KPMG

STATE OF ALASKA RETIREE HEALTH FUND

(A Pension Trust Fund of the State of Alaska)

Financial Statements

June 30, 2010 and 2009

(With Independent Auditors' Report Thereon)

STATE OF ALASKA RETIREE HEALTH FUND
(A Pension Trust Fund of the State of Alaska)

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KPMG LLP
Suite 600
701 West Eighth Avenue
Anchorage, AK 99501

Independent Auditors' Report

Division of Retirement and Benefits and
Members of the Alaska Retirement Management Board
State of Alaska Retiree Health Fund:

We have audited the accompanying statements of fiduciary net assets of the State of Alaska Retiree Health Fund (Plan), a Pension Trust Fund of the State of Alaska, as of June 30, 2010 and 2009, and the related statements of changes in fiduciary net assets for the years then ended. These financial statements are the responsibility of the Plan's management. Our responsibility is to express an opinion on these 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 audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the fiduciary net assets of the State of Alaska Retiree Health Fund as of June 30, 2010 and 2009, and the changes in fiduciary net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Management's Discussion and Analysis is not a required part of the financial statements, but is supplementary information required by the Governmental Accounting Standards Board (GASB). We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit this information and express no opinion on it.

KPMG LLP

October 29, 2010

This section presents management's discussion and analysis (MD&A) of the Retiree Health Fund's (Plan) financial condition and performance for the years ended June 30, 2010 and 2009. This section is presented as a narrative overview and analysis. Please read the MD&A in conjunction with the financial statements and notes to the financial statements to better understand the financial condition and performance of the Plan during the fiscal years ended June 30, 2010 and 2009. Information for fiscal year 2008 is presented for comparative purposes.

Financial Highlights

The Plan's total net assets held in trust for postemployment healthcare benefits as of June 30, 2010 and 2009 are $195,565,020 and $165,572,103, respectively.

The Plan's total net assets held in trust for postemployment healthcare benefits as of June 30, 2010 and 2009 increased by $29,992,917 or 18.1% and decreased by $12,503,194 or 6.8% over the closing balances of those assets in fiscal years 2009 and 2008.

Health premiums totaled $49,981,997 and $47,108,376 during fiscal years 2010 and 2009, respectively, an increase of $2,873,621 or 6.1% and an increase of $3,216,561 or 7.3% from fiscal years 2009 and 200, respectively.

Net investment income increased from a loss of $23,283,038 during fiscal 2009 to a gain of $19,925,906 during fiscal year 2010 and decreased from a loss of $6,960,689 during fiscal 2008 to a loss of $23,283,038 during fiscal year 2009.

Benefit expenses totaled $38,686,919 and $38,473,565 during fiscal years 2010 and 2009, respectively, a increase of $213,354 or 0.6% and a decrease of $156,137,419 or 80.2% from fiscal years 2009 and 2008. Decrease from fiscal year 2008 to 2009 was due to the creation of the Alaska Retiree Health Care Trust (ARHCT).

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the Plan's basic financial statements. The Plan's basic financial statements are comprised of three components: (1) statement of fiduciary net assets, (2) statement of changes in fiduciary net assets, and (3) notes to financial statements.

Statement of Fiduciary Net Assets – This statement presents information regarding the Plan's assets, liabilities, and resulting net assets held in trust for postemployment healthcare benefits. This statement reflects the Plan's investments at fair market value, along with cash and short-term investments, receivables, and other assets less liabilities at June 30, 2010 and 2009.

Statement of Changes in Fiduciary Net Assets – This statement presents how the Plan's net assets held in trust for postemployment healthcare benefits changed during the fiscal years ended June 30, 2010 and 2009. This statement presents health premiums earned and net investment income (loss) during the period. Deductions for postemployment healthcare benefits and operating deductions are also presented.

The above statements represent resources available for investment and payment of benefits as of the fiscal year–end and the sources and uses of those funds during the fiscal year.

Notes to Financial Statements – The notes to financial statements are an integral part of the financial statements and provide additional detailed information and schedules to better understand the Plan's financial statements.

Condensed Financial Information

Fiduciary Net Assets

Description	2010	2009	Increase (decrease) Amount	Increase (decrease) Percentage	2008
Assets:					
Cash and receivables	$ 36,325,225	37,957,666	(1,632,441)	(4.3)%	$ 28,438,971
Due from other funds	—	—	—	—	5,493,278
Investments, at fair value	186,494,644	154,418,451	32,076,193	20.8	162,890,166
Other	351,455	351,455	—	—	—
Total assets	223,171,324	192,727,572	30,443,752	15.8	196,822,415
Liabilities:					
Claims payable	20,434,000	19,700,286	733,714	3.7	15,568,302
Accrued expenses	151,363	141,883	9,480	6.7	2,577,741
Due to other funds	7,020,941	7,313,300	(292,359)	(4.0)	1,051,075
Total liabilities	27,606,304	27,155,469	450,835	1.7	19,197,118
Total net assets	$ 195,565,020	165,572,103	29,992,917	18.1%	$ 177,625,297

Changes in Fiduciary Net Assets

Description	2010	2009	Increase (decrease) Amount	Increase (decrease) Percentage	2008
Net assets, beginning of year	$ 165,572,103	177,625,297	(12,053,194)	(6.8)%	$ 332,799,401
Additions (reductions):					
Healthcare premiums	49,981,997	47,108,376	2,873,621	6.1	43,891,815
Medicare retiree drug subsidy	58,586	2,720,681	(2,662,095)	(97.8)	14,288,617
Other	27,790	1,599,489	(1,571,699)	(98.3)	2,564,550
Net investment income (loss)	19,925,906	(23,283,038)	43,208,944	185.6	(6,960,689)
Total additions	69,994,279	28,145,508	41,848,771	148.7	53,784,293
Deductions:					
Benefits	38,686,919	38,473,565	213,354	0.6	194,610,984
Administrative	1,314,443	1,725,137	(410,694)	(23.8)	14,347,413
Total deductions	40,001,362	40,198,702	(197,340)	(0.5)	208,958,397
Increase (decrease) in net assets	29,992,917	(12,053,194)	42,046,111	(348.8)	(155,174,104)
Net assets, end of year	$ 195,565,020	165,572,103	29,992,917	18.1%	$ 177,625,297

Financial Analysis of the Plan

The Statements of Fiduciary Net Assets as of June 30, 2010 and 2009 showed net assets held in trust for postemployment healthcare benefits of $195,565,020 and $165,572,103, respectively. The entire amount is available to cover the Plan's obligations to pay postemployment healthcare benefits for its members and their beneficiaries.

These amounts also represent an increase in total net assets held in trust for postemployment healthcare benefits of $29,992,917 or 18.1% and a decrease of $12,053,194 or 6.8% over fiscal years 2009 and 2008, respectively. Beginning on July 1, 2007, the Alaska Retiree Healthcare Trust (ARHCT) replaced the major medical fund of the Plan for retired members and beneficiaries covered under Public Employees' Retirement System (PERS), Teachers' Retirement System (TRS), and Judicial Retirement System (JRS). Previously, these Systems had paid a monthly health insurance premium to the Plan. With the creation of the ARHCT, participating PERS, TRS, and JRS employer contributions were deposited directly to the ARHCT replacing the monthly health insurance premiums. Healthcare coverage is still accounted for some retired members, dependents, and beneficiaries in the major medical fund via monthly health insurance premiums. Over the long term, healthcare premiums collected for the Dental, Visual and Audio (DVA) and Long-Term Care (LTC) funds are expected to cover all claims costs. With continued increases in healthcare costs, the Plan must continue to accumulate assets to meet current and future claims costs.

The investment of Plan assets is a long–term undertaking. On an annual basis, the Commissioner of Revenue reviews the asset allocation policies related to Plan assets and adopts an asset allocation strategy to ensure the asset mix will remain at an optimal risk/return level given the Plan's constraints and objectives.

(Continued)

In fiscal years 2010 and 2009, the Department of Revenue allocated invested assets in the following manner:

	2010		
	Major Medical	**Dental, Visual and Audio**	**Long-term Care**
General Fund and Other Non Segregated Investments	—%	100%	—%
Broad domestic equity	—	—	26
Short-term fixed income pool	100	—	1
International equity	—	—	22
Domestic equity	—	—	48
U.S. Treasury fixed income	—	—	3
Total	100%	100%	100%

	2009		
	Major Medical	**Dental, Visual and Audio**	**Long-term Care**
General Fund and Other Non Segregated Investments	—%	100%	—%
Broad domestic equity	—	—	28
Short-term fixed income pool	100	—	1
International equity	—	—	21
Domestic equity	—	—	50
Total	100%	100%	100%

Premium Calculations

The overall objective of the Plan is to have sufficient funds to meet claim costs. The premiums are recommended each year by the Division of Retirement and Benefits' (Division) benefit consultant with the governing body's concurrence and the Administrator's approval. Premiums are based on a calendar year. The benefit consultant reviews the historical claims experience and administrative costs and uses that data to estimate trends to develop recommended premiums for the next calendar year.

Healthcare Premiums and Investment Income

The additions required to fund postemployment healthcare benefits are accumulated through a combination of health premiums, prescription drug rebates, and net investment income.

	Additions (Reductions)				
			Increase (decrease)		
	2010	2009	Amount	Percentage	2008
Employer health premiums	$ 1,410,804	1,287,169	123,635	9.6%	$ 1,245,672
Member health premiums	48,571,193	45,821,207	2,749,986	6.0	42,646,143
Medicare retiree drug subsidy	58,586	2,720,681	(2,662,095)	(97.8)	14,288,617
Other	27,790	1,599,489	(1,571,699)	(98.3)	2,564,550
Net investment income (loss)	19,925,906	(23,283,038)	43,208,944	185.6	(6,960,689)
Total	$ 69,994,279	28,145,508	41,848,771	148.7%	$ 53,784,293

Premiums are $1,068 per month per person for calendar year 2010 and were $937 per month per person for calendar year 2009 and $876 per month person for calendar year 2008. The Division's consultant recommended a 14% premium increase and the Division remains vigilant of rising healthcare costs related to covered benefits.

Other income is primarily composed of reimbursements for retiree prescription medication. The Plan was approved for participation in the Medicare Part D retiree drug subsidy (RDS) program starting in calendar year 2006. One of the provisions of Medicare Part D provides sponsors of pension healthcare plans the opportunity to receive a payment, the retiree drug subsidy (RDS), if the sponsor's plan provides a prescription drug benefit that is actuarially equivalent to the Medicare Part D benefit. The RDS is equal to twenty–eight percent of the amount of eligible prescription drug benefit costs of retirees who are eligible for, but not enrolled in, Medicare Part D, by virtue of continuing to be covered by the sponsor's plan.

Net investment income increased by $43,208,944 or 185.6% from amounts recorded in fiscal year 2009. Net investment loss increased by $16,322,349 or 234.5% from amounts recorded in fiscal year 2008.

For fiscal years 2010 and 2009, the Retiree Health Fund Medical Plan investments generated 1.17% and 1.19% rate of return. The Retiree Health Fund Medical Plan annualized rate of return was 1.69% over the last three years and 3.08% over the last five years. For fiscal years 2010 and 2009, the Retiree Health Fund LTC Plan investments generated 12.48% and (14.84%) rate of return. The Retiree Health Fund LTC Plan annualized rate of return was (3.38%) over the last three years and 2.54% over the last five years. The Retiree Health Fund DVA Plan is invested in the General Fund and Other Non Segregated Investments (GeFONSI). The GeFONSI is an investment pool managed by the State of Alaska Treasury Division in the Department of Revenue. For fiscal years 2010 and 2009, the GeFONSI investments generated 3.38% and 4.24% rate of return. The GeFONSI annualized rate or return was 4.49% over the last three years and 4.39% over the last five years.

Benefits and Deductions

The primary deduction of the Plan is the payment of postemployment healthcare benefits. These benefit costs and the cost of administering the Plan comprises the costs of operation.

	Deductions				
			Increase (decrease)		
	2010	2009	Amount	Percentage	2008
Healthcare benefits	$ 38,686,919	38,473,565	213,354	0.6%	$ 194,610,984
Administrative	1,314,443	1,725,137	(410,694)	(23.8)	14,347,413
Total	$ 40,001,362	40,198,702	(197,340)	(0.5)%	$ 208,958,397

Benefit expense increased $213,354 and decreased $156,137,419 or 0.6% and 80.2% from fiscal years 2009 and 2008, respectively. The increase in fiscal year 2010 was due to increasing healthcare costs and an increase in covered members. Beginning on March 1, 2008, healthcare claims related to eligible members and dependents of the PERS, TRS, and JRS plans are paid from the respective ARHCT. Those retirees eligible for healthcare coverage but not eligible under PERS, TRS, or JRS health benefits are accounted for separately within the Plan. The Plan's benefit consultants identify and develop premiums necessary to cover the increased claims costs.

Funding

Postemployment healthcare benefits are funded by premiums received from the remaining participating retirement systems and plan members as well as from income earned on Plan investments. Healthcare premiums are recommended each year by the Division's consultant with the governing body's concurrence and the Administrator's approval.

Economic Conditions, Market Environment, and Results

The overall objective of the Plan is to have sufficient funds to meet current and future claim costs. The premiums for the major medical and DVA plans are calculated each year based on the anticipated claims and administrative costs for the following year. The benefit consultant reviews the historical claims experience and administrative costs and uses that data to estimate trends to develop premiums. The amount of reserves is considered when setting the premiums. The premiums for the LTC plan have been developed to provide future benefits for the retirees, much like an annuity. The LTC plan will accumulate large reserves to pay future benefits.

Requests for Information

This financial report is designed to provide a general overview of the Plan's financial condition for all those with interest in the Plan's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to:

State of Alaska Retiree Health Fund
Division of Retirement and Benefits, Accounting Section
P.O. Box 110203
Juneau, Alaska 99811–0203

STATE OF ALASKA RETIREE HEALTH FUND
(A Pension Trust Fund of the State of Alaska)

Statements of Fiduciary Net Assets

June 30, 2010 and 2009

	2010				2009			
	Major medical	**Dental, visual and audio**	**Long-term care**	**Total**	**Major medical**	**Dental, visual and audio**	**Long-term care**	**Total**
Assets:								
Cash and cash equivalents (notes 2 and 3):								
Investment in State of Alaska General Fund and other nonsegregated investments pool	$ —	15,800,372	—	15,800,372	—	16,603,395	—	16,603,395
Short-term fixed income pool	17,612,701	—	2,676,813	20,289,514	20,061,579	—	1,155,182	21,216,761
Total cash and cash equivalents	17,612,701	15,800,372	2,676,813	36,089,886	20,061,579	16,603,395	1,155,182	37,820,156
Investments (notes 2, 3 and 4):								
Broad market fixed income pool	—	—	48,885,994	48,885,994	—	—	—	—
Conservative fixed income pool	—	—	—	—	—	—	41,681,080	41,681,080
Domestic equity account	—	—	90,603,544	90,603,544	—	—	78,278,089	78,278,089
International equity pool	—	—	41,936,840	41,936,840	—	—	34,459,282	34,459,282
U.S. Treasury fixed income pool	—	—	5,068,266	5,068,266	—	—	—	—
Total investments	—	—	186,494,644	186,494,644	—	—	154,418,451	154,418,451
Other:								
Premiums receivable	93,524	26,420	54,344	174,288	45,544	3,152	2,548	51,244
Interest and dividends receivable	15,561	—	1,808	17,369	67,660	—	7,807	75,467
Other receivables	43,682	—	—	43,682	10,799	—	—	10,799
Other assets	32,346	281,717	37,392	351,455	32,346	281,717	37,392	351,455
Total other	185,113	308,137	93,544	586,794	156,349	284,869	47,747	488,965
Total assets	17,797,814	16,108,509	189,265,001	223,171,324	20,217,928	16,888,264	155,621,380	192,727,572
Liabilities:								
Claims payable (note 5)	163,000	2,987,000	17,284,000	20,434,000	179,948	4,487,627	15,032,711	19,700,286
Accrued expenses	18,022	84,933	48,408	151,363	17,130	95,208	29,545	141,883
Due to State of Alaska General Fund (note 2)	1,931,857	284,772	105,144	2,321,773	2,265,192	492,516	52,549	2,810,257
Due to PERS Alaska Retiree Health Care Trust	1,189,512	—	—	1,189,512	1,051,018	—	—	1,051,018
Due to TRS Alaska Retiree Health Care Trust	3,496,609	—	—	3,496,609	3,439,416	—	—	3,439,416
Due to JRS Alaska Retiree Health Care Trust	13,047	—	—	13,047	12,609	—	—	12,609
Total liabilities	6,812,047	3,356,705	17,437,552	27,606,304	6,965,313	5,075,351	15,114,805	27,155,469
Total net assets held in trust for postemployment healthcare benefits	$ 10,985,767	12,751,804	171,827,449	195,565,020	13,252,615	11,812,913	140,506,575	165,572,103

See accompanying notes to the financial statements.

STATE OF ALASKA RETIREE HEALTH FUND
(A Pension Trust Fund of the State of Alaska)

Statements of Changes in Fiduciary Net Assets

Years ended June 30, 2010 and 2009

		2010				2009			
		Major medical	**Dental, visual and audio**	**Long-term care**	**Total**	**Major medical**	**Dental, visual and audio**	**Long-term care**	**Total**
Additions (reductions):									
Contributions:									
Employer health insurance premiums	$	1,410,804	—	—	1,410,804	1,287,169	—	—	1,287,169
Member health insurance premiums		1,088,256	28,044,890	19,438,047	48,571,193	1,129,968	26,356,023	18,335,216	45,821,207
Total contributions		2,499,060	28,044,890	19,438,047	49,981,997	2,417,137	26,356,023	18,335,216	47,108,376
Medicare retiree drug subsidy (note 6)		58,586	—	—	58,586	2,719,561	—	1,120	2,720,681
Investment income (loss):									
Net appreciation (depreciation) in fair value		—	—	15,222,695	15,222,695	—	—	(27,435,994)	(27,435,994)
Interest		237,131	542,910	1,050,439	1,830,480	275,734	674,645	433,122	1,383,501
Dividends		—	—	2,930,345	2,930,345	—	—	2,848,627	2,848,627
Total investment income (loss)		237,131	542,910	19,203,479	19,983,520	275,734	674,645	(24,154,245)	(23,203,866)
Less investment expense		1,789	—	55,825	57,614	—	—	79,172	79,172
Net investment income (loss)		235,342	542,910	19,147,654	19,925,906	275,734	674,645	(24,233,417)	(23,283,038)
Other income		27,050	653	87	27,790	1,599,489	—	—	1,599,489
Total additions (reductions)		2,820,038	28,588,453	38,585,788	69,994,279	7,011,921	27,030,668	(5,897,081)	28,145,508
Deductions:									
Benefits		4,916,384	26,740,565	7,029,970	38,686,919	4,118,341	27,839,254	6,515,970	38,473,565
Administrative		170,502	908,997	234,944	1,314,443	242,350	1,287,882	194,905	1,725,137
Total deductions		5,086,886	27,649,562	7,264,914	40,001,362	4,360,691	29,127,136	6,710,875	40,198,702
Net change in fiduciary net assets		(2,266,848)	938,891	31,320,874	29,992,917	2,651,230	(2,096,468)	(12,607,956)	(12,053,194)
Net assets held in trust for postemployment healthcare benefits:									
Net assets, beginning of year		13,252,615	11,812,913	140,506,575	165,572,103	10,601,385	13,909,381	153,114,531	177,625,297
Net assets, end of year	$	10,985,767	12,751,804	171,827,449	195,565,020	13,252,615	11,812,913	140,506,575	165,572,103

See accompanying notes to the financial statements.

(1) Description

The following brief description of the State of Alaska Retiree Health Fund (Plan), a pension trust fund of the State of Alaska (State), is provided for general information purposes only. Participants should refer to the Retiree Group Insurance Information Booklet for more complete information.

General

The Plan was established to provide self–insured healthcare benefits to retirees of the Public Employees' Retirement System, Teachers' Retirement System, Judicial Retirement System and Elected Public Officers Retirement System (collectively referred to as the Retirement Systems) beginning July 1, 1997. The Plan is a pension trust fund of the State financial reporting entity and is included as such in the State's comprehensive annual financial report. As of June 30, 2010 and 2009, there were approximately 34,000 and 32,800 retirees, respectively, excluding dependents, covered by the Plan.

Prior to July 1, 1997, healthcare benefits for retirees were fully insured through the payment of premiums to an insurance company.

Benefits

The Plan offers major medical, voluntary dental–visual–audio (DVA) and voluntary long–term care (LTC) benefits to eligible benefit recipients of the Retirement Systems and their dependents.

Medical

The Plan provides medical benefits to qualified benefit recipients of the Retirement Systems. The State pays the medical premiums for benefit recipients of the Elected Public Officers Retirement System, for benefit recipients of the Marine Engineers Beneficial Association who retired from the State after July 1, 1986 and for benefit recipients of the NorthWest Marine Trust who retired from the State before July 1, 1984. The following benefit recipients must elect coverage and pay a premium:

Benefit recipients of the Public Employees' Retirement System (PERS) first hired under the PERS on or after July 1, 1986, who are under age 60, are not receiving a disability benefit, and had less than 25 years of peace officer/firefighter service or less than 30 years of other service.

Benefit recipients of the Teachers' Retirement System (TRS) first hired under the TRS on or after July 1, 1990, who are under age 60, are not receiving a disability benefit, and had less than 25 years of service.

Benefit recipients of the PERS first hired under the PERS on or after July 1, 1996, who are age 60 or older and do not have at least 10 years of credited service.

Alternate payees under a Qualified Domestic Relations Order (QDRO).

Beginning July 1, 2007, the Alaska Retiree Healthcare Trust (ARHCT), a healthcare trust fund of the State, was established. The ARHCT is self funded and provides major medical coverage to retirees of the Plan. The Plan retains the risk of loss of allowable claims for eligible members. The ARHCT began paying member healthcare claims on March 1, 2008. Prior to that, healthcare claims were paid for by the Plan.

(1) Description (cont.)

Voluntary DVA and LTC

Individuals receiving benefits from one of the Retirement Systems, excluding alternate payees under a QDRO, may elect coverage for themselves and their eligible dependents. If coverage is elected, the premiums are paid by deductions from retirement checks.

(2) Summary of Significant Accounting Policies

Basis of Accounting

The Plan's financial statements are prepared using the economic resource focus and the accrual basis of accounting. Premiums are recognized in the period in which they are due. Benefits are recognized when due and payable.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of additions and deductions during the reporting period. Actual results could differ from those estimates.

Investments

The Department of Revenue, Division of Treasury (Treasury) has created a pooled environment by which it manages investments the Commissioner has fiduciary responsibility for. Actual investing is performed by investment officers in Treasury or by contracted external investment managers. Specifically, the Domestic Equity and the International Equity Pools are managed externally. Treasury manages the Short-term Fixed Income Pool, Intermediate-term Fixed Income Pool, Broad Market Fixed Income Pool, Conservative Broad Market Fixed Income Pool, and the U.S. Treasury Fixed Income Pool in addition to acting as oversight manager for all externally managed investments. The Dental Vision and Audio Plan (DVA) invests in the State's internally managed General Fund and Other Nonsegregated Investments (GeFONSI). GeFONSI consists of investments in the State's internally managed Short-term and Intermediate-term Fixed Income Pools.

Valuation and Income Allocation

The accrual basis of accounting is used for investment income. GeFONSI investment income is distributed to pool participants if prescribed by statute or if appropriated by state legislature. Assets are reported at fair value. Investment purchases and sales are recorded on a trade-date basis. Net contributions (withdrawals) are recorded on a cash basis. Net contributions (withdrawals) represent contributions from employers and employees net of benefits paid to participants as well as administrative and investment management expenses.

Fixed income securities are valued each business day using prices obtained from a pricing service when such prices are available; otherwise, such securities are valued at the most current sale price or based on a

(2) Summary of Significant Accounting Policies (cont.)

valuation provided by investment managers. Domestic and international equity securities are valued each business day using prices obtained from a pricing service or prices quoted by one or more independent brokers. Securities expressed in terms of foreign currencies are translated into U.S. dollars at the prevailing exchange rates. Forward currency contracts are valued at the mid-point of representative quoted bid and ask prices.

Income in the Short-term, Intermediate-Term, and Broad Market Fixed Income Pools as well as the International Equity Pool is allocated to pool participants daily on a pro rata basis. Domestic Equity income is credited and allocated in accordance with the participants pro rata share of the fund when received.

Federal Income Tax Status

The Plan is a qualified plan under Section 401(a) of the Internal Revenue Code and exempt from federal income taxes under Section 501(a).

Administration

The Plan is administered by the State's Division of Retirement and Benefits (DRB). DRB utilizes the services of a claims administrator, Wells Fargo, to process all medical, dental, and prescription drug claims. Claims were processed by Premera during fiscal year 2009.

Funding

The Plan is self–insured for all benefits. The Plan's funding policy provides for the collection of premiums from the Retirement Systems and benefit recipients, as applicable. Premium amounts are actuarially determined on an annual basis and adjusted as necessary. The Retirement Systems retain the risk of loss of allowable claims.

Due to State of Alaska General Fund

Due to the State of Alaska General Fund represent reimbursements to be made by the Plan to other funds for net payments made by other funds on behalf of the Plan.

(Continued)

(3) Deposit and Investment Risk

At June 30, 2010, the Plan had the following investments:

	Fair value					
	Fixed income pools					
Investment type	**Short-term**	**Intermediate-term**	**Broad market**	**U.S. Treasury**	**Other**	**Total**
Deposits	$ (69,323)	—	—	—	31,408	(37,915)
Short-term investment fund	—	—	—	—	1,027,755	1,027,755
Commercial paper	1,839,396	—	—	—	—	1,839,396
Municipal bonds	—	—	16,831	—	—	16,831
U.S. Treasury notes	—	2,406,264	10,959,002	3,767,238	—	17,132,504
U.S. Treasury bills	4,476,279	—	—	—	—	4,476,279
U.S. Treasury bonds	—	—	2,621,604	495,466	—	3,117,070
U.S. Treasury when-issued	688,665	3,124,824	—	—	—	3,813,489
U.S. government agency	2,445,124	816,823	1,837,050	278,622	—	5,377,619
U.S. gov. agency discount note	—	176,897	—	—	—	176,897
Mortgage-backed	290,234	459,084	18,151,584	—	—	18,900,902
Other asset-backed	8,085,817	12,487	1,037,224	—	—	9,135,528
Corporate bonds	17,230,221	1,102,803	10,017,566	477,435	—	28,828,025
Yankees:						
Government	—	69,509	517,056	28,116	—	614,681
Corporate	482,476	283,977	1,746,056	—	—	2,512,509
Domestic equity	—	—	—	—	90,603,544	90,603,544
International equity	—	—	—	—	40,692,040	40,692,040
Total invested assets	35,468,889	8,452,668	46,903,973	5,046,877	132,354,747	228,227,154
Pool related net assets (liabilities)	16,318	(194,744)	(4,153,714)	(392,190)	185,637	(4,538,693)
Other pool ownership	(7,635,876)	—	6,135,737	413,579	—	(1,086,560)
Unallocated cash	—	—	(2)	—	—	(2)
Net invested assets	$ 27,849,331	8,257,924	48,885,994	5,068,266	132,540,384	222,601,899

(3) Deposit and Investment Risk (cont.)

At June 30, 2009, the Plan had the following investments:

	Fair value						
	Fixed income pools						
Investment type	**Short-term**	**Intermediate-term**	**Broad market**	**U.S. Treasury**	**Conservative broad market**	**Other**	**Total**
Deposits	$ 92,277	—	—	—	—	(1)	92,276
Short-term investment fund	—	—	—	—	—	612,520	612,520
Commercial paper	1,850,471	—	—	—	—	—	1,850,471
U.S. Treasury notes	—	4,504,749	6,021,566	3,093,678	—	—	13,619,993
U.S. Treasury bills	10,440,296	—	—	—	—	—	10,440,296
U.S. Treasury bonds	—	—	688,894	495,512	—	—	1,184,406
U.S. government agency	809,630	2,935,576	1,315,970	287,949	—	—	5,349,125
Mortgage-backed	1,164,598	930,528	18,370,251	—	—	—	20,465,377
Other asset-backed	3,686,926	61,186	459,251	—	—	—	4,207,363
Corporate bonds	9,967,224	1,083,787	7,346,991	339,046	—	—	18,737,048
Yankees:							
Government	—	77,376	102,891	—	—	—	180,267
Corporate	2,145,606	426,935	1,481,527	—	—	—	4,054,068
Domestic equity	—	—	—	—	—	78,278,089	78,278,089
International equity	—	—	—	—	—	33,717,481	33,717,481
Total invested assets	30,157,028	10,020,137	35,787,341	4,216,185	—	112,608,089	192,788,780
Pool related net assets (liabilities)	25,179	27,262	(676,465)	20,034	—	129,284	(474,706)
Other pool ownership	(2,333,985)	—	(35,110,876)	(4,236,219)	41,681,080	—	—
GeFONSI	—	—	—	—	—	—	—
Unallocated cash	—	—	—	—	—	—	—
Net invested assets	$ 27,848,222	10,047,399	—	—	41,681,080	112,737,373	192,314,074

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment.

Short–term Fixed Income Pool

As a means of limiting its exposure to fair value losses arising from increasing interest rates, Treasury's investment policy limits individual fixed rate securities to fourteen months to maturity or fourteen months expected average life upon purchase. Floating rate securities are limited to three years to maturity or three years expected average life upon purchase. Treasury utilizes the actual maturity date for commercial paper and twelve-month prepay speeds for other securities. At June 30, 2010, the expected average life of individual fixed rate securities ranged from one day to twenty-nine years and the expected average life of floating rate securities ranged from one day to nine and three-quarters years.

(3) Deposit and Investment Risk (cont.)

Intermediate, Broad Market, and U.S. Treasury Fixed Income Pools

Duration is a measure of interest rate risk. It measures a security's sensitivity to a 100-basis point change in interest rates. The duration of a pool is the average fair value weighted duration of each security in the pool taking into account all related cash flows.

Treasury uses industry-standard analytical software developed by The Yield Book Inc. to calculate effective duration. The software takes into account various possible future interest rates, historical and estimated prepayment rates, call options and other variable cash flows for purposes of the effective duration calculation.

Through its investment policy, Treasury manages its exposure to fair value losses arising from increasing interest rates by limiting effective duration of the Intermediate-term Fixed Income Pool, the Broad Market Fixed Income Pool, and the U.S. Treasury Fixed Income Pool to the following:

Intermediate-term Fixed Income Pool – ± 20% of the Merrill Lynch 1-5 year Government Bond Index. The effective duration for the Merrill Lynch 1-5 year Government Bond Index at June 30, 2010, was 2.49 years.

Broad Market Fixed Income Pool – ± 20% of the Barclays Capital U.S. Aggregate Bond Index. The effective duration for the Barclays Capital U.S. Aggregate Bond Index at June 30, 2010, was 4.30 years.

U.S. Treasury Fixed Income Pool – ± 20% of the Barclays Capital U.S. Aggregate Treasury Index. The effective duration for the Barclays Capital U.S. Aggregate Treasury Index at June 30, 2010, was 5.27 years.

(3) Deposit and Investment Risk (cont.)

At June 30, 2010, the effective duration of the Plan's fixed income pools by investment type was as follows:

	Effective duration (in years)		
	Intermediate-term fixed income pool	**Broad market fixed income pool**	**U.S. Treasury fixed income pool**
Corporate bonds	2.24	6.18	2.01
Municipal bonds	—	12.56	—
Mortgage-backed	1.71	2.70	—
Other asset-backed	0.65	3.10	—
U.S. Treasury bonds	—	9.94	8.34
U.S. Treasury notes	2.91	4.37	3.60
U.S. Treasury when-issued	2.73	—	—
U.S. government and agency securities	1.69	4.74	4.70
U.S. government agency discount note	0.67	—	—
Yankees:			
Corporate	2.65	5.32	—
Government	1.87	4.95	4.29
Portfolio effective duration	**2.47**	**4.29**	**3.97**

Credit Risk

Credit risk is the risk that an issuer or other counter party to an investment will not fulfill its obligations.

Treasury's investment policy has the following limitations with regard to credit risk:

Short-term Fixed Income Pool investments are limited to instruments with a long-term credit rating of at least A3 or equivalent and instruments with a short-term credit rating of at least P-1 or equivalent. Asset-backed and nonagency mortgage securities must be rated A3 or equivalent. The A3 rating is defined as the median rating of the following three rating agencies: Standard & Poor's Corporation, Moody's and Fitch. Asset-backed and nonagency mortgage securities may be purchased if only rated by one of these agencies if they are rated AAA.

Intermediate-term and Broad Market Fixed Income Pool investments are limited to securities with a long-term credit rating of at least Baa3 or equivalent and securities with a short-term credit rating of at least P-1 or equivalent. Asset-backed and nonagency mortgage securities must be rated investment grade. The investment grade rating is defined as the median rating of the following three rating agencies: Standard & Poor's Corporation, Moody's and Fitch. Asset-backed and nonagency mortgage securities may be purchased if only rated by one of these agencies if they are rated AAA.

In the U.S. Treasury Fixed Income Pool commercial paper must be rated at least P-1 by Moody's and A-1 by Standard and Poor's Corporation. In addition, corporate, asset-backed and nonagency mortgage

(3) Deposit and Investment Risk (cont.)

securities must be rated investment grade. The investment grade rating is defined as the median rating of the following three rating agencies: Standard & Poor's Corporation, Moody's and Fitch. In addition, asset-backed and nonagency mortgage securities may be purchased if only rated by one of these agencies if they are rated AAA. Corporate bonds may be purchased if rated by two of these agencies.

(3) Deposit and Investment Risk (cont.)

At June 30, 2010, the State's internally managed pools consisted of investments with credit quality ratings issued by nationally recognized statistical rating organizations as follows (using Standard and Poor's Corporation rating scale):

Investment type	Rating	Short-term fixed income pool	Intermediate-term fixed income pool	Broad market fixed income pool	U.S. Treasury pool
Commercial paper	A-1	1.17%	—%	—%	—%
Commercial paper	Not Rated	4.03	—	—	—
Corporate bonds	AAA	41.70	6.53	1.89	9.42
Corporate bonds	AA	1.88	1.78	3.11	—
Corporate bonds	A	3.74	2.90	8.87	—
Corporate bonds	BBB	—	1.12	6.47	—
Corporate bonds	Not Rated	1.35	0.51	0.15	—
Mortgage-backed	AAA	0.79	4.51	26.52	—
Mortgage-backed	AA	—	0.05	1.02	—
Mortgage-backed	A	—	—	0.04	—
Mortgage-backed	BBB	—	0.20	0.16	—
Mortgage-backed	Not Rated	0.03	0.58	9.41	—
Municipal bonds	AA	—	—	0.03	—
Other asset-backed	AAA	21.16	0.05	1.74	—
Other asset-backed	AA	—	0.03	0.05	—
Other asset-backed	A	—	0.06	0.08	—
Other asset-backed	BBB	—	—	0.05	—
Other asset-backed	Not Rated	1.68	—	0.19	—
U.S. government agency	AAA	1.07	9.47	3.61	5.50
U.S. government agency	Not Rated	5.84	0.04	0.14	—
U.S. government agency Discount notes	Not Rated	—	2.06	—	—
U.S. Treasury bills	AAA	12.65	—	—	—
U.S. Treasury bonds	AAA	—	—	5.36	9.78
U.S. Treasury notes	AAA	—	28.02	22.43	74.33
U.S. Treasury when-issued	AAA	1.95	36.40	—	—
Yankees:					
Government	AAA	—	0.07	0.47	—
Government	AA	—	0.74	0.34	0.55
Government	BBB	—	—	0.24	—
Corporate	AAA	0.58	1.81	0.65	—
Corporate	AA	0.20	0.91	0.51	—
Corporate	A	—	0.46	1.31	—
Corporate	BBB	—	0.08	1.11	—
Corporate	Not Rated	0.58	0.05	—	—
No credit exposure		(0.40)	1.57	4.05	0.42
		100.00%	100.00%	100.00%	100.00%

(3) Deposit and Investment Risk (cont.)

Custodial Credit Risk – Deposits

Custodial credit risk is the risk that deposits may not be returned in the event of a bank failure. Treasury's policy with regard to custodial credit risk is to collateralize state deposits to the extent possible. The bond indentures governing the investment of tobacco revenue related bond proceeds, do not establish policy with regard to custodial credit risk. At June 30, 2010, the State had the following uncollateralized and uninsured deposits:

		Amount
International Equity Pool	$	30,048

Foreign Currency Risk

The Commissioner of Revenue formally adopts asset allocation policies for the Plan at the beginning of each fiscal year which places policy limitations on the amount of international securities the Plan is allowed to hold. The following policy was in place during fiscal year 2010 and invested assets included the following holdings at June 30, 2010, for the Plan's investment in the International Equity Pool:

	Policy	Actual
Retiree Health Insurance Fund, Long-term Care	23% ±4%	22.17%

(3) Deposit and Investment Risk (cont.)

At June 30, 2010, the Plan had exposure to foreign currency risk as follows:

Currency		Fair value amount
Deposits:		
Euro currency	$	381
Japanese Yen		29,667
		30,048
Investments – international equity:		
Australian Dollar		247,815
Canadian Dollar		676,877
Danish Krone		308,058
Euro Currency		5,931,156
Hong Kong Dollar		801,031
Japanese Yen		6,145,305
Norwegian Krone		213,248
Pound Sterling		7,647,683
Singapore Dollar		286,901
Swiss Franc		2,584,695
		24,842,769
Total	$	24,872,817

Concentration of Credit Risk

The Board's policy with regard to concentration of credit risk is to prohibit the purchase of more than five percent of a pool's holdings in corporate bonds of any one company or affiliated group.

At June 30, 2010, the Plan had more than five percent of their investments in Federal National Mortgage Association as follows:

		Fair value	Percent of total plan investments
Federal National Mortgage Association	$	15,310,576	6.88%

Federal National Mortgage Association securities are not classified as corporate bonds, are backed by the full faith and credit of the U.S. Government and therefore may be held in higher concentration.

(4) Foreign Exchange, Foreign Exchange Contracts, Off-Balance Sheet Risk, and Derivative Exposure

The Commissioner is exposed to credit risk on investment derivative instruments that are in asset positions. The Commissioner has no policy of requiring collateral or other security to support derivative instruments subject to credit risk. Additionally, the Commissioner has no policy regarding entering into netting arrangements when it enters into derivative instrument transactions with a counterparty, nor does the Commissioner have a policy for contingencies. The International Equity Pool investment includes the following income from forward contracts at June 30, 2010:

Net realized gain on foreign currency	$	400,058
Net realized gain on foreign exchange contracts		6,151

The International Equity Pool includes foreign currency forward contracts to buy and sell specified amounts of foreign currencies at specified rates on specified future dates for the purpose of hedging existing security positions. The counterparties to the foreign currency forward contracts consist of a diversified group of financial institutions. Credit risk exposure exists to the extent of nonperformance by these counterparties; however, the risk of default is considered to be remote. The market risk is limited to the difference between contractual rates and forward rates at the balance sheet date. At June 30, 2010 the International Equity Pool had no outstanding contracts.

(5) Claims Payable

The liability for claims incurred but not reported represents the estimated amounts necessary to settle all outstanding claims, incurred but not reported, as of the balance sheet date. The Plan’s reserve estimates are based primarily on historical development patterns adjusted for current trends that would modify past experience. Claims are reevaluated periodically to consider the effects of inflation, claims settlement trends and other economic factors. The process of establishing loss reserves is subject to uncertainties that are normal, recurring and inherent in the healthcare business.

(Continued)

(5) Claims Payable (cont.)

Changes in the balances of claims liabilities follows:

		2010	2009
Beginning of year:			
Due to State of Alaska General Fund for outstanding warrants	$	2,810,257	296,775
Outstanding claims received but not paid		532,286	416,302
Incurred but not reported		19,168,000	15,152,000
Total, beginning of year		22,510,543	15,865,077
Benefit deductions		38,686,919	38,473,565
Benefits paid		(38,441,689)	(31,828,099)
Total, end of year	$	22,755,773	22,510,543
End of year:			
Due to State of Alaska General Fund for outstanding warrants	$	2,321,773	2,810,257
Outstanding claims received but not paid		—	532,286
Incurred but not reported		20,434,000	19,168,000
Total, end of year	$	22,755,773	22,510,543

(6) Medicare Part D Retiree Drug Subsidy

One of the provisions of Medicare Part D provides sponsors of pension healthcare plans the opportunity to receive a retiree drug subsidy (RDS) payment if the sponsor’s plan provides a prescription drug benefit that is actuarially equivalent to the Medicare Part D benefit. The RDS is equal to twenty–eight percent of the amount of eligible prescription drug benefit costs of retirees who are eligible for, but not enrolled in, Medicare Part D, by virtue of continuing to be covered by the sponsor’s plan. The Plan was approved for participation in the Medicare Part D program beginning calendar year 2006. The RDS for the six-month period ended June 30, 2010, cannot be reasonably estimated, and therefore is not recorded in the financial statements for the period ended June 30, 2010.