	405,082	358,293	335,601	328,470
4) Paid (Cumulative) As Of:						
End of Policy Year	370,538	337,554	369,699	325,011	302,514	301,214
One Year Later		371,587	405,359	359,430	332,943	329,529
5) Reestimated Incurred Claims & Expense:						
End of Policy Year	405,257	371,964	405,082	358,293	335,601	328,470
One Year Later		371,587	405,359	359,430	332,943	329,529
6) Increase/(Decrease) in Estimated Incurred Claims & Expenses						
End of Policy Year		(377)	277	1,137	(2,658)	1,059