ALLSCRIPTS HEALTHCARE SOLUTIONS, INC.
Form 10-K
February 29, 2012
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended December 31, 2011

or

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
Commission File Number 000-32085

ALLSCRIPTS HEALTHCARE SOLUTIONS, INC.

(Exact name of registrant as specified in its charter)

Delaware	36-4392754
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

222 Merchandise Mart Plaza, Suite 2024, Chicago, IL 60654

(Address of principal executive offices and zip code)

(866) 358-6869

(Registrant s telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class:	Name of Each Exchange on which Registered
Common Stock, par value $0.01 per share	**The NASDAQ Global Select Market**

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No ¨

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or section 15(d) of the Exchange Act. Yes ¨ No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding twelve months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of accelerated filer , large accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer x	Accelerated filer ¨	Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

The aggregate market value of the voting and non-voting common stock held by non-affiliates of the registrant based upon the closing sale price of the common stock on June 30, 2011, the last business day of the registrant s most recently completed second quarter, as reported by NASDAQ Global Select Market, was approximately $3,610,303,939.

The number of outstanding shares of the registrant s common stock as of February 10, 2012 was 190,514,662.

Documents Incorporated by Reference: Portions of the Proxy Statement for the 2012 annual stockholders meeting are incorporated by reference into Part III.

Table of Contents

ALLSCRIPTS HEALTHCARE SOLUTIONS, INC.

TABLE OF CONTENTS TO

2011 ANNUAL REPORT ON FORM 10-K

Item		Page
	PART I	
1.	Business	5
1A.	Risk Factors	21
1B.	Unresolved Staff Comments	41
2.	Properties	41
3.	Legal Proceedings	41
4.	Mine Safety Disclosures	41
	PART II	
5.	Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	42
6.	Selected Financial Data	45
7.	Management s Discussion and Analysis of Financial Condition and Results of Operations	47
7A.	Quantitative and Qualitative Disclosures About Market Risk	78
8.	Financial Statements and Supplementary Data	79
9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	130
9A.	Controls and Procedures	130
9B.	Other Information	130
	PART III	
10.	Directors, Executive Officers and Corporate Governance	131
11.	Executive Compensation	131
12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	131
13.	Certain Relationships and Related Transactions and Director Independence	131
14.	Principal Accountant Fees and Services	131
	PART IV	
15.	Exhibits and Financial Statement Schedules	132
	Signatures	140

Allscripts Healthcare Solutions, Inc. was incorporated in the state of Delaware. In this report, we, us, our and Allscripts refer to Allscripts Healthcare Solutions, Inc. and its wholly owned subsidiaries, unless the context indicates otherwise.

Table of Contents

Safe Harbor for Forward-Looking Statements

This report contains forward-looking statements within the meaning of the federal securities laws that involve risks and uncertainties. We develop forward-looking statements by combining currently available information with our beliefs and assumptions. These statements relate to future events, including our future performance, and management s expectations, beliefs, intentions, plans or projections relating to the future and some of these statements can be identified by the use of forward-looking terminology such as believes, expects, anticipates, estimates, project intends, seeks, future, continue, contemplate, would, will, may, should, and the negative or other variations of those terms or cor terminology or by discussion of strategy, plans, opportunities or intentions. As a result, actual results, performance or achievements may vary materially from those anticipated by the forward-looking statements.

Among the factors that could cause actual results, performance or achievements to differ materially from those indicated by such forward-looking statements are:

- the risk that we will not achieve the strategic benefits of the August 24, 2010 merger with Eclipsys Corporation (the Eclipsys Merger);
- the possibility that the expected synergies and cost savings of the Eclipsys Merger will not be realized, or will not be realized within the expected time period;
- unexpected requirements to achieve interoperability certification pursuant to the Health Information Technology for Economic and Clinical Health Act, with resulting increases in development and other costs for us;
- the volume and timing of systems sales and installations, the length of sales cycles and the installation process and the possibility that our products will not achieve or sustain market acceptance;
- the timing, cost and success or failure of new product and service introductions, development and product upgrade releases;
- competitive pressures including product offerings, pricing and promotional activities;
- errors or similar problems in our software products;
- the outcome of any legal proceeding that has been or may be instituted against us and others;
- compliance obligations under existing laws, regulations and industry initiatives and future changes in laws or regulations in the healthcare industry, including possible regulation of our software by the U.S. Food and Drug Administration;
- the possibility of product-related liabilities;
- our ability to attract and retain qualified personnel;

the implementation and speed of acceptance of the electronic record provisions of the American Recovery and Reinvestment Act of 2009, as well as elements of the Patient Protection and Affordable Care Act (aka health reform) which pertains to healthcare IT adoption;

maintaining our intellectual property rights and litigation involving intellectual property rights;

legislative, regulatory and economic developments;

risks related to third-party suppliers and our ability to obtain, use or successfully integrate third-party licensed technology;

breach of our security by third parties; and

those factors discussed in Risk Factors in our periodic filings with the Securities and Exchange Commission (the SEC).

Table of Contents

We make these statements under the protection afforded by Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Because forward-looking statements are subject to assumptions and uncertainties, actual results, performance or achievements may differ materially from those expressed or implied by such forward-looking statements. Stockholders are cautioned not to place undue reliance on such statements, which speak only as of the date such statements are made. Except to the extent required by applicable law or regulation, Allscripts undertakes no obligation to revise or update any forward-looking statement, or to make any other forward-looking statements, whether as a result of new information, future events or otherwise.

Table of Contents

PART I

Item 1. Business

Overview

Allscripts is a leading provider of clinical, financial, connectivity and information solutions and related professional services that empower hospitals, physicians and post-acute organizations to deliver world-class outcomes. We deliver innovative solutions that provide physicians and other healthcare professionals with the information, insights and connectivity required to transform healthcare by improving the quality and efficiency of patient care.

We provide a variety of integrated clinical software applications for hospitals, physician practices and post-acute organizations. For hospitals and health systems these applications include our Sunrise Enterprise suite of clinical solutions, comprising a full acute care Electronic Health Record (EHR), integrated with financial/administrative solutions including performance management and revenue cycle/access management. Our acute care solutions include modules of the Sunrise suite that are available on a stand-alone basis, as well as additional stand-alone solutions including Emergency Department Information System (EDIS), care management and discharge management. Allscripts IT Outsourcing enables hospitals and physician groups to concentrate on their core mission while using IT to improve clinical, financial and operational outcomes. Allscripts Remote Hosting helps healthcare organizations manage their complex healthcare IT solutions infrastructure while freeing up the physical space, resources and costs associated with maintaining computer servers and deploying client-based applications on-site.

For physician practices of every size and kind, our solutions include: integrated EHR and practice management functionality available either via traditional on-premise delivery or via Software-as-a-Service (SaaS) (such solutions are also available independent of one another); revenue cycle management software and our new Revenue Cycle Management Services solution, which enables practices to outsource their full revenue cycle to us or address requirements in-house; clearinghouse services; stand-alone electronic prescribing; and document imaging solutions for physician practices. We also provide a variety of solutions for home care, hospice, skilled nursing, and other post-acute organizations; these range from a fully integrated EHR and financial management solution to Referral Management.

Clients in every care setting can leverage Allscripts mobile solutions to deliver remote access to EHR and other capabilities on a wide variety of mobile devices including iPad, iPhone, BlackBerry, Android and Windows Mobile smartphones. Additional add-on applications include our Patient Portal, Patient Kiosk, Prenatal, and Analytics solutions. Our community-based solutions for hospitals and health systems, provided in partnership with dbMotion, deliver meaningful health information exchange and enable information connectivity across entire communities of providers, regardless of which technology vendor they use, helping our clients to compete in an evolving marketplace.

We primarily derive our revenue from sales of our proprietary software and related hardware, professional services and IT outsourcing services. These sales also are the basis for our recurring service contracts for software maintenance and transaction processing services. We report our financial results utilizing three business segments: clinical solutions, hospital solutions and health solutions. Our clinical solutions segment presents the operations of our ambulatory solutions for physician practices; hospital solutions reflects the operations, subsequent to the completion of our merger with Eclipsys Corporation on August 24, 2010, of our acute care hospital solutions acquired in the merger; and health solutions reflects the operations of our acute and post-acute solutions for health systems.

Table of Contents

Recent Developments

Completing the Eclipsys Merger

In 2011, we made progress delivering on strategic goals related to the August 24, 2010 merger with Eclipsys Corporation (the Eclipsys Merger), an enterprise provider of solutions and services to hospitals and clinicians (Eclipsys). At the time of the merger, we committed to increase new sales of Sunrise Enterprise in 2011; to execute on cross-sell opportunities within our combined client base; and to make progress integrating our ambulatory and acute product portfolio.

The combination of Allscripts and Eclipsys has produced a larger, more competitive and complete solutions provider within the healthcare information technology industry. Today we bring to market one of the most comprehensive solution offerings for healthcare organizations of every size and setting. We provide a single platform of clinical, financial, connectivity and information solutions for every segment of the acute, ambulatory and post-acute market.

Given our unique breadth of solutions and customer types, we are ideally positioned to connect physicians, other care providers and patients across all health care provider settings including hospitals, small or large physician practices, post-acute facilities, or a home care setting. We provide one of the broadest suites of applications available in healthcare, enabling our clients to connect caregivers, provide information where and when needed, and generate insights that lead to better clinical and financial outcomes. We are well-positioned to compete for opportunities among large hospitals and health systems that increasingly are looking to one information technology vendor to provide a single, end-to-end solution across all points of care.

At the same time, our unique service-oriented architecture enables hospitals and health systems to pursue a best-of-breed strategy that protects their current IT investments and applications without the added expense of the rip and replace strategy promoted by many acute care competitors. Moreover, our ability to field interoperable, vendor agnostic solutions built on an open IT architecture provides us a competitive edge by enabling hospitals to easily connect their IT systems with those of affiliated physicians who use systems from another vendor. Hospitals view their affiliated base of referring physicians as important clinical partners, so information connectivity with these physicians not only streamlines the referral process but also strengthens bonds with a key business constituency.

Reduction of Misys Share Ownership

On June 9, 2010, Allscripts entered into a Framework Agreement with Misys plc (Misys), which was subsequently amended on July 26, 2010 (as amended, the Framework Agreement). Pursuant to the Framework Agreement, Allscripts and Misys agreed to reduce Misys existing indirect ownership interest in Allscripts through a series of transactions, which we refer to as the Coniston Transactions. As of June 8, 2010, Misys held indirectly 80 million shares of Allscripts common stock, representing approximately 55% of the aggregate voting power of Allscripts capital stock.

Table of Contents

The Coniston Transactions were completed on August 27, 2010; accordingly, Misys equity stake in Allscripts was reduced to approximately 10% of the outstanding shares of Allscripts common stock. The repurchased stock was retired and the associated excess of the repurchase price over par totaling $679 million was allocated to additional paid-in capital.

On November 17, 2010, Kapiti Limited and ACT Sigmex Limited, each a wholly-owned subsidiary of Misys, sold shares of common stock of Allscripts resulting in Misys holding approximately 4% of the outstanding shares of our common stock.

On February 24, 2011, Misys announced that it had disposed of its remaining investment in Allscripts common stock.

Our Competitive Strengths

We believe that the following competitive strengths are the keys to our success:

Industry-Leading Solutions

We have been an innovator in the development and adoption of healthcare information technology solutions. We believe our clinical and healthcare solutions provide the following advantages:

Client Reach. Healthcare providers can instantly access our web-based clinical solutions from the hospital, the clinic or remote locations. Providers appreciate the convenience of remote connectivity that lets them easily perform critical tasks such as documenting patient visits, reviewing lab results and writing prescriptions after hours and while on call. In addition to the standard desktop computers, our solutions run on a wide variety of mobile devices including tablet PCs, every major smartphone, desktop workstations and other wireless devices.

Innovation. Allscripts has developed a reputation for innovation through the introduction of pioneering new products. Recent examples include:

Sunrise Mobile MD, a mobile solution that offers physicians greater control of the patient encounter on an Apple iPhone® or iPod touch®. Sunrise Mobile MD is built on Helios by Allscripts, the company s industry-defining open platform to enable proprietary, native integration with the Sunrise Enterprise 5.5 suite. Physicians using the Allscripts iPhone application gain direct access to and from the Sunrise Enterprise electronic health record (EHR) enabling them to remotely monitor their hospitalized patients.

Allscripts Remote, the ambulatory corollary to Sunrise Mobile MD, lets physicians access their Allscripts ambulatory EHR using an iPhone , iPod touch®, BlackBerry®, Windows Mobile® or Android® smartphone. Capabilities include quick access to real-time patient summary information; fast communication to local hospital emergency rooms; convenient ePrescribing to the patient s regular pharmacy; and real-time access to all the information a physician needs to make decisions, including medical history, lab results and medications.

Allscripts Patient Kiosk is the first kiosk from a major practice management and EHR vendor. The kiosk connects to our EHR and practice management solutions to enable patients to quickly check-in, pay their co-pays using a credit card and conduct other business while taking control of their own healthcare with a dashboard view of all their personal information, including a complete health maintenance plan and alerts about upcoming or overdue tests.

Allscripts Prenatal is both a stand-alone and EHR-integrated SaaS solution that addresses the unique workflow and cross-provider information sharing needs of prenatal care. Currently, obstetricians must fax patient information between their offices and hospital labor and delivery rooms. Too often, the process leaves them without the critical information they need to make clinical decisions. Allscripts Prenatal enables real-time sharing of patient information between all settings. To match the normal workflow of

obstetricians, the solution also provides an easy-to-navigate web-based version of the paper forms used today by most physicians providing obstetric care.

Table of Contents

The Allscripts Developer Program (ADP) enables clients and third parties to use Helios by Allscripts technology to natively integrate their applications with our clinical and business performance solutions. Clients can search the new Allscripts Application Store & Exchange (ASX) to select or share applications developed through the ADP. By enabling Allscripts clients to easily locate and exchange technologies that are natively integrated with Sunrise Enterprise, ASX protects their existing technology investments and helps avoid expensive rip and replace situations.

The Allscripts Referral Network (ARN) makes it easy for physicians to deliver seamless electronic patient referrals between physicians using a certified Allscripts EHR or the Allscripts ePrescribe module. A breakthrough in health information exchange, ARN enables physicians to easily send, receive and track round-trip patient referrals to physicians, as well as collaborate via secure messages throughout the referral process. Available at no additional charge to users of any American Recovery and Reinvestment Act of 2009 (ARRA) certified Allscripts EHR, as well as users of Allscripts ePrescribe, the service enhances care coordination, promotes quality of care, and reduces administrative time and hassle associated with referral management, one of the most time consuming physician tasks.

Allscripts Revenue Cycle Management Services (RCM Services) is an end-to-end, integrated financial and administrative management solution for physician practices. The SaaS business solution requires no new hardware or up-front costs, and is designed to meet the regulatory requirements of health reform. Allscripts RCM Services provides physician practices of every size and specialty with a complete outsourced revenue cycle solution that is paid for on an ongoing basis, as a percentage of their monthly collections. The turnkey, full-service billing and collections solution manages the entire revenue cycle continuum, from operational planning to final collections and denials management all working in synch to drive out costs and drive in cash flow.

SaaS solutions. By making a wide variety of our solutions available on-demand over the Internet using a web browser we believe we have significantly increased their ease of adoption. This capability is especially important for physicians in independent practice and small groups who lack the resources and know-how to manage an on-premise software application. Notably, SaaS delivers all of the benefits of a cloud-based approach to delivering software while also providing the rich features and functionality capability of traditional software, which can be limited in some cloud-based healthcare IT architectures. Furthermore, our approach is a prudent response to persistent concerns with data privacy in the cloud. We believe our SaaS approach to on-demand software offers significant future flexibility without sacrificing current performance.

Interoperability. Our products are designed to operate with existing installed systems, in both ambulatory and acute settings. Our Helios by Allscripts open architecture platform allows vendor freedom of choice to our clients and brings the management of healthcare technology into the modern age. Helios is intended to reduce the costs and resource demands hospitals experience in managing hundreds of vendor systems while effectively ending the battle between best-of-breed applications versus enterprise solutions. Helios opens the door to clients and third parties to natively build applications on a platform that eliminates the need for interfaces, thus providing a cost of ownership that can be dramatically lower than a single vendor with a closed proprietary architecture. Additionally, by making it easy for clients to deploy our Sunrise Enterprise and SCM solutions in combination with their existing IT assets, we are able to deliver Sunrise at a total-cost-of-ownership that is more manageable for mid-sized community hospitals than a total rip-and-replace approach, a model that we believe represents a significant market opportunity.

Enhancing the Revenue Cycle. We focus on making it easier for our clients to access new opportunities for financial gain through a variety of revenue cycle solutions. In particular, we believe that our Payerpath solution is one of the leading revenue cycle management and clearinghouse services in the United States with over 600 million revenue cycle management transactions processed each year. Available on a stand-alone basis or integrated with our practice management systems, Payerpath s

Table of Contents

comprehensive suite of internet solutions addresses every step in the reimbursement cycle for physician practices, clearinghouses and payers, delivering improved reimbursement and claim management processes that lead to cleaner claims and faster payments. For example, Payerpath Eligibility provides instant verification of patient insurance eligibility, ending phone calls to payers to clarify covered procedures and patient eligibility. Another example, Allscripts Patient Payment Assurance provides point-of-care collection of credit card and debit card payments, reducing the need for patient billing, which can dramatically reduce patient receivables. By enabling significant return on investment, our revenue cycle solutions allow providers to focus less on running their businesses and more on providing quality patient care. Our new Allscripts RCM Services takes this approach to the next level with a fully outsourced business office.

A Comprehensive Portfolio for Physicians. We offer physicians our complete EHR portfolio including stand-alone, web-based electronic prescribing, document management, and revenue cycle management solutions. For physicians who already utilize an EHR and practice management system, our portfolio includes connections to other physicians, to our Emergency Department and Care Management solutions and to post-acute providers and third-party hospital inpatient information systems. We also offer add-ons to the EHR that enable physicians to more easily enroll patients in clinical trials, automate the process of reporting quality outcomes to government and private pay for performance and quality-driven incentive programs, and connect to communities of healthcare organizations such as regional Health Information Exchanges. Importantly, we differentiate ourselves in the market by offering EHR solutions for every potential ambulatory setting including solo practices, small, medium and large physician groups and solutions to address the needs of nearly all medical specialties.

Accelerated Implementations. The Allscripts Speed to Value methodology for accelerated deployment program answers the growing need for faster, standardized implementations of Electronic Health Records. Federal incentives for the adoption and meaningful use of EHRs under the HITECH Act, a portion of the ARRA continues to drive a significant increase in the number of hospitals and physician practices seeking to deploy an EHR, increasing the pressure to implement the software more quickly and with fewer human resources. Speed to Value provides the answer with a series of complete solution packages that combine best-in-class recommendations for products, certified workflows and implementation, as well as remote e-learning in place of onsite training. Leveraging experience from thousands of successful clients, Speed to Value standardizes an EHR implementation and delivers a faster installation with minimized costs.

Accelerated Upgrades. Our Upgrade Enablement Center (UEC) provides a quick and accelerated migration path for users of our legacy Misys EMR. The customary four- to six-week process lets clients protect their investment in software and information while upgrading to our Professional EHR, providing a rapid opportunity to participate in HITECH incentives. We have extended our UEC platform to upgrade Allscripts clients on all of our legacy EHR systems, helping Allscripts clients to attest to the meaningful use of their EHR and so qualify for HITECH incentives.

Significant Installed Base

Approximately 180,000 physicians, 1,500 hospitals and 10,000 post-acute organizations nationwide utilize Allscripts solutions to automate and connect their clinical and business operations. Our significant installed base, including some of the country s most prestigious medical groups and hospitals, serves as a reference source for prospective clients who are interested in purchasing our solutions.

Significant Market Demand for Ambulatory EHR among Hospital Base

Towards the end of 2010, the proportion of US physician practices owned by hospitals or health systems surpassed 50 percent for the first time, a trend that continued to gain momentum in 2011. Industry observers expect this trend to continue for the foreseeable future as hospitals seek to strengthen their relationships with

Table of Contents

physicians, who constitute by far their largest source of income (via patient referrals), and seek competitive advantage in their communities. A primary strategic imperative of hospital CIOs is to bring their current and newly-employed physicians live on a common EHR platform, ensuring continuity of care and greater efficiencies through seamless information exchange. At the same time, hospitals increasingly are seeking to take advantage of the HITECH incentives for EHR adoption by providing an EHR to their affiliated physicians at a subsidized rate. Their selection of an ambulatory EHR for both employed and affiliated physicians hinges in large part on the level of integration between the EHR and their existing inpatient information system. The integration of Allscripts ambulatory EHRs and the Eclipsys acute care solutions is intended in part to meet this rapidly evolving market demand. We believe many of the company s existing Sunrise hospitals (approximately 700 at the time of the merger) are likely to turn to Allscripts when they are considering an EHR or EHR replacement for their employed and/or affiliated physicians.

A Solution for Accountable Care

Key healthcare stakeholders have proposed several solutions that fall under the general heading of Value-Driven Healthcare. The federal government s leadership in this arena includes not only the HITECH Act but pilots for Patient Centered Medical Homes, and Accountable Care Organizations (ACOs). Each of these initiatives hinges on the need to improve transitions in care the movement of patients from one care setting to another still the weakest link in the healthcare chain. An interoperable, connected Electronic Health Record is a required element to improve care transitions and ensure that providers in every setting have access to the latest information on their patients. The Allscripts Connected Community of Health takes the EHR to its logical conclusion. The connected community utilizes a combination of our open technology platform, our full spectrum connectivity to ambulatory, acute and post-acute solutions, and our robust community solutions to securely share information between providers in all care settings, no matter which health IT systems they use. Not only does this facilitate seamless care coordination between providers inside their own organization, but also with affiliated physicians and other independent stakeholders outside their organization. The goal is to create a single source of truth about a patient a unified community record to deliver effective and economical care.

Breadth of Product and Service Offering

Allscripts provides one of the most comprehensive solution offerings in the industry for healthcare organizations of every size and setting. We offer a single platform of clinical, financial, connectivity and information solutions, as well as standalone best-of-breed solutions in virtually every health information management category. Moreover, we are one of the few healthcare IT companies able to provide solutions that service every healthcare setting, from solo physician practices to the largest academic medical groups, hospitals of every size and configuration, and post-acute organizations including skilled nursing facilities, homecare and hospice.

Strength of our Distribution Network and Payor Relationships

We employ a highly differentiated sales and distribution strategy to reach potential clients in all segments of the physician market, ranging from solo and small-group practices to the largest academic medical groups. Our strategy employs three sales channels a large direct sales force, a national distribution network, and multiple hospitals that are marketing our solutions. Augmenting our direct sales force, the Allscripts Distribution Network (ADN) is composed of more than 100 leading resellers and distributors of healthcare products and services that provide our MyWay, Professional EHR and Practice Management solutions to small physician groups across the nation. The ADN significantly extends our market presence with a sales force of more than 1,500 that have existing physician relationships primarily in the one- to three-physician market, a market comprised of over 160,000 physicians.

Table of Contents

The strength of our distribution network has enabled Allscripts to take a unique, three-pronged approach to addressing the ambulatory market one practice at a time, one community at a time, and one region at a time. *One practice at a time* refers to our basic selling model executed by our direct sales force. *One community at a time* is an approach demonstrated by multiple sales in 2011 including Children s Hospital of Michigan, which is implementing our Enterprise EHR for their employed and affiliated physicians in Southeast Michigan and plans to use Allscripts to enable collaboration with other hospitals in the community. *One region at a time* is a strategy developed recently through our partnership with a large payer in North Carolina. Blue Cross and Blue Shield of North Carolina, in partnership with NC Health Information Exchange, announced in September 2011 they will provide an 85 percent subsidy for at least 750 physicians across the state to acquire Allscripts Electronic Health Records and related training and support. The program will also enable participating providers to electronically exchange patient information with other North Carolina healthcare organizations through the NC Health Information Exchange. This partnership is representative of more payers investing in healthcare IT to encourage their network providers to deliver higher quality care.

Allscripts Certified Sales Partners build stronger connected communities

By partnering with trusted, market-leading healthcare organizations, Allscripts is able to reach, serve and support thousands of smaller practices across the country in their adoption of Allscripts MyWay. The Allscripts Certified Sales Partners provide local experts and comprehensive value-added services to assist Allscripts in meeting and exceeding client expectations nationwide.

Unique and Comprehensive Connect Strategy

The Allscripts Community Solution helps local and regional health systems to share information between a range of technologies from any source, creating a single patient record for providers across the continuum of care. The Allscripts Community Solution enables all the members of a patient s care team to access the same up-to-date information about the patient, regardless of whether they work in acute, ambulatory or post-acute settings inside or outside the health system. The Allscripts Community Solution combines the Allscripts Community Exchange with the Allscripts Community Record. The Exchange efficiently connects and manages electronic transactions of all kinds between health systems and community/affiliated physician practices. The Community Record, provided in partnership with dbMotion, aggregates and harmonizes data from virtually any EHR or other clinical IT system, creating a single patient record across a health system or community.

Meaningful Use Certification

Our core go-to-market acute care and ambulatory EHRs have been certified as meeting the Stage 1 requirements for demonstrating meaningful use of an EHR, a requirement for healthcare organizations that apply for financial incentives under the HITECH portion of ARRA. The following products are certified as being 2011/2012 compliant with ARRA s Stage 1 criteria by either the Drummond Group or Certification Commission for Health Information Technology (CCHIT), both of which qualify as an Office of the National Coordinator for Health Information Technology Authorized Testing and Certification Body (ONC-ATCB), in accordance with the applicable eligible provider and hospital certification criteria adopted by the Secretary of Health and Human Services. Initial certifications were completed by the end of 2010 and subsequently have continued to be enhanced.

Allscripts MyWay EHR v9.0 (Complete EHR)

Allscripts MyWay EHR v9.1 (Complete EHR)

Allscripts MyWay EHR v10.0 (Complete EHR)

Allscripts Professional EHR, V9.2 (Complete EHR)

Table of Contents

Allscripts Professional EHR, V9.2,2 (Complete EHR)

Allscripts Professional EHR, V9.3 (Complete EHR)

Allscripts Enterprise EHR v11.2 (Complete EHR)

Allscripts Enterprise EHR v11.2 (EHR Modular)

Allscripts ePrescribe V 15.2 (EHR Modular)

Allscripts ED, Version 6.3 Release 4 (EHR Modular)

Allscripts ED, Version 7.0 (Complete EHR Inpatient)

Allscripts ED, Version 7.1 (Complete EHR Inpatient)

Sunrise Patient Portal Version 5.5 and Sunrise Acute Care EHR Version 5.5

Sunrise Patient Portal Version 5.5 and Sunrise Ambulatory Care EHR Version 5.5

Sunrise Acute Care 5.5

Sunrise Emergency Care 5.5

Sunrise Acute Care Module Set 5.5

Sunrise Ambulatory Care Module Set 5.5

Sunrise Emergency Care Module Set 5.5

Sunrise Acute Care Module Set 5.5 FP1

Sunrise Ambulatory Care Module Set 5.5 FP1

Sunrise Acute Care 5.5 FP1

Sunrise Emergency Care Module Set 5.5 FP1

Sunrise Emergency Care 5.5 FP1

We elected to certify some of our solutions as both complete and modular EHRs under the ARRA regulations to provide clients with the flexibility to adjust the EHR to their current IT environment. For instance, if an Enterprise EHR client wants to keep a previously-installed and certified patient portal application, under ARRA rules they need to implement our modularly certified version of that EHR, which is stripped of Enterprise s portal capabilities.

Sales and Marketing

We employ experienced sales executives with extensive industry expertise, and we primarily sell directly to our customers through our sales force. In addition to our direct sales force and our ADN for MyWay sales, we also have established reseller relationships with strategic partners, such as Cardinal Health, Inc., Dell, Inc., Henry Schein, Inc., Synnex and Etransmedia, with whom we also sell MyWay and Etransmedia hosting services in Costco stores nationwide. A number of our large hospital and health system clients also actively resell our solutions to other healthcare entities, primarily physician practices.

We continue efforts to expand sales of our solutions outside of North America, primarily in the Asia-Pacific region. We achieved initial success with sales of Sunrise Enterprise to SingHealth, the largest healthcare provider in Singapore; Parkway Holdings Limited, one of the largest private hospital groups in Asia; and Pantai Holdings Berhad, a 1,500-bed network of hospitals in Malaysia. As a result, approximately 70 percent of Singapore s hospitals currently use Allscripts solutions to automate care and business processes, and our performance with our Asian clients is proving to be a catalyst to help us drive additional business across the Asia-Pacific region. For example, in December, 2011 we announced an agreement with SA Health, the public health system of South

Table of Contents

Australia, to implement our Sunrise Enterprise acute care solution across SA Health s network of 80 hospitals and health clinics.

Allscripts Offerings

We provide the following software and services:

Allscripts Enterprise EHR is an award-winning EHR solution designed to enhance physician productivity using Tablet PCs, wireless handheld devices, or a desktop workstation for the purpose of automating the most common physician activities, including prescribing, dictating, ordering lab tests and viewing results, documenting clinical encounters and capturing charges, among others. Allscripts Enterprise is the clinical software solution of choice for multi-specialty and specialty practices as well as academic medical centers and hospital sponsored initiatives. Uniquely designed for the specific needs of physicians in today s increasingly interconnected healthcare environment, Allscripts Enterprise empowers and connects an organization clinically, operationally and financially.

Allscripts Enterprise PM is a practice management system that streamlines administrative aspects of physician practices, including patient scheduling, electronic remittances, electronic claims submission and electronic statement production. This system also provides multiple resource scheduling, instant reporting and referral tracking. Our electronic data interchange (EDI) solution facilitates statement management processing, claims management processing, electronic remittances and appointment reminders.

Allscripts Professional EHR is targeted at small to mid-sized physician practice groups. Similar to our Enterprise EHR, this solution automates the most common physician activities, such as prescribing, clinical reporting, ordering lab tests and viewing results and capturing charges. We also offer a disaster recovery solution that safeguards data and provides remote application access in the event of a failure at the primary system site.

Allscripts Professional PM is a practice management system that streamlines administrative aspects of physician practices, including patient scheduling, electronic remittances, electronic claims submission and electronic statement production. This system, which provides the engine for Enterprise Practice Management, also provides multiple resource scheduling, instant reporting and referral tracking. Our EDI solution facilitates statement management processing, claims management processing, electronic remittances and appointment reminders.

Allscripts MyWay is an integrated solution utilizing one unified database covering practice management, EHR and claims management. The MyWay solution is designed for smaller-sized physician practices and allows physicians to choose from a hosted service to minimize the cost and effort of using advanced technology or from an on-premise solution version which allows for the leverage of existing IT infrastructure and in-house capabilities.

Allscripts Document Management is a proven medical document management solution used by more than 18,000 healthcare professionals throughout the U.S. This award-winning program instantly improves chart access and practice workflow by electronically scanning and filing your current documents and making them accessible to an entire staff regardless of their location. Allscripts Document Management offers physician practices a Bridge for their technology adoption.

Allscripts ePrescribe is an easy-to-use, web-based e-prescribing solution that is safe, secure, requires no downloading and no new hardware. The software is being offered free of charge to every prescriber in America in furtherance of the National ePrescribing Patient Safety Initiative, a collaborative initiative introduced and led by us to enhance patient safety and reduce preventable medication errors. Allscripts ePrescribe can be a starting point for medical groups to transition over time to a complete EHR.

Allscripts ED is an emergency department information system designed to manage patient flow through the emergency department by tracking patient location, activity and outstanding orders and procedures.

Table of Contents

These solutions guide emergency clinicians in entering consistent, complete and efficient documentation on patients and provide shareable, real-time, mobile access to patient information from registration to discharge.

Allscripts Payerpath is a claims management service in the United States with more than 600 million claims and revenue cycle transactions processed annually. Used by approximately 110,000 physicians, Payerpath provides the credibility, experience and results demanded by both payers and providers. Payerpath can help organizations succeed in the business of healthcare through improved medical claim and claim management processes that lead to cleaner claims and faster payments.

Allscripts Revenue Cycle Management Services (RCM Services) is a complete end-to-end, integrated financial and administrative management solution for physician practices. The SaaS business solution requires no new hardware and minimal up-front costs, and is designed to meet the regulatory requirements of health reform. Allscripts RCM Services provides physician practices of every size and specialty with a complete outsourced revenue cycle solution that is paid for on an ongoing basis, as a percentage of their monthly collections.

Allscripts Homecare is a care system designed to improve clinical quality of care, financial performance, and operational control for large, integrated home care organizations and small home care companies. Business, clinical, and scheduling functionality for multiple lines of business home health, hospice, and private duty are combined seamlessly in one integrated home care software system.

Allscripts Post-Acute Solutions streamline the transition of care process between hospitals and post-acute care facilities. We currently have approximately 10,000 acute and post-acute care customers nationwide that will exchange over four million electronic hospital referrals. Allscripts post-acute solutions include: Referral Management, Referral Management Plus, Allscripts Mobile and Core System Integration.

Allscripts Care Management is a fully-integrated web-based solution that simplifies and consolidates utilization management, discharge planning, documentation integrity, audit management, quality management and risk management. Providing a single worklist for all care management processes, the Allscripts Care Management system transforms the administrative process for hospitals and post-acute care facilities, improving efficiency, streamlining and improving the quality of patient care, and generating cost savings and higher revenues. The suite of software that makes up Allscripts Care Management includes: Allscripts Utilization Management, Allscripts Discharge Planning, Allscripts Documentation Integrity, Allscripts Audit Management, Allscripts Quality and Risk Management. These systems are based on a SaaS solution model designed to provide ease of use and minimal IT staff involvement at the hospital.

Sunrise Enterprise is our software family of acute solutions, including the following clinical, access, financial and departmental solutions for hospitals:

Sunrise Clinical Manager includes the major integrated applications Sunrise Acute Care, Sunrise Ambulatory Care, Sunrise Critical Care, Sunrise Emergency Care and Sunrise Pharmacy, in addition to related modules and capabilities, such as Knowledge-Based Charting, Knowledge-Based Medication Administration and others. Sunrise Clinical Manager enables a physician or other authorized clinician to view patient data and enter orders quickly at the point of care, from virtually any other point in the enterprise or through secure remote access, providing evidence-based clinical decision support at the time of order entry.

Sunrise Ambulatory Care is considered a module of Sunrise Clinical Manager that is typically implemented within physician practices owned by SCM-client hospitals; however, it is a full-service EHR that may also serve as a stand-alone solution for independent physician practices. Sunrise Ambulatory Care is built on the same database as Sunrise Clinical Manager, ensuring seamless integration and flow of patient information between the physician office and hospital.

Table of Contents

Sunrise Access Manager, which shares the Sunrise Clinical Manager platform and health data repository, includes Sunrise Enterprise Scheduling and Sunrise Enterprise Registration. These integrated solutions enable healthcare providers to identify a patient at any time within a healthcare organization and to collect and maintain patient information on an enterprise-wide basis.

Sunrise Patient Financials provides centralized enterprise-wide business office capabilities that help healthcare organizations improve financial workflows and more effectively manage their patient billing, accounts receivable, and contract management functions. This helps them reduce costs for this important function and maximize and accelerate appropriate reimbursements from patients and other parties.

Sunrise EPSi provides integrated analytics, budgeting and knowledge-based decision support designed to bring together all the major components of financial management strategic planning, product line budgeting, cost accounting, and operational and capital budgeting to plan more effectively and accurately for the future and address the financial challenges facing healthcare organizations today. Sunrise EPSi is a fully integrated, web-based solution that can load and process data from virtually any healthcare or business software or system.

Sunrise Patient Flow gives hospitals effective management and visibility of patients movements throughout the enterprise enabling hospital management to identify bottlenecks and operational constraints and better coordinate resources to optimize patient flow. The solution provides enterprise-wide transparency and control over the flow process from a patient s arrival in the Emergency Department or Admitting to patient placement and care delivery throughout hospital departments and through well-coordinated discharge planning and fast bed turnover.

Sunrise Clinical Analytics is an advanced clinical business intelligence solution that enables organizations to effectively track and measure clinical performance and identify how clinician actions impact outcomes. This healthcare-specific, integrated and flexible solution helps organizations monitor and improve performance related to core measures, hospital-acquired complications and other quality initiatives. The capability to track and report on such quality measures is increasingly being required of healthcare organizations.

Other Clinical/Ancillary acute solutions include:

Sunrise Record Manager is a health information management (HIM) solution that automates the workflow associated with the collection, maintenance and distribution of information to maximize EHR benefits. Sunrise Record Manager helps hospitals better meet regulatory reporting requirements by making data centrally, electronically accessible for easier, faster information gathering and compilation in the enterprise health information system.

Sunrise Laboratory helps high-volume hospital laboratories improve operational performance, saving both time and money and improving effective patient care. Sunrise Laboratory helps automate laboratory departmental workflow from end to end, with decision-making and reporting driven by real-time clinical information. Laboratory departments face increasing regulatory requirements, growing cost pressures, and the need to meet clinical service levels and maintain patient and physician satisfaction despite increasing volumes of work. With fully automated workflow and support for multi-departmental laboratories across a healthcare organization integrated into one information system, Sunrise Laboratory helps labs maximize throughput, decrease turnaround time, capture more revenue, and improve quality and compliance.

Sunrise Radiology, a comprehensive radiology information system, and the **Sunrise PACS** picture archiving and communications system (the latter powered by Sectra) can be implemented together, separately, or as part of an image-enabled clinical information system. They deliver imaging data as an integrated part of the overall patient record that is accessible to clinicians at the point of care or other points of decision-making using any Sunrise Enterprise-enabled device.

15

Table of Contents

Services

Professional Services. We offer our clients professional services associated with the implementation of our software, the conversion and integration of their historical data into our software and systems, ongoing training and support in the use of our software, and consulting services to help clients improve their operations. Allscripts Speed to Value methodology helps our clients quickly achieve value from their investment in Allscripts solutions through accelerated software installation and systems configuration. Allscripts implementation and consulting services teams work collaboratively with clients to design and execute a project plan that is adapted to each client s unique timelines, software dependencies, hardware and network prerequisites, workflows and operational goals.

Remote Hosting. We offer remote hosting services to help our clients manage their complex healthcare IT solutions infrastructure while freeing up physical space, resources and costs associated with maintaining computer servers and deploying client-based applications on-site. Under this offering, we assume responsibility for processing Allscripts and/or non-Allscripts applications for our clients using equipment and personnel at our facilities. Other remote services, such as remote monitoring and remote help desk, are also offered. Software installation, upgrades and patches and network configuration and repairs are handled by Allscripts IT professionals behind the scenes, so hospital IT departments can focus on more strategic initiatives.

Information Technology Outsourcing. We provide full, partial or transitional IT outsourcing services to our clients. This service allows healthcare organizations to concentrate on their core mission while leveraging Allscripts knowledge of healthcare processes and proven healthcare IT methodologies to build and manage an IT infrastructure that helps organizations derive value from their technology investments. We assume partial to total responsibility for a healthcare organization s IT operations using our employees and assets. These services include facilities management, by which we assume responsibility for all aspects of client internal IT operations. These services may also include remote hosting and/or other remote services. In one or more combinations, these services help our clients to minimize the capital investment involved in staffing and maintaining its IT operations.

Research and Development

The majority of our software is based on Microsoft s .NET Framework and other industry standards.

Our latest-generation clinical and access solutions utilize the same architecture and share the same health data repository and many other components, while being adapted for the workflows of different environments. This enables our clients to tie together their workflows and operations across the entire continuum of care. Further, our software is built upon an open architecture that supports the secure exchange of data between systems, as well as the ability to embed and present content.

Our commitment to deliver world-class products means we must continually invest in software development. In recent years we have significantly expanded our software development efforts in India, which enables us to respond more efficiently and cost effectively to changes in our software design and product development strategy.

The primary purposes of our research and development groups are to develop new features and enhancements to our respective solutions, ensure that our solutions comply with continually evolving regulatory requirements and create additional opportunities to connect our systems to the healthcare community.

Table of Contents

We capitalize software development costs incurred from the time technological feasibility of the software is established until the software is available for general release. Non-capitalizable research and development costs and other computer software maintenance costs related to software development are expensed as incurred. Our total spending consists of research and development costs directly recorded to expense and also includes capitalized software development costs as follows:

(Dollar amounts in thousands)	Year Ended December 31, 2011	Seven Months Ended December 31, 2010	Year Ended May 31, 2010	2009
Research and development costs directly recorded to expense	$104,106	$43,261	$49,206	$39,431
Capitalized software development costs	60,748	36,936	21,097	14,001
Total spending	$164,854	$80,197	$70,303	$53,432
Software and related services revenue	$1,444,077	$613,309	$704,502	$534,018
Total spending as a % of software and related services revenue	11%	13%	10%	10%

Industry and Competition

The market for our products and services is intensely competitive and is characterized by rapidly evolving technology and product standards, technology and user needs and the frequent introduction of new products and services. Some of our competitors may be more established, benefit from greater name recognition and have substantially greater financial, technical, and marketing resources than us. We compete on the basis of several factors, including: breadth and depth of services, reputation, reliability, accuracy and security, client service, price, and industry expertise and experience.

There are numerous companies that offer acute and/or ambulatory EHR (along with related services) and practice management products, and the marketplace remains fragmented. We face competition from several types of organizations, including providers of practice management solutions, electronic prescribing solutions, ambulatory and acute care EHR solutions, hospital computerized physician order entry, emergency department information systems, analytics, performance management and care management solutions, post-acute discharge management solutions, and homecare EHR solutions.

Our principal existing competitors in the physician healthcare information systems and services market include athenahealth Inc., Cerner Corporation, eClinicalWorks Inc., Emdeon Business Services LLC, Epic Systems Corporation, General Electric Company, Greenway Medical, McKesson Corporation, Quality Systems, Inc., The Trizetto Group, Inc., Vitera Healthcare Solutions and Wellsoft Corporation.

Our principal existing competitors in the hospital and post-acute healthcare information systems and services market include Cerner Corporation, Curaspan Health Group, Epic Systems Corporation, General Electric Company, Maxsys Ltd., McKesson Corporation, MedHost, Meditech, Midas+, Picis, ProviderLink, Quadramed, Siemens AG and Wellsoft Corporation.

Recent Industry Developments

On February 17, 2009, President Barack Obama signed the American Recovery & Reinvestment Act (ARRA), which incorporated the HITECH Act (HITECH) and federal meaningful use incentive program. HITECH provides financial incentives through the Centers for Medicare and Medicaid Services (CMS) to physicians and hospitals that prove they have adopted and are using Electronic Health Record (EHR) technology to improve both the quality and cost-effectiveness of patient care. Studies demonstrate that effective use of EHRs

Table of Contents

reduces medical errors, improves clinical quality and leads to better patient outcomes by enabling real-time access to patient records, medical information and best practices, and electronic connectivity to all healthcare stakeholders, including patients.

In addition to other components focused on economic stimulus, the ARRA law provides for what is expected to be over $30 billion in funds supporting health information technology utilization. The total includes $2 billion in discretionary funds for supporting programs and an estimated $27 billion for incentives to be distributed through Medicare and Medicaid beginning in 2011 to ensure widespread adoption and use of interoperable healthcare IT systems, such as the EHR. Physicians who have not adopted certified EHR systems by 2014 will have their Medicare reimbursements reduced by up to 5 percent beginning in 2015. Hospitals that do not successfully demonstrate meaningful use in 2015 and beyond will have a payment adjustment in their Medicare reimbursement.

Through the meaningful use incentives, CMS provides physicians financial incentive payments of up to $44,000 for Medicare providers or $64,000 for Medicaid providers over five years, beginning in 2011, for deploying and using a certified EHR to care for patients. Hospital incentives under HITECH are tied to several factors but begin with a base payment of $2 million. The law already has ignited significant job growth in the information technology sector and, according to a Congressional Budget Office review of the law s impact, is expected to drive up to 90 percent of US physicians to adopt EHRs in the next decade.

The U.S. Department of Health & Human Services announced in early December 2011 that providers (hospitals and physicians) who participated in the meaningful use program in 2011 by attesting in that year will not have to start complying with Stage 2 requirements until 2014 rather than the originally scheduled 2013. The deferral was provided in order to provide sufficient time to develop and test updates to software applications meeting the anticipated Stage 2 requirements and transition all providers to the updated applications while also ensuring patient safety. We do not expect the deferral to provide incentive nor a disincentive for new orders. Under this change, we will have to transition all clients who attest in 2011 and 2012 to our Stage 2 versions by the start of 2014. This is because the announced policy change offers no timing delay for those first attesting in 2012, coupled with the fact that providers must show a full year s use after their first year; accordingly, the result is that anyone who started in 2011 or 2012 will need to comply with the same deadline.

The required implementation of new diagnosis and disease codes under ANSI-5010 and ICD-10 by 2013 is also of immediate interest to our client base. These regulations will present a positive opportunity for the company in the context of product upgrades, client service and training. However, the adoption of these standards could place additional burden on us to meet implementation and training demands during a period of significant client upgrades and new orders associated with accelerating EHR adoption.

Another factor impacting demand for our solutions is the significant revision to provider reimbursement that is being undertaken at the federal level, fostering the move to a value-based system of care. As an example, the Centers for Medicare and Medicaid Services, or CMS, published the Final Rule for Accountable Care Organizations in October that will reward providers who can prove they ve decreased the cost of caring for Medicare patients while also exceeding certain quality thresholds. Healthcare organizations will need solutions like ours to shift from fee-for-service to fee-for-value because their basic reimbursement will be based, ultimately, on proving quality outcomes that are captured, communicated, measured and shared with other relevant providers. Coordinated care models, of which ACOs are one example, will require an interoperable Electronic Health Record that connects providers across entire communities to coordinate care. Another notable element of the new models being created by the department of Health & Human Services is that every part of the healthcare community is important, which highlights our strategic asset the Allscripts footprint in our 50,000 ambulatory practices, our relationships with over 1,500 acute care hospitals and our strong and growing penetration of the post-acute world, with more than 10,000 locations including homecare. Allscripts open platform is able to connect patient information into a single view and help to coordinate care, both inside an organization and throughout a community. Our analytics capabilities also provide insights that will drive both clinical and financial outcomes which will be core to provider revenue in the future.

Table of Contents

A related recent development is the Hospital Readmission Reduction Program which took effect October 1, 2011. The final rules require hospitals to be financially responsible for the cost of care provided to discharged patients readmitted to the hospital for the same problem within 30 days after discharge. As a result, we believe more hospitals may be interested in utilizing our Care Management and Discharge Management products, which streamline the flow of patient information from the hospital to community providers.

Strategic Alliances

Our key strategic relationships include the following:

Cisco Systems, Inc. We have a strategic partnership with Cisco to support our core business through enhanced communications technologies. Cisco technology powers many of the systems by which we communicate with our clients and employees. Additionally, Cisco® and Allscripts have partnered to offer an integrated solution that combines the latest in communications technology with Allscripts MyWay EHR. The combination of Cisco s secure network and communication system with Allscripts MyWay s key application features, easy to use interface and low acquisition costs provides physicians with a fully synchronized Digital Physician Office designed to raise their clinical productivity to new levels.

CVS Caremark. Our strategic partnership with CVS Caremark, the largest pharmacy healthcare provider in the United States, began in January 2010 when CVS Caremark transitioned thousands of providers using the company s proprietary iScribe e-prescribing tool to Allscripts e-prescribing and retired iScribe. Since then, the companies have continued to collaborate. For example, most recently CVS Caremark selected Allscripts MyWay EHR as the EHR for its MinuteClinic retail clinics nationwide. The first phase of the MyWay deployment, which is expected to ultimately include all 600+ MinuteClinics, is scheduled to begin in early 2012.

dbMotion. In 2011, we made a strategic investment in dbMotion, a private company that provides the technology behind the Allscripts Community Record. dbMotion and Allscripts are working together to deliver integrated core solutions to improve meaningful use of information from the physician s office to the hospital connecting the community within the patient s continuum of care and the physician s existing workflow.

Dell, Inc. We have a strategic partnership with Dell that encompasses hardware, hosting, and connecting healthcare communities. Dell is Allscripts primary hardware partner, providing the computer equipment needed by our clients to implement our solutions. Additionally, we signed an agreement with Dell in early 2010 to integrate Allscripts EHR and Practice Management solutions into Dell s hosted EHR solution for U.S. health systems and their affiliated physicians. The Dell program offers health systems and physicians the scale and expertise of one of the world s largest technology services organizations. Dell helps sponsor hospitals to configure the Allscripts solutions they select to meet the specific needs of their affiliated physician community. The solution includes application hosting, Health Information Exchange management and revenue opportunities for sponsor hospitals, and everything necessary to promote the solution to physicians.

Intuit, Inc. We have a strategic partnership with Intuit, a provider of business and financial management solutions for small and mid-sized businesses; financial institutions, including banks and credit unions; consumers and accounting professionals. Allscripts was the first practice management company to offer Quicken HealthSM Bill Pay. The online service integrates with our practice management and revenue cycle management solutions, used by 110,000 physicians, to help patients understand their medical bills and pay them online while helping physicians get paid faster. We also collaborate with Intuit in providing secure patient portals and personal health records, connecting patients to selected information about their physician s practice, including information from Allscripts EHR, e-prescribing and practice management solutions.

Medflow, Inc. Allscripts has a strategic partnership with Medflow that encompasses bundling Allscripts Professional PM with Medflow s EHR, a software solution designed exclusively for Ophthalmologists,

19

Table of Contents

and bringing it to market as a comprehensive solution. Since 1999, Medflow has been dedicated to serving the eye care community. They have 1500+ eye care specialists successfully using the Medflow EHR and no failed implementations. We believe that the Allscripts Professional PM and Medflow EHR create the most robust all-in-one software for eye care organizations.

M*Modal (formerly MedQuist Inc.) In August of 2011, we entered into a strategic partnership with Medquist/M*Modal Inc. to license their CDS Interactive Speech Recognition Applications for our suite of EHR solutions. M*Modal is a leading provider of clinical narrative capture services, speech understanding technology and clinical documentation workflow. M*Modal s enterprise solutions include mobile voice capture devices, speech recognition, Natural Language Understanding, and web-based workflow platforms and global network of medical editors. This strategic partnership helps healthcare organizations adopt our EHRs, transition to ICD-10, improve patient care, increase physician satisfaction and lower operational costs.

Microsoft. We have a strategic partnership with Microsoft, on whose technology Allscripts products are built. Microsoft SQL Server database and .NET Framework are at the core of our product development platform. The Microsoft platform and .NET Framework offer the ability to improve developer productivity and to deliver flexible applications faster. Microsoft .NET technologies enable healthcare organizations to achieve a lower total cost of ownership by easily integrating legacy applications with new technologies and enabling them to share information across organizations and platforms. By developing our solutions on the Microsoft platform, we have been able to integrate our ambulatory care, hospital, and post-acute care applications and make them easily available to physicians across the spectrum of care on a wide variety of devices.

Nuance. Our strategic partnership with Nuance encompasses utilizing the Nuance Dragon Speech recognition products with our suite of EHR and Radiology applications. Nuance, a leading provider of voice and language solutions for businesses and consumers around the world, has been a longtime partner of Allscripts and is considered a market leader in the areas of speech recognition, medical transcription, and clinical language understanding. By speech-enabling our applications, Nuance is helping to drive increased utilization of our products and improving overall client satisfaction. Revenue from the resale of Dragon has increased significantly over the past three years.

Financial Information About Segments

Financial information about our segments is described in Part II, Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations.

Backlog

As of December 31, 2011 and 2010, we had a committed contract backlog of $2.9 billion and $2.7 billion, respectively. A portion of the contracts in the committed contract backlog are accounted for under the percentage of completion accounting method. The determination of the revenue related to percentage of completion contracts which is expected to be recognized over the next twelve months is based upon the projected implementation period for such contracts. We estimate that approximately 41% of the total backlog at December 31, 2011 will be recognized as revenue during 2012.

Employees

As of December 31, 2011, we had approximately 6,300 employees. None of our employees are covered by a collective bargaining agreement or are represented by a labor union.

Geographic Information

We hereby incorporate by reference Note 18, Geographic Information, of the Notes to Consolidated Financial Statements in Part II, Item 8 of this report.

Table of Contents

Available Information

Our website address is www.allscripts.com. Information on our website is not incorporated by reference herein. Copies of our annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K and any amendments to those reports, as well as Section 16 reports filed by our insiders, are available free of charge on our website as soon as reasonably practicable after we file the reports with, or furnish the reports to, the Securities and Exchange Commission.

Item 1A. Risk Factors

You should carefully consider the risks and uncertainties described below and other information in this report. These are not the only risks and uncertainties that we face. Additional risks and uncertainties that we do not currently know about or that we currently believe are immaterial may also harm our business operations. If any of these risks or uncertainties occurs, it could have a material adverse effect on our business.

Risks Related to Our Business

If physicians and hospitals do not accept our products and services, or delay in deciding whether to purchase our products and services, our business, financial condition and results of operations will be adversely affected.

Our business model depends on our ability to sell our products and services. Acceptance of our products and services requires physicians and hospitals to adopt different behavior patterns and new methods of conducting business and exchanging information. We cannot assure you that physicians and hospitals will integrate our products and services into their workflow or that participants in the healthcare market will accept our products and services as a replacement for traditional methods of conducting healthcare transactions. Achieving market acceptance for our products and services will require substantial sales and marketing efforts and the expenditure of significant financial and other resources to create awareness and demand by participants in the healthcare industry. If we fail to achieve broad acceptance of our products and services by physicians, hospitals and other healthcare industry participants, or if we fail to position our services as a preferred method for information management and healthcare delivery, our business, financial condition and results of operations will be adversely affected.

We may not see the benefits of government programs initiated to accelerate the adoption and utilization of health information technology and to counter the effects of the current economic situation.

While government programs have been initiated to improve the efficiency and quality of the healthcare sector and also counter the effects of the current economic situation, including expenditures to stimulate business and accelerate the adoption and utilization of health care technology, we cannot assure you that we will receive any of those funds. For example, the passage of the Health Information Technology for Economic and Clinical Health Act, or HITECH, under the American Recovery and Reinvestment Act of 2009 (ARRA) authorizes what is expected to be up to almost $30 billion in expenditures, including discretionary funding, to further adoption of electronic health records. Although we believe that our service offerings will meet the requirements of the HITECH Act in order for our clients to qualify for financial incentives for implementing and using our services, there can be no certainty that the planned financial incentives, if made, will be made in regard to our services**.** We also cannot predict the speed at which physicians will adopt electronic health record systems in response to such government incentives, whether physicians will select our products and services or whether physicians will implement an electronic health record system at all. Any delay in the purchase and implementation of electronic health records systems by physicians in response to government programs, or the failure of physicians to purchase an electronic health record system, could have an adverse effect on our business, financial condition and results of operations. It is also possible that Congress will repeal or not fund HITECH or otherwise amend it in a manner that would be unfavorable to our business**.**

Table of Contents

Our integration of the legacy Eclipsys business is a complicated undertaking, which presents significant risks and expenses.

The success of the Eclipsys Merger will depend, in part, on the ability to realize the anticipated synergies, growth opportunities and cost savings from integrating Eclipsys legacy business with our other business segments. The integration of two independent companies is a complex, costly and time-consuming process and involves numerous risks, including difficulties in the assimilation of operations, services, products and personnel, the diversion of management s attention from other business concerns, the entry into markets in which we have little or no direct prior experience, the potential loss of our key employees, and the potential inability to maintain the goodwill of existing clients.

Additionally, the integration process involves significant expenses. During the ended December 31, 2011 and during the seven months ended December 31, 2010, we incurred expenses of approximately $36 million and $57 million, respectively, resulting from the Eclipsys Merger. As we work to integrate the businesses, we expect to incur significant additional expenses relating to the integration of personnel, geographically diverse operations, information technology systems, accounting systems, customers, and strategic partners of each company and the implementation of consistent standards, policies, and procedures, and we may be subject to possibly material write downs in assets and charges to earnings, which are expected to include severance pay and other costs. The integration process will be long-term and will continue to create significant expenses.

If management is unable to successfully combine our businesses in a manner that permits us to achieve the cost savings and operating synergies anticipated to result from the Eclipsys Merger, such anticipated benefits of the Eclipsys Merger may not be realized fully or at all or may take longer to realize than expected. Any of the above difficulties could adversely affect our ability to maintain relationships with customers, partners, suppliers and employees or our ability to achieve the anticipated benefits of the Eclipsys Merger, or could reduce our earnings or otherwise adversely affect our business and financial results.

Our failure to compete successfully could cause our revenue or market share to decline.

The market for our products and services is intensely competitive and is characterized by rapidly evolving technology and product standards, technology and user needs and the frequent introduction of new products and services. Some of our competitors may be more established, benefit from greater name recognition and have substantially greater financial, technical and marketing resources than us. Moreover, we expect that competition will continue to increase as a result of potential incentives provided by the Stimulus and as a result of consolidation in both the information technology and healthcare industries. If one or more of our competitors or potential competitors were to merge or partner with another of our competitors, the change in the competitive landscape could adversely affect our ability to compete effectively. We compete on the basis of several factors, including:

- breadth and depth of services;
- reputation;
- reliability, accuracy and security;
- client service;
- price; and
- industry expertise and experience.

Our principal existing competitors in the physician healthcare information systems and services market include Aprima Medical Software (formerly iMedica Corporation), athenahealth, Inc., Cerner Corporation, eClinicalWorks Inc., Emdeon Business Services LLC, Epic Systems Corporation, General Electric Company, Greenway Medical Technologies, McKesson Corporation, Quality Systems, Inc., Sage Software, Inc., The Trizetto Group, Inc., and Wellsoft Corporation.

Table of Contents

Our principal existing competitors in the hospital and post-acute healthcare information systems and services market include Cerner Corporation, eDischarge, Epic Systems Corporation, General Electric Company, Maxsys Ltd., McKesson Corporation, MedHost, Meditech, Midas+, Picis, ProviderLink, Quadramed, Siemens AG and WellSoft.

There can be no assurance that we will be able to compete successfully against current and future competitors or that the competitive pressures that we face will not materially adversely affect our business, financial condition and results of operations.

It is difficult to predict the sales cycle and implementation schedule for our software solutions.

The duration of the sales cycle and implementation schedule for our software solutions depends on a number of factors, including the nature and size of the potential customer and the extent of the commitment being made by the potential customer, which is difficult to predict. Our sales and marketing efforts with respect to hospitals and large health organizations generally involve a lengthy sales cycle due to these organizations complex decision-making processes. Additionally, in light of increased government involvement in healthcare, and related changes in the operating environment for healthcare organizations, our current and potential customers may react by curtailing or deferring investments, including those for our services. If potential customers take longer than we expect to decide whether to purchase our solutions, our selling expenses could increase and our revenues could decrease, which could harm our business, financial condition and results of operations. If customers take longer than we expect to implement our solutions, our recognition of related revenue would be delayed, which would adversely affect our business, financial condition and results of operations.

Our future success depends upon our ability to grow, and if we are unable to manage our growth effectively, we may incur unexpected expenses and be unable to meet our customers requirements.

We will need to expand our operations if we successfully achieve market acceptance for our products and services. We cannot be certain that our systems, procedures, controls and existing space will be adequate to support expansion of our operations. Our future operating results will depend on the ability of our officers and key employees to manage changing business conditions and to implement and improve our technical, administrative, financial control and reporting systems. We may not be able to expand and upgrade our systems and infrastructure to accommodate these increases. Difficulties in managing any future growth, including as a result of the Eclipsys Merger, could have a significant negative impact on our business, financial condition and results of operations because we may incur unexpected expenses and be unable to meet our customers requirements.

Competition for our employees is intense, and we may not be able to attract and retain the highly skilled employees we need to support our business.

Our ability to provide high-quality services to our clients depends in large part upon our employees experience and expertise. We must attract and retain highly qualified personnel with a deep understanding of the healthcare and health information technology industries. We compete with a number of companies for experienced personnel and many of these companies, including clients and competitors, have greater resources than we have and may be able to offer more attractive terms of employment. In addition, we invest significant time and expense in training our employees, which increases their value to clients and competitors who may seek to recruit them and increases the costs of replacing them. If we fail to retain our employees, the quality of our services could diminish, which could have a material adverse effect on our business, financial condition and results of operations.

Table of Contents

If we lose the services of our key personnel, we may be unable to replace them, and our business, financial condition and results of operations could be adversely affected.

Our success largely depends on the continued skills, experience, efforts and policies of our management and other key personnel and our ability to continue to attract, motivate and retain highly qualified employees. In particular, the services of Glen E. Tullman, our Chief Executive Officer, are integral to the execution of our business strategy. If one or more of our key employees leaves our employment, we will have to find a replacement with the attributes necessary to execute our strategy. Because competition for skilled employees is intense, and the process of finding qualified individuals can be lengthy and expensive, we believe that the loss of the services of key personnel could adversely affect our business, financial condition and results of operations. We cannot assure you that we will continue to retain such personnel. We do not maintain keyman insurance for any of our key employees.

If we are unable to successfully introduce new products or services or fail to keep pace with advances in technology, our business, financial condition and results of operations will be adversely affected.

The successful implementation of our business model depends on our ability to adapt to evolving technologies and increasingly aggressive industry standards and introduce new products and services accordingly. We cannot assure you that we will be able to introduce new products on schedule, or at all, or that such products will achieve market acceptance. Moreover, competitors may develop competitive products that could adversely affect our results of operations. A failure by us to introduce planned products or other new products or to introduce these products on schedule could have an adverse effect on our business, financial condition and results of operations.

If we cannot adapt to changing technologies, our products and services may become obsolete, and our business could suffer. Because the health information technology market is characterized by rapid technological change, we may be unable to anticipate changes in our current and potential customers requirements that could make our existing technology obsolete. Our success will depend, in part, on our ability to continue to enhance our existing products and services, develop new technology that addresses the increasingly sophisticated and varied needs of our prospective customers, license leading technologies and respond to technological advances and emerging industry standards and practices on a timely and cost-effective basis. The development of our proprietary technology entails significant technical and business risks. We may not be successful in using new technologies effectively or adapting our proprietary technology to evolving customer requirements or emerging industry standards, and, as a result, our business could suffer.

Our business depends in part on our ability to establish and maintain additional strategic relationships.

To be successful, we must continue to maintain our existing strategic relationships and establish additional strategic relationships with leaders in a number of healthcare and health information technology industry segments. This is critical to our success because we believe that these relationships contribute towards our ability to:

- extend the reach of our products and services to a larger number of physicians and hospitals and to other participants in the healthcare industry;
- develop and deploy new products and services;
- further enhance the Allscripts brand; and
- generate additional revenue and cash flows.

Entering into strategic relationships is complicated because strategic partners may decide to compete with us in some or all of our markets. In addition, we may not be able to maintain or establish relationships with key participants in the healthcare industry if we conduct business with their competitors. We depend, in part, on our

Table of Contents

strategic partners ability to generate increased acceptance and use of our products and services. If we lose any of these strategic relationships or fail to establish additional relationships, or if our strategic relationships fail to benefit us as expected, we may not be able to execute our business plan, and our business, financial condition and results of operations may suffer.

Future acquisitions may result in potentially dilutive issuances of equity securities, the incurrence of indebtedness and increased amortization expense.

Future acquisitions may result in dilutive issuances of equity securities, the incurrence of debt, the assumption of known and unknown liabilities, and the amortization of expenses related to intangible assets, all of which could have an adverse effect on our business, financial condition and results of operations. We have taken, and, if an impairment occurs, could take, charges against earnings in connection with acquisitions.

If our products fail to perform properly due to errors or similar problems, our business could suffer.

Complex software, such as ours, often contains defects or errors, some of which may remain undetected for a period of time. It is possible that such errors may be found after the introduction of new software or enhancements to existing software. We continually introduce new solutions and enhancements to our solutions, and, despite testing by us, it is possible that errors may occur in our software. If we detect any errors before we introduce a solution, we might have to delay deployment for an extended period of time while we address the problem. If we do not discover software errors that affect our new or current solutions or enhancements until after they are deployed, we would need to provide enhancements to correct such errors. Errors in our software could result in:

harm to our reputation;

lost sales;

delays in commercial releases;

product liability claims;

delays in or loss of market acceptance of our solutions;

license terminations or renegotiations;

unexpected expenses and diversion of resources to remedy errors; and

privacy and/or security vulnerabilities.

Furthermore, our customers might use our software together with products from other companies or those that they have developed internally. As a result, when problems occur, it might be difficult to identify the source of the problem. Even when our software does not cause these problems, the existence of these errors might cause us to incur significant costs, divert the attention of our technical personnel from our solution development efforts, impact our reputation and cause significant customer relations problems.

Our business depends on our intellectual property rights, and if we are unable to protect them, our competitive position may suffer.

Our business plan is predicated on our proprietary systems and technology products. Accordingly, protecting our intellectual property rights is critical to our continued success and our ability to maintain our competitive position. In addition to existing trademark, trade secret and

copyright law, we protect our proprietary rights through confidentiality agreements and technical measures. We generally do not have any patents on our technology. We generally enter into non-disclosure and assignment agreements with our employees and consultants and limit access to our trade secrets and technology. Nonetheless, in some instances, third parties

Table of Contents

may have access to source-code versions of software. Furthermore, our use and distribution of open source software and modules in connection with our business also presents risks. Open source commonly refers to software whose source code is subject to a license allowing it to be modified, combined with other software and redistributed, subject to restrictions set forth in the license. We cannot be certain that, under the terms of those licenses, our software will not become publicly available or that we will be found to be in material compliance with such agreements or that it might subject the company to claims of infringement. We cannot assure you that the steps we have taken have prevented or will prevent misappropriation of our technology. Misappropriations of our intellectual property have occurred in the past. Misappropriation of our intellectual property could have an adverse effect on our competitive position. In addition, we may have to engage in litigation in the future to enforce or protect our intellectual property rights or to defend against claims of infringement, misappropriation or other violations of third-party intellectual property rights. We may incur substantial costs and the diversion of management s time and attention as a result and an adverse decision could have a negative impact on our business.

If we are deemed to infringe, misappropriate or violate the proprietary rights of third parties, we could incur unanticipated expense and be prevented from providing our products and services.

We are and may continue to be subject to intellectual property infringement, misappropriation or other intellectual property violation claims as our applications functionality overlaps with competitive products and third parties may claim that we do not own or have rights to use all intellectual property rights used in the conduct of our business. We do not believe that we have infringed or are infringing on any valid or enforceable proprietary rights of third parties. However, claims are occasionally asserted against us, and we cannot assure you that infringement, misappropriation or claims alleging intellectual property violations will not be asserted against us in the future. Also, we cannot assure you that any such claims will be unsuccessful. We could incur substantial costs and diversion of management resources defending any such claims. Furthermore, a party making a claim against us could secure a judgment awarding substantial damages, as well as injunctive or other equitable relief that could effectively block our ability to provide products or services. In addition, we cannot assure you that licenses for any intellectual property of third parties that might be required for our products or services will be available on commercially reasonable terms, or at all. Such claims also might require indemnification of our clients at significant expense.

We are and in the future may be involved in legal proceedings that could materially adversely affect us.

We are currently engaged in legal proceedings on a variety of matters and additional claims or disputes may arise in the future. Results of legal proceedings are subject to significant uncertainty and, regardless of the merit of the claims, litigation may be expensive, time-consuming, disruptive to our operations and distracting to management. If one or more of these matters were resolved against us, it could have a material adverse impact on our business, financial condition, results of operations or cash flows. Legal proceedings could also result in consent decrees, criminal sanctions or orders requiring a change in our business practices, which could also adversely affect our business and results of operations. For additional information regarding certain legal proceedings in which we are involved, see Note 19, Contingencies, of the Notes to Consolidated Financial Statements in Part II, Item 8 of this report.

If our content and service providers fail to perform adequately, or to comply with laws, regulations or contractual covenants, our reputation and our business, financial condition and results of operations could be adversely affected.

We depend on independent content and service providers for communications and information services and for many of the benefits we provide through our software applications and services, including the maintenance of managed care pharmacy guidelines, drug interaction reviews, the routing of transaction data to third-party payers and the hosting of our applications. Our ability to rely on these services could be impaired as a result of the failure of such providers to comply with applicable laws, regulations and contractual covenants, or as a result of

Table of Contents

events affecting such providers, such as power loss, telecommunication failures, software or hardware errors, computer viruses and similar disruptive problems, fire, flood and natural disasters. Any such failure or event could adversely affect our relationships with our customers and damage our reputation. This would adversely affect our business, financial condition and results of operations. In addition, we may have no means of replacing content or services on a timely basis or at all if they are inadequate or in the event of a service interruption or failure. We also rely on independent content providers for the majority of the clinical, educational and other healthcare information that we provide. In addition, we depend on our content providers to deliver high quality content from reliable sources and to continually upgrade their content in response to demand and evolving healthcare industry trends. If these parties fail to develop and maintain high quality, attractive content, the value of our brand and our business, financial condition and results of operations could be impaired.

We may be liable for use of content we provide.

We provide content for use by healthcare providers in treating patients. Third-party contractors provide us with most of this content. If this content is incorrect or incomplete, adverse consequences, including death, may occur and give rise to product liability and other claims against us. In addition, certain of our solutions provide applications that relate to patient clinical information, and a court or government agency may take the position that our delivery of health information directly, including through licensed practitioners, or delivery of information by a third party site that a consumer accesses through our websites, exposes us to personal injury liability, or other liability for wrongful delivery or handling of healthcare services or erroneous health information. While we maintain product liability insurance coverage in an amount that we believe is sufficient for our business, we cannot assure you that this coverage will prove to be adequate or will continue to be available on acceptable terms, if at all. A claim that is brought against us that is uninsured or under-insured could harm our business, financial condition and results of operations. Even unsuccessful claims could result in substantial costs and diversion of management resources.

If our security is breached, we could be subject to liability, and customers could be deterred from using our products and services.

Our business relies on the secure electronic transmission, storage, and hosting of sensitive information, including protected health information, financial information, and other sensitive information relating to our customers, company and workforce. As a result, we face some risk of a deliberate or unintentional incident involving unauthorized access to our computer systems that could result in misappropriating or losing assets or sensitive information, corrupting data, or otherwise disrupting business operations. Similarly, denial-of-service or other Internet-based attacks may range from mere vandalism of our electronic systems to systematic theft of sensitive information and intellectual property.

In light of this risk, we have devoted and continue to devote significant resources to protecting and maintaining the confidentiality of this information, including implementing security and privacy programs and controls, training our workforce, and implementing new technology. We have no guarantee that these programs and controls will be adequate to prevent all possible security threats. We believe that any compromise of our electronic systems, including the unauthorized access, use or disclosure of sensitive information or a significant disruption of our computing assets and networks, would adversely affect our reputation, our ability to fulfill contractual obligations, and would require us to devote significant financial and other resources to mitigate such problems, and increase our future cybersecurity costs including through organizational changes, deploying additional personnel and protection technologies, further training employees, and engaging third party experts and consultants. Moreover, unauthorized access, use, or disclosure of such sensitive information could result in civil or criminal liability or regulatory action, including potential fines and penalties. In addition, any real or perceived compromise of our security or disclosure of sensitive information, may result in lost revenues by, deterring customers from using or purchasing our products and services in the future or to use competing suppliers.

Table of Contents

In addition, we utilize third-party contractors, to store, transmit, or host sensitive information for our customers. While we have contractual relationships with these third-party contractors that require them to have appropriate security programs and controls in place and, frequently, to indemnify us, any compromise of these contractors security, could adversely affect our reputation, require us to devote financial and other resources to mitigate these breaches, or subject us to litigation from our customers.

Recently, other companies have experienced many high profile incidents involving data security breaches by entities that transmit and store sensitive information. Lawsuits resulting from these security breaches have sought very significant monetary damages, although many of these suits have yet to be resolved. While we maintain some insurance to cover these types of damages and costs, if we are sued for this type of security breach it is uncertain whether this coverage would be sufficient to cover the costs or damages assessed in this type of lawsuit against us.

If we are unable to obtain additional financing for our future needs, our ability to respond to competitive pressures may be impaired and our business, financial condition and results of operations could be adversely affected.

We cannot be certain that additional financing will be available to us on favorable terms, or at all. If adequate financing is not available or is not available on acceptable terms, our ability to fund our expansion, take advantage of potential acquisition opportunities, develop or enhance services or products, or respond to competitive pressures would be significantly limited.

If we are forced to reduce our prices, our business, financial condition and results of operations could suffer.

We may be subject to pricing pressures with respect to our future sales arising from various sources, including practices of managed care organizations, group purchasing arrangements made through government programs such as the Regional Extension Centers, and government action affecting reimbursement levels affecting physicians, hospitals, home health professionals or any combination thereof under Medicare, Medicaid and other government health programs. Our customers and the other entities with which we have a business relationship are affected by changes in statutes, regulations and limitations in governmental spending for Medicare, Medicaid and other programs. Recent government actions and future legislative and administrative changes could limit government spending for the Medicare and Medicaid programs, limit payments to hospitals and other providers, increase emphasis on competition, impose price controls, initiate new and expanded value-based reimbursement programs and create other programs that potentially could have an adverse effect on our customers and the other entities with which we have a business relationship. If our pricing experiences significant downward pressure, our business will be less profitable and our results of operations would be adversely affected. In addition, because cash from sales funds some of our working capital requirements, reduced profitability could require us to raise additional capital sooner than we would otherwise need.

If we incur costs exceeding our insurance coverage in lawsuits pending against us or that are brought against us in the future, it could adversely affect our business, financial condition and results of operations.

We are a defendant in lawsuits arising in the ordinary course of business. In the event we are found liable in any lawsuits filed against us, and if our insurance coverage were unavailable or inadequate to satisfy these liabilities, it could have an adverse effect on our business, financial condition and results of operations.

Our failure to license and integrate third-party technologies could harm our business.

We depend upon licenses for some of the technology used in our solutions from third-party vendors, and intend to continue licensing technologies from third parties. These technologies might not continue to be available to us on commercially reasonable terms or at all. Most of these licenses can be renewed only by mutual

Table of Contents

consent and may be terminated if we breach the terms of the license and fail to cure the breach within a specified period of time. Our inability to obtain, maintain or comply with any of these licenses could delay development until equivalent technology can be identified, licensed and integrated, which would harm our business, financial condition and results of operations.

Most of our third-party licenses are non-exclusive and our competitors may obtain the right to use any of the technology covered by these licenses and use the technology to compete directly with us. Our use of third-party technologies exposes us to increased risks, including, but not limited to, risks associated with the integration of new technology into our solutions, the diversion of our resources from development of our own proprietary technology and our inability to generate revenue from licensed technology sufficient to offset associated acquisition and maintenance costs. In addition, if our vendors choose to discontinue support of the licensed technology in the future or are unsuccessful in their continued research and development efforts, we might not be able to modify or adapt our own solutions.

If we fail to maintain and expand our business with our existing customers, or to effectively transition our customers to newer products, our business, financial condition and results of operations could be adversely affected.

Our business model depends on our success with maintaining our existing customers and selling follow-on and incremental products and services to our existing customers. In addition, our success with certain clients requires our achieving interoperability among the products offered by legacy Allscripts and legacy Eclipsys in order to provide a single solution that connects healthcare providers across care settings. Also critical to our success is our ability to sell our electronic health record products to our legacy entities practice management customer base. Additionally, certain of our clinical solutions business unit customers initially purchase one or a limited number of our products and services. These customers might choose not to expand their use of, or purchase, additional modules. Also, as we deploy new applications and features for our existing solutions or introduce new solutions and services, our current customers could choose not to purchase these new offerings. If we fail to generate additional business from our current customers, our revenue could grow at a slower rate or even decrease.

In addition, the transition of our existing customers to current versions of our products presents certain risks, including the risk of data loss or corruption, or delays in completion. If such events occur, our client relationships and reputation could be damaged, which could adversely affect our business and results of operations.

Changes in interoperability and other regulatory standards applicable to our software could require us to incur substantial additional development costs.

Our clients and the industry leaders enacting regulatory requirements are concerned with and often require that our software solutions be interoperable with other third party health IT suppliers. Market forces or governmental/regulatory authorities could create software interoperability standards that would apply to our solutions, and if our software solutions and/or healthcare devices are not consistent with those standards, we could be forced to incur substantial additional development costs. HITECH, which is part of ARRA, provides financial incentives to hospitals and doctors who demonstrate that they are meaningful electronic health record users, including a requirement that they use health information technology systems that are certified according to a set of standards for functionality, interoperability and security developed under the supervision of the Secretary of the Department of Health and Human Services. HITECH also imposes certain requirements upon governmental agencies to use, and requires health care providers, health plans, and insurers contracting with such agencies to use, systems that are certified according to such standards. The Secretary of the Department of Health and Human Services continues to modify those standards. Achieving HITECH certification is becoming a competitive requirement, resulting in increased software development and administrative expense to conform to these requirements. These standards and specifications, once finalized, will be subject to interpretation by the entities designated to test and certify such technology.

Table of Contents

We will incur increased development costs in delivering solutions to upgrade our software and healthcare devices to be in compliance with these varying and evolving standards, and delays may result in connection therewith. If our software solutions are not consistent with these evolving standards, our market position and sales could be impaired and we may have to invest significantly in changes to our software solutions, although we do not expect such costs to be significant in relation to the overall development costs for our solutions.

Changes in CMS diagnosis and inpatient procedure coding require us to make modifications to our products and services, which could result in significant development costs and which if unsuccessful could adversely affect our sales.

The Centers for Medicare and Medicaid Services, or CMS, has mandated the use of new patient codes for reporting medical diagnosis and inpatient procedures, referred to as the ICD-10 codes. CMS is requiring all providers, payers, clearinghouses, and billing services to utilize these ICD-10 codes when submitting claims for payment. ICD-10 codes will affect diagnosis and inpatient procedure coding for everyone covered by the Health Insurance Portability and Accountability Act (HIPAA), not just those who submit Medicare or Medicaid claims. Claims for services provided on or after October 1, 2013 must use ICD-10 codes for medical diagnosis and inpatient procedures or they will not be paid.

If our products and services do not accommodate CMS mandates at any future date, customers may cease to use those products and services that are not compliant or may choose alternative vendors and products that are compliant. This could adversely impact future revenues.

We are subject to a number of existing laws, regulations and industry initiatives, non-compliance with certain of which could materially adversely affect our operations or otherwise adversely affect our business, financial condition and results of operations, and we are susceptible to a changing regulatory environment.

As a participant in the healthcare industry, our operations and relationships, and those of our customers, are regulated by a number of federal, state and local governmental entities. The impact of this regulation on us is direct, to the extent we are ourselves subject to these laws and regulations, and is also indirect in that, in a number of situations, even though we may not be directly regulated by specific healthcare laws and regulations, our products must be capable of being used by our customers in a manner that complies with those laws and regulations. Inability of our customers to do so could affect the marketability of our products or our compliance with our customer contracts, or even expose us to direct liability under the theory that we had assisted our customers in a violation of healthcare laws or regulations. Because our business relationships with physicians, hospitals and other provider customers are unique and the healthcare information technology industry as a whole is relatively young, the application of many state and federal regulations to our business operations and to our customers is uncertain. Indeed, there are federal and state fraud and abuse laws, including anti-kickback laws and limitations on physician referrals, and laws related to distribution and marketing, including off-label promotion of prescription drugs that may be directly or indirectly applicable to our operations and relationships or the business practices of our customers. It is possible that a review of our business practices or those of our customers by courts or regulatory authorities could result in a determination that could adversely affect us. In addition, the healthcare regulatory environment may change in a way that restricts our existing operations or our growth. The healthcare industry generally and the EHR industry specifically is expected to continue to undergo significant legal and regulatory changes for the foreseeable future, which could have an adverse effect on our business, financial condition and results of operations. We cannot predict the effect of possible future enforcement, legislation and regulation.

Table of Contents

Specific risks include, but are not limited to, risks relating to:

Healthcare Fraud. Federal and state governments continue to enhance regulation of and increase their scrutiny over practices involving healthcare fraud affecting healthcare providers and professionals whose services are reimbursed by Medicare, Medicaid and other government healthcare programs. The healthcare industry is subject to laws and regulations on fraud and abuse which, among other things, prohibit the direct or indirect payment or receipt of any remuneration for patient referrals, or for the purchase or order, or arranging for or recommending referrals or purchases, of any item or service paid for in whole or in part by these federal or state healthcare programs. Federal enforcement personnel have substantial funding, powers and remedies to pursue suspected or perceived fraud and abuse. Moreover, both federal and state laws forbid bribery and similar behavior. Any determination by a regulatory, prosecutorial or judicial authority that any of our activities involving our clients, vendors or channel partners violate any of these laws could subject us to civil or criminal penalties, require us to change or terminate some portions of our business, require us to refund a portion of our license or service fees and disqualify us from providing services to clients doing business with government programs, all of which could have a material adverse effect on our business, financial condition and results of operations. Even an unsuccessful challenge by regulatory or prosecutorial authorities of our activities could result in adverse publicity, could require a costly response from us and could have a material adverse effect on our business, financial condition and results of operations.

Patient Information. As part of the operation of our business, our customers provide to us patient-identifiable medical information related to the prescription drugs that they prescribe and other aspects of patient treatment. Government and industry legislation and rulemaking, especially HIPAA, HITECH and standards and requirements published by industry groups such as the Joint Commission on Accreditation of Healthcare Organizations, require the use of standard transactions, standard identifiers, security and other standards and requirements for the transmission of certain electronic health information. National standards and procedures under HIPAA include the Standards for Electronic Transactions and Code Sets (the Transaction Standards); the Security Standards (the Security Standards); and the Standards for Privacy of Individually Identifiable Health Information (the Privacy Standards). The Transaction Standards require the use of specified data coding, formatting and content in all specified Health Care Transactions conducted electronically. The Security Standards require the adoption of specified types of security measures for certain patient identifiable health information (called Protected Health Information) in electronic form. The Privacy Standards grant a number of rights to individuals as to their Protected Health Information and restrict the use and disclosure of Protected Health Information by Covered Entities, defined as health plans, health care providers, and health care clearinghouses.

We have reviewed our activities and believe that we are a Covered Entity to the extent that we maintain a group health plan for the benefit of our employees. We have taken steps we believe to be appropriate and required to bring our group health plan into compliance with HIPAA and HITECH. For our operating functions, we believe that we are a hybrid entity, with both covered and non-covered functions under HIPAA. The Payerpath portion of our business qualifies as a health care clearinghouse when it files electronic health care claims on behalf of health care providers that are subject to HIPAA and HITECH and we have instituted policies and procedures to comply with HIPAA and HITECH in that role.

With respect to our other business functions, we do not believe we are a Covered Entity as a health care provider or as a health care clearinghouse; however, the definition of a health care clearinghouse is broad and we cannot offer any assurance that we could not be considered a health care clearinghouse under HIPAA or that, if we are determined to be a healthcare clearinghouse, the consequences would not be adverse to our business, financial condition and results of operations. In addition, certain provisions of the Privacy and Security Standards apply to third parties that create, access, or receive Protected Health Information in order to perform a function or activity on behalf of a Covered Entity. Such third parties are called Business Associates. Covered Entities and Business Associates must

Table of Contents

enter a written Business Associate Agreement , containing specified written satisfactory assurances, consistent with the Privacy and Security Standards and HITECH and its implementing regulations, that the third party will safeguard Protected Health Information that it creates or accesses and will fulfill other material obligations. Most of our customers are Covered Entities, and we function in many of our relationships as a Business Associate of those customers. We would face liability under our Business Associate Agreements and HIPAA and HITECH if we do not comply with our Business Associate obligations and applicable provisions of the Privacy and Security Standards and HITECH and its implementing regulations. The penalties for a violation of HIPAA or HITECH are significant and could have an adverse impact upon our business, financial condition and results of operations, if such penalties ever were imposed.

Subject to the discussion set forth above, we believe that the principal effects of HIPAA are, first, to require that our systems be capable of being operated by us and our customers in a manner that is compliant with the Transaction, Security and Privacy Standards and, second, to require us to enter into and comply with Business Associate Agreements with our Covered Entity customers. For most Covered Entities, the deadlines for compliance with the Privacy Standards and the Transaction Standards occurred in 2003, and for the Security Standards occurred in 2005.

Additionally, Covered Entities that are providers are required to adopt a unique standard National Provider Identifier, or NPI, for use in filing and processing health care claims and other transactions. Most Covered Entities were required to use NPIs in standard transactions by May 23, 2007.

We have policies and procedures that we believe comply with federal and state confidentiality requirements for the handling of Protected Health Information that we receive and with our obligations under Business Associate Agreements. In particular, we believe that our systems and products are capable of being used by or for our customers in compliance with the Transaction, Security and Privacy Standards and are capable of being used by or for our customers in compliance with the NPI requirements. If, however, we do not follow those procedures and policies, or they are not sufficient to prevent the unauthorized disclosure of Protected Health Information, we could be subject to civil and/or criminal liability, fines and lawsuits, termination of our customer contracts or our operations could be shut down. Moreover, because all HIPAA Standards and HITECH implementing regulations and guidance are subject to change or interpretation, we cannot predict the full future impact of HIPAA, HITECH or their implementing regulations on our business and operations. In the event that HIPAA, HITECH or their implementing regulations change or are interpreted in a way that requires any material change to the way in which we do business, our business, financial condition and results of operations could be adversely affected. Additionally, certain state privacy laws are not preempted by HIPAA and HITECH and may impose independent obligations upon our customers or us. Additional legislation governing the acquisition, storage and transmission or other dissemination of health record information and other personal information, including social security numbers, continues to be proposed and come into force at the state level. There can be no assurance that changes to state or federal laws will not materially restrict the ability of providers to submit information from patient records using our products and services.

Electronic Prescribing. The use of our software by physicians to perform a variety of functions, including electronic prescribing (ePrescribing), which refers to the electronic routing of prescriptions to pharmacies and the ensuing dispensation, is governed by state and federal law, including fraud and abuse laws. States have differing prescription format requirements, which we have programmed into our software. Many existing laws and regulations, when enacted, did not anticipate methods of e-commerce now being developed. While federal law and the laws of many states permit the electronic transmission of certain prescription orders, the laws of several states neither specifically permit nor specifically prohibit the practice. Restrictions exist at the Federal level, however, on the use of ePrescribing for controlled substances and certain other drugs, including a new regulation enacted by the Drug Enforcement Association (DEA) in mid-2010. Given the rapid growth of electronic transactions in

Table of Contents

healthcare, and particularly the growth of the Internet, we expect many additional states to directly address these areas with regulation in the near future. In addition, the Department of Health and Human Services published its final E-Prescribing and the Prescription Drug Program regulations on November 7, 2005 (effective January 1, 2006), and final regulations governing the standards for EPrescribing Under Medicare Part D on April 7, 2008 (effective June 6, 2008) (E-Prescribing Regulations). These regulations are required by the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (MMA). The E-Prescribing Regulations consist of detailed standards and requirements, in addition to the HIPAA Standard discussed above, for prescription and other information transmitted electronically in connection with a drug benefit covered by the MMA s Prescription Drug Benefit. These standards cover not only transactions between prescribers and dispensers for prescriptions but also electronic eligibility and benefits inquiries and drug formulary and benefit coverage information. The standards apply to prescription drug plans participating in the MMA s Prescription Drug Benefit. Other rules governing ePrescribing apply to other areas of Medicare and to Medicaid. The Medicare Improvements for Patients and Providers Act of 2008 (MIPPA) authorized a new and separate incentive program for individual eligible professionals who are successful electronic prescribers as defined by MIPPA. This incentive program is separate from and is in addition to the quality reporting incentive program authorized by Division B of the Tax Relief and Health Care Act of 2006 Medicare Improvements and Extension Act of 2006 and which is now known as the Physician Quality Reporting System (PQRS). Eligible professionals do not need to participate in PQRS to participate in the ePrescribing Incentive Program. Both programs were in effect throughout 2011 and will remain in effect for 2012. To the extent that these new initiatives and regulations foster the accelerated adoption of ePrescribing and Allscripts is a leader in the ePrescribing space, our business benefits from these incentive programs. However HITECH is the most prominent incentive program since its passage, reducing the impact the MIPPA and PQRS programs have in spurring greater adoption of ePrescribing or other health information technology.

In general, regulations in this area impose certain requirements which can be burdensome and evolve regularly, meaning that any potential benefits may be reversed by a newly-promulgated regulation that adversely affects our business model. Aspects of our clinical products are affected by such regulation because of the need of our customers to comply, as discussed above. Compliance with these regulations could be burdensome, time-consuming and expensive. We also are subject, as discussed above, to future legislation and regulations concerning the development and marketing of healthcare software systems or requirements related to product functionality. These could increase the cost and time necessary to market new services and could affect us in other respects not presently foreseeable.

Electronic Health Records. A number of important federal and state laws govern the use and content of electronic health record systems, including fraud and abuse laws that may affect the donation of such technology. As a company that provides electronic health record systems to a variety of providers of healthcare, our systems and services must be designed in a manner that facilitates our customers compliance with these laws. Because this is a topic of increasing state and federal regulation, we continue to monitor legislative and regulatory developments that might affect our business practices as they relate to electronic health record systems, revenue cycle management systems, ePrescribing and others. We cannot predict the content or effect of possible future regulation on our business practices. Also, as described above under Risks Related to Our Business, our Sunrise Clinical Manager suite of solutions, Allscripts ED, Allscripts Enterprise EHR, modular and complete, Allscripts Professional EHR, Allscripts MyWay EHR and Allscripts PeakPractice EHR are all certified by an ONC-approved certifying body as meeting the standards for functionality, interoperability and security under HITECH. Our failure to maintain this certification or otherwise meet industry standards would adversely impact our business.

Under HITECH, eligible health care professionals and hospitals may qualify for Medicare and Medicaid payment for the meaningful use of certified electronic health record technology that meets specified objectives. The criteria for meaningful use will be staged in three stages over the course of five years,

Table of Contents

from 2011 to 2015. On July 28, 2010, CMS published a final rule, effective September 27, 2010, to implement the first stage and define the minimum requirements that providers must meet through their use of certified electronic health record technology. On the same day, the Office of the National Coordinator for Health Information Technology (ONC) published a final rule, effective August 27, 2010, to identify the standards and certification criteria for the certification of electronic health record technology to support the achievement of Stage 1 meaningful use objectives. In addition, the Department of Health and Human Services is expected to propose regulations in 2012 defining capabilities providers and hospitals must meet in the second stage in order to receive incentive payments. Compliance with any such regulations could be expensive and time-consuming.

Claims Transmission. Our system electronically transmits medical claims by physicians to patients payers for immediate approval and reimbursement In addition, we offer revenue cycle management services that include the manual and electronic processing and submission of medical claims by physicians to patients payers for approval and reimbursement. Federal law provides that it is both a civil and a criminal violation for any person to submit, or cause to be submitted, a claim to any payer, including, without limitation, Medicare, Medicaid and all private health plans and managed care plans, seeking payment for any services or products that overbills or bills for items that have not been provided to the patient. We have in place policies and procedures that we believe assure that all claims that are transmitted by our system and through our services are accurate and complete, provided that the information given to us by our customers is also accurate and complete. If, however, we do not follow those procedures and policies, or they are not sufficient to prevent inaccurate claims from being submitted, we could be subject to liability. As discussed above, the HIPAA Transaction and Security Standards also affect our claims transmission services, since those services must be structured and provided in a way that supports our customers HIPAA compliance obligations. Furthermore, to the extent that there is some type of information security breach, it could have a material adverse effect on our business.

Medical Devices. Certain computer software products are regulated as medical devices under the Federal Food, Drug, and Cosmetic Act The FDA may become increasingly active in regulating computer software intended for use in healthcare settings. Depending on the product, we could be required to notify the FDA and demonstrate substantial equivalence to other products on the market before marketing such products or obtain FDA approval by demonstrating safety and effectiveness before marketing a product. Depending on the intended use of a device, the FDA could require us to obtain extensive data from clinical studies to demonstrate safety or effectiveness or substantial equivalence. If the FDA requires these data, we could be required to obtain approval of an investigational device exemption before undertaking clinical trials. Clinical trials can take extended periods of time to complete. We cannot provide assurances that the FDA will approve or clear a device after the completion of such trials. In addition, these products would be subject to the Federal Food, Drug and Cosmetic Act s general controls. The FDA can impose extensive requirements governing pre- and post-market conditions like approval, labeling and manufacturing. The FDA can impose extensive requirements governing product design controls and quality assurance processes. Failure to comply with FDA requirements can result in criminal and civil fines and penalties, product seizure, injunction, and civil monetary policies each of which could have an adverse effect on our business.

Additionally, recently enacted public laws reforming the U.S. healthcare system may have an impact on our business. The Patient Protection and Affordable Care Act (H.R. 3590; Public Law 111-148) (PPACA) and The Health Care and Education Reconciliation Act of 2010 (H.R. 4872; Public Law 111-152) (the Reconciliation Act), which amends the PPACA (collectively the Health Reform Laws), were signed into law in March 2010. The Health Reform Laws contain various provisions which may impact us and our customers. Some of these provisions may have a positive impact by implementing reimbursement programs that reward providers for patient-centered, health IT-dependent activities (e.g., Accountable Care Organizations), for example, while others, such as reductions in reimbursement for certain types of providers, may have a negative impact due to fewer available resources. Increases in fraud and abuse penalties may also adversely affect participants in the health care sector, including us.

Table of Contents

Increased government involvement in healthcare could adversely affect our business.

U.S. healthcare system reform at both the federal and state level could increase government involvement in healthcare, lower reimbursement rates and otherwise change the business environment of our customers and the other entities with which we have a business relationship. We cannot predict whether or when future healthcare reform initiatives at the federal or state level or other initiatives affecting our business will be proposed, enacted or implemented or what impact those initiatives may have on our business, financial condition or results of operations. Our customers and the other entities with which we have a business relationship could react to these initiatives and the uncertainty surrounding these proposals by curtailing or deferring investments, including those for our products and services. Additionally, the government has signaled increased enforcement activity targeting healthcare fraud and abuse, which could adversely impact our business, either directly or indirectly. To the extent that our customers, most of whom are providers, may be affected by this increased enforcement environment, our business could correspondingly be affected. Additionally, government regulation could alter the clinical workflow of physicians, hospitals and other healthcare participants, thereby limiting the utility of our products and services to existing and potential customers and curtailing broad acceptance of our products and services. Further examples of government involvement could include requiring the standardization of technology relating to electronic health records, providing customers with incentives to adopt electronic health record solutions or developing a low-cost government sponsored electronic health record solution, such as the VistA-Office electronic health record. Additionally, certain safe harbors to the federal Anti-Kickback Statute and corresponding exceptions to the federal Stark law may alter the competitive landscape. These safe harbors and exceptions are intended to accelerate the adoption of electronic prescription systems and electronic health records systems, and therefore provide new and attractive opportunities for us to work with hospitals and other donors who wish to provide our solutions to physicians. At the same time, such safe harbors and exceptions may result in increased competition from providers of acute electronic health record solutions, whose hospital customers may seek to donate their existing acute electronic health record solutions to physicians for use in ambulatory settings.

If the electronic healthcare information market fails to develop as quickly as expected, our business, financial condition and results of operations will be adversely affected.

The electronic healthcare information market is in the early stages of development and is rapidly evolving. A number of market entrants have introduced or developed products and services that are competitive with one or more components of the solutions we offer. We expect that additional companies will continue to enter this market, especially in response to recent government subsidies. In new and rapidly evolving industries, there is significant uncertainty and risk as to the demand for, and market acceptance of, recently introduced products and services. Because the markets for our products and services are new and evolving, we are not able to predict the size and growth rate of the markets with any certainty. We cannot assure you that markets for our products and services will develop or that, if they do, they will be strong and continue to grow at a sufficient pace. If markets fail to develop, develop more slowly than expected or become saturated with competitors, our business, financial condition and results of operations will be adversely affected.

Consolidation in the healthcare industry could adversely affect our business, financial condition and results of operations.

Many healthcare industry participants are consolidating to create integrated healthcare delivery systems with greater market power. As provider networks and managed care organizations consolidate, thus decreasing the number of market participants, competition to provide products and services like ours will become more intense, and the importance of establishing relationships with key industry participants will become greater. These industry participants may try to use their market power to negotiate price reductions for our products and services. Further, consolidation of management and billing services through integrated delivery systems may decrease demand for our products. If we were forced to reduce our prices, our business would become less profitable unless we were able to achieve corresponding reductions in our expenses.

Table of Contents

Business disruptions could affect our operating results.

A significant portion of our research and development activities and certain other critical business operations are concentrated in a few geographic areas. We are a highly automated business and a disruption or failure of our systems could cause delays in completing sales and providing services. A major earthquake, fire or other catastrophic event that results in the destruction or disruption of any of our critical business or information technology systems could severely affect our ability to conduct normal business operations and, as a result, our future operating results could be materially and adversely affected.

Risks Related to Our International Business Strategy

Our growing operations in India expose us to risks that could have an adverse effect on our results of operations.

We have a significant workforce employed in India engaged in a broad range of development, support and corporate infrastructure activities that are integral to our business and critical to our profitability. Further, while there are certain cost advantages to operating in India, significant growth in the technology sector in India has increased competition to attract and retain skilled employees with commensurate increases in compensation costs. In the future, we may not be able to hire and retain such personnel at compensation levels consistent with our existing compensation and salary structure. Many of the companies with which we compete for hiring experienced employees have greater resources than we have and may be able to offer more attractive terms of employment. In addition, our operations in India require ongoing capital investments and expose us to foreign currency fluctuations, which may significantly reduce or negate any cost benefit anticipated from such expansion.

In addition, our reliance on a workforce in India exposes us to disruptions in the business, political and economic environment in that region. Maintenance of a stable political environment is important to our operations, and terrorist attacks and acts of violence or war may directly affect our physical facilities and workforce or contribute to general instability. Our operations in India may also be affected by trade restrictions, such as tariffs or other trade controls, as well as other factors that may adversely affect our operations.

Our business strategy includes expansion into markets outside North America, which will require increased expenditures and if our international operations are not successfully implemented, such expansion may cause our operating results and reputation to suffer.

We are working to expand operations in markets outside North America. There is no assurance that these efforts will be successful. We have limited experience in marketing, selling, implementing and supporting our software abroad. Expansion of our international sales and operations will require a significant amount of attention from our management, establishment of service delivery and support capabilities to handle that business and commensurate financial resources, and will subject us to risks and challenges that we would not face if we conducted our business only in the United States. We may not generate sufficient revenues from international business to cover these expenses.

The risks and challenges associated with operations outside the United States may include: the need to modify our software to satisfy local requirements and standards, including associated expenses and time delays; laws and business practices favoring local competitors; compliance with multiple, conflicting and changing governmental laws and regulations, including healthcare, employment, tax, privacy, healthcare information technology, and data and intellectual property protection laws and regulations; laws regulating exports of technology products from the United States; fluctuations in foreign currency exchange rates; difficulties in setting up foreign operations, including recruiting staff and management; and longer accounts receivable payment cycles and other collection difficulties. One or more of these requirements and risks may preclude us from operating in some markets.

Table of Contents

Foreign operations subject us to numerous stringent U.S. and foreign laws, including the Foreign Corrupt Practices Act, or FCPA, and comparable foreign laws and regulations that prohibit improper payments or offers of payments to foreign governments and their officials and political parties by U.S. and other business entities for the purpose of obtaining or retaining business. As we expand our international operations, there is some risk of unauthorized payments or offers of payments by one of our employees, consultants, sales agents or distributors, which could constitute a violation by Allscripts of various laws including the FCPA, even though such parties are not always subject to our control. Safeguards we implement to discourage these practices may prove to be less than effective and violations of the FCPA and other laws may result in severe criminal or civil sanctions, or other liabilities or proceedings against us, including class action law suits and enforcement actions from the SEC, Department of Justice and overseas regulators.

Foreign operations present certain additional risks, including:

- the general economic and political conditions existing in those countries;
- difficulties in staffing and managing our foreign offices, and the increased travel, infrastructure and legal and compliance costs associated with multiple international locations;
- devaluations and fluctuations in currency exchange rates;
- imposition of limitations on conversion of foreign currencies or remittance of dividends and other payments by foreign subsidiaries;
- imposition or increase of withholding and other taxes on remittances and other payments by subsidiaries;
- imposition or increase of investment and other restrictions by foreign governments;
- longer payment cycles; and
- greater difficulties in accounts receivable collection.

Risks Related to Our Common Stock

Future sales of our common stock in the public market could adversely affect the trading price of our common stock that we may issue and our ability to raise funds in new securities offerings.

Future sales of substantial amounts of our common stock in the public market, or the perception that such sales could occur, could adversely affect prevailing trading prices of our common stock and could impair our ability to raise capital through future offerings of equity or equity-related securities. As of February 10, 2012, we had approximately:

- 191 million shares of common stock outstanding;
- 4 million shares of common stock reserved and available for issuance pursuant to outstanding stock options (at a weighted average exercise price of $10.23 per share); and

4 million shares of common stock reserved and available for issuance to settle outstanding restricted stock units and awards.

In connection with our acquisition strategy, we may issue shares of our common stock as consideration in other acquisition transactions. We cannot predict the effect, if any, that future sales of shares of common stock or the availability of shares of common stock for future sale will have on the trading price of our common stock.

Our issuance of preferred stock could adversely affect holders of our common stock and discourage a takeover.

Our Board of Directors is authorized to issue up to 1 million shares of preferred stock without any action on the part of our stockholders. Our Board of Directors also has the power, without stockholder approval, to set the

Table of Contents

terms of any series of preferred stock that may be issued, including voting rights (except that shares of preferred stock may not have more than one vote per share), dividend rights, preferences over our common stock with respect to dividends or in the event of a dissolution, liquidation or winding up and other terms. In the event that we issue preferred stock in the future that has preference over our common stock with respect to payment of dividends or upon our liquidation, dissolution or winding up, or if we issue preferred stock that is convertible into our common stock at greater than a one-to-one ratio, the voting and other rights of the holders of our common stock or the market price of our common stock could be adversely affected. In addition, the ability of our Board of Directors to issue shares of preferred stock without any action on the part of our stockholders may impede a takeover of us and prevent a transaction favorable to the holders of our common stock.

Other provisions of our charter documents and Delaware law may delay or inhibit potential acquisition bids that stockholders may believe are desirable, and the market price of our common stock may be lower as a result.

Our charter documents include an election to be governed by Section 203 of the Delaware General Corporation Law, which we refer to as the DGCL, which prohibits us from engaging in any business combination with an interested stockholder for a period of three years from the date the person became an interested stockholder, unless certain conditions are met. These provisions will make it more difficult for stockholders or potential acquirers to acquire us without negotiation and may apply even if some of our stockholders consider the proposed transaction beneficial to them. These provisions could also limit the price that investors are willing to pay in the future for shares of our common stock.

Our charter documents also contain provisions that may delay or inhibit potential acquisition bids, including provisions that:

- our stockholders are not allowed to act by written consent; and
- our stockholders are not allowed to call a special meeting of stockholders.

Our goodwill, which increased significantly as a result of the 2008 Transactions and the Eclipsys Merger, could become impaired and adversely affect our net worth and the market value of our common stock.

Under the purchase method of accounting, our assets and liabilities were recorded, as of completion of the 2008 Transactions, at their respective fair values and added to those of Misys, which are carried at their book values. The purchase price for the 2008 Transactions was allocated to legacy Allscripts tangible assets and liabilities and identifiable intangible assets, based on their fair values as of the date of completion of the 2008 Transactions. The excess of such price over those fair values has been recorded as goodwill.

Under the acquisition method of accounting, the purchase price paid in the Eclipsys Merger was allocated to the tangible and intangible assets acquired and liabilities assumed based on their estimated fair values as of the acquisition date. The fair value of the assets acquired and liabilities assumed represent management s best estimate of fair value. Goodwill was based on the residual difference between the purchase price and the value assigned to tangible and intangible assets and liabilities, and is not deductible for tax purposes. Among the factors that contributed to a purchase price resulting in the recognition of goodwill were Eclipsys history of profitability and high operating margins, strong sales force and overall employee base, and position in the healthcare information technology market.

Goodwill and other acquired intangibles expected to contribute indefinitely to our cash flows are not amortized, but must be evaluated by management at least annually for impairment. If the carrying value of goodwill exceeds its estimated fair value, impairment is deemed to have occurred and the carrying value of goodwill is written down to fair value. Under generally accepted accounting principles (GAAP) in the United States of America, this would result in a charge to our operating earnings. Accordingly, any determination requiring the write-off of a significant portion of goodwill could have a material impact on our operating results.

Table of Contents

Failure to maintain effective internal controls in accordance with Section 404 of the Sarbanes-Oxley Act of 2002 could have an adverse effect on our business and the trading price of our common stock.

Section 404 of the Sarbanes-Oxley Act requires us to evaluate annually the effectiveness of our internal controls over financial reporting as of the end of each fiscal year and to include a management report assessing the effectiveness of our internal controls over financial reporting in our annual report. If we fail to maintain the adequacy of our internal controls, as such standards are modified, supplemented, or amended from time to time, we can make no assurance that we will be able to conclude in the future that we have effective internal controls over financial reporting in accordance with Section 404. Additionally, if our independent registered public accounting firm is not satisfied with our internal controls over financial reporting or the level at which these controls are documented, designed, operated, tested or assessed, or if our independent registered public accounting firm interprets the requirements, rules or regulations differently than we do, then it may issue an adverse opinion. If we fail to maintain a system of effective internal controls, it could have an adverse effect on our business and stock price and we could be subject to sanctions or investigations by NASDAQ, the SEC or other regulatory authorities, which would require additional financial and management resources.

The market price of our common stock has been and may continue to be volatile.

The market price of our common stock is volatile and could fluctuate significantly in response to the factors described above and other factors, many of which are beyond our control, including:

- actual or anticipated variations in our quarterly operating results;
- announcements of technological innovations or new services or products by our competitors or us;
- changes in financial estimates by securities analysts;
- conditions and trends in the electronic healthcare information, Internet, e-commerce and pharmaceutical markets; and
- general market conditions and other factors.

In addition, the stock markets, especially The NASDAQ Global Select Market, have experienced extreme price and volume fluctuations that have affected the market prices of equity securities of many technology companies and Internet-related companies in particular. These fluctuations have often been unrelated or disproportionate to operating performance. These broad market factors may materially affect the trading price of our common stock. General economic, political and market conditions such as recessions and interest rate fluctuations may also have an adverse effect on the market price of our common stock. Volatility in the market price for our common stock may result in the filing of securities class action litigation.

Our quarterly operating results may vary.

Our quarterly operating results have varied in the past, and we expect that our quarterly operating results will continue to vary in future periods depending on a number of factors, some of which we have no control over, including customers budgetary constraints and internal acceptance procedures, seasonal variances in demand for our products and services, the sales, service and implementation cycles for our software products, potential downturns in the healthcare market and in economic conditions generally, and other factors described in this Risk Factors section.

We base our expense levels in part upon our expectations concerning future revenue, and these expense levels are relatively fixed in the short term. If we have lower revenue than expected, we may not be able to reduce our spending in the short term in response. Any shortfall in revenue would have a direct impact on our results of operations. In addition, our product sales cycle for larger sales is lengthy and unpredictable, making it difficult to estimate our future bookings for any given period. If we do not achieve projected booking targets for a given period, securities analysts may change their recommendations on our common stock. For these and other reasons, we may not meet the earnings estimates of securities analysts or investors, and our stock price could suffer.

39

Table of Contents

Our indebtedness will decrease business flexibility and increase borrowing costs.

The covenants under the Credit Agreement and our increased indebtedness and higher debt-to-equity ratio in comparison to our debt-to-equity ratio on a recent historical basis could have the effect, among other things, of:

- requiring us to apply a substantial portion of our cash flow from operations to payments on our debt, reducing the availability of cash flow to fund working capital, capital expenditures and other general corporate purposes;
- increasing our vulnerability to adverse general economic and industry conditions;
- limiting our flexibility in planning for, or reacting to, changes in business and the industry in which we operate;
- placing us at a competitive disadvantage compared to competitors that have less debt;
- limiting our ability to borrow additional funds on terms that are satisfactory or at all; and
- increasing our interest rates.

If we fail to comply with financial covenants under our credit facilities, our results of operation and financial condition could be adversely affected.

Our credit facilities contain certain financial covenants, including interest coverage and total leverage ratios. If we fail to comply with these covenants, an event of default may occur, resulting in, among other things, the requirement to immediately repay all outstanding amounts owed thereunder. Depending on borrowing levels in such an event, our liquid assets might not be sufficient to repay in full the debt outstanding under the credit facilities. Such an acceleration also would expose us to the risk of liquidation of collateral assets at unfavorable prices.

Coniston Exchange LLC (successor to Coniston, Inc.) may be liable for significant potential contingent tax liabilities arising out of the Misys Transactions and certain related transactions, or out of prior activities of Coniston Exchange LLC unrelated to those transactions.

Coniston Exchange LLC (successor to Coniston, Inc.), a Delaware limited liability company acquired by us in exchange for approximately 61 million shares of our common stock issued to subsidiaries of Misys (which transaction we refer to as the Exchange), might be subject to significant taxes, which we refer to as Transaction Taxes, arising out of the Exchange, certain share repurchases by us from subsidiaries of Misys and certain related restructuring transactions, which we refer to collectively as the Misys Transactions. In particular, the Exchange or other Misys Transactions might have resulted in the recognition of the built-in gain inherent in our shares of common stock held by Coniston Exchange LLC, which is significant. At the time of the Exchange, Coniston Exchange LLC held approximately 61 million shares of our common stock. Pursuant to the Framework Agreement, Misys agreed to indemnify us against any Transaction Taxes imposed on Coniston Exchange LLC. On November 3, 2010, Coniston Exchange LLC received a letter ruling from the Internal Revenue Service, which we refer to as the IRS, in response to a request submitted to the IRS by Misys on August 9, 2010. The letter ruling confirms, in effect, that the Misys Transactions will not result in the recognition of the built-in gain inherent in our shares of common stock held by Coniston Exchange LLC, and addresses certain other tax issues related to the Misys Transactions.

The ability to rely on any letter ruling depends on the accuracy and completeness of the information submitted to the IRS, which was primarily determined by Misys as the party that requested the letter ruling from the IRS. If any factual statements or representations submitted to the IRS were incorrect or untrue in any material respect, the letter ruling could be invalidated. As a result, no assurances can be given that our ability to rely on the letter ruling could not be challenged, in which case we would be required to rely on Misys indemnification obligation and ability to satisfy such indemnification obligation. Additionally, while the letter ruling addresses

40

Table of Contents

the material tax issues related to the Misys Transactions, not all issues were addressed. Pursuant to the Framework Agreement, Misys has also agreed to indemnify us against any contingent tax liability of Coniston Exchange LLC other than Transaction Taxes, such as taxes imposed as a result of prior activities of Coniston Exchange LLC, which we refer to as Historic Taxes, and Misys provided a bank guarantee in the amount of $45 million to support that indemnification obligation. The amount of the bank guarantee might be insufficient to fully cover Historic Taxes that might be imposed. Furthermore, although not expected, there could be circumstances in which the bank guarantee is reduced or terminated prior to the extinguishment of the resulting tax liabilities.

Misys also has agreed to indemnify us from taxes imposed on us as a result of the Exchange and from taxes imposed on us relating to certain withholding taxes, including any liability for failing to withhold certain taxes. Those indemnification obligations are not supported by a bank guarantee.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

Our properties consist of approximately 900 thousand square feet of leased facilities. Our facilities house various sales, services, support, development, data processing, technology functions, certain ancillary functions and other back-office functions for current operations of all segments. We believe that adequate, suitable lease space will continue to be available for our needs. Our corporate headquarters are located in Chicago, Illinois. In addition, we maintain leased facilities in Raleigh and Morrisville, North Carolina; Atlanta, Georgia; Burlington, Vermont; Richmond, Virginia; Louisville, Kentucky; West Des Moines, Iowa; Burlington, Massachusetts; Nashua, New Hampshire; Malverne and Pittsburgh, Pennsylvania; St. Louis, Missouri; Richmond, British Columbia, Canada; Vadodara (formerly known as Baroda), Pune and Bangalore, India; and certain other smaller facilities.

Item 3. Legal Proceedings

We hereby incorporate by reference Note 19, Contingencies, of the Notes to Consolidated Financial Statements in Part II, Item 8 of this report.

Item 4. Mine Safety Disclosures

Not applicable.

Table of Contents

PART II

Item 5. Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities Public Market for Common Stock

Our common stock is quoted on the NASDAQ Global Select Market under the symbol MDRX. The following table sets forth, for the periods indicated, the high and low sales prices per share of the common stock of Allscripts Healthcare Solutions, Inc. for the applicable periods as reported on the NASDAQ Global Select Market.

	High	Low
Fiscal Year Ended December 31, 2011		
Fourth Quarter (October 1, 2011 to December 31, 2011)	$21.10	$16.13
Third Quarter (July 1, 2011 to September 30, 2011)	$20.51	$13.85
Second Quarter (April 1, 2011 to June 30, 2011)	$23.13	$18.27
First Quarter (January 1, 2011 to March 31, 2011)	$22.21	$19.20
Seven Months Ended December 31, 2010		
Fourth Quarter (October 1, 2010 to December 31, 2010)	$19.97	$17.23
Third Quarter (July 1, 2010 to September 30, 2010)	$18.70	$15.65
June 1, 2010 to June 30, 2010	$19.93	$15.65
Fiscal Year Ended May 31, 2010		
Fourth Quarter (March 1, 2010 to May 31, 2010)	$22.55	$17.51
Third Quarter (December 1, 2009 to February 28, 2010)	$20.73	$16.38
Second Quarter (September 1, 2009 to November 30, 2009)	$22.21	$14.32
First Quarter (June 1, 2009 to August 31, 2009)	$17.48	$12.69

We had 190 million and 188 million common shares outstanding at December 31, 2011 and 2010, respectively. On February 10, 2012, we had approximately 465 common stock holders of record according to the records of our transfer agent. We currently do not intend to declare or pay cash dividends on our shares of common stock in the foreseeable future. Any future determination to pay cash dividends will be at the discretion of our Board of Directors and will depend upon our results of operations, financial condition, current and anticipated cash needs, contractual restrictions, restrictions imposed by applicable law and other factors that our Board of Directors deems relevant. Our Senior Secured Credit Facility covenants include a restriction on our ability to declare dividends and other payments in respect of our capital stock.

In April 2011, our Board of Directors approved a stock repurchase program under which we may purchase up to $200 million of our common stock over three years. Any share repurchases may be made through open market transactions, block trades, privately negotiated transactions (including accelerated share repurchase transactions) or other means.

Any repurchase activity will depend on factors such as our working capital needs, cash requirements for investments, debt repayment obligations, our stock price, and economic and market conditions. Our stock repurchase program may be accelerated, suspended, delayed or discontinued at any time.

Table of Contents

The following table summarizes the stock repurchase activity for the three months ended December 31, 2011 and the approximate dollar value of shares that may yet be purchased pursuant to our stock repurchase program:

(In thousands, except per share amounts)

Period	Total Number Of Shares Purchased	Average Price Paid Per Share	Total Number Of Share Purchased As Part Of Publicly Announced Plans Or Programs	Approximate Dollar Value Of Shares That May Yet Be Purchased Under The Plans Or Programs
10/1/11 10/31/11	0	$0.00	0	$150,000
11/1/11 11/30/11	0	$0.00	0	$150,000
12/1/11 12/31/11	80	$17.62	80	$148,591
	80	$17.62	80	

See Stock Repurchases under Liquidity and Capital Resources within Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, within this Annual Report for additional information regarding the share repurchase program.

For equity compensation plan information, please refer to Item 12 in Part III of this Annual Report.

Table of Contents

Performance Graph

The following graph compares the cumulative 5-year total return provided shareholders on Allscripts Healthcare Solutions, Inc. s common stock relative to the cumulative total returns of the NASDAQ Composite index and the NASDAQ Health Services index. An investment of $100 (with reinvestment of all dividends) is assumed to have been made in our common stock and in each of the indexes on December 31, 2006 and its relative performance is tracked through December 31, 2011.

	12/06	6/07	12/07	6/08	12/08	6/09	12/09	6/10	12/10	6/11	12/11
Allscripts Healthcare Solutions, Inc.	**100.00**	**94.41**	**71.95**	**45.98**	**72.09**	**115.26**	**147.01**	**117.00**	**140.04**	**141.13**	**137.64**
NASDAQ Composite	**100.00**	**108.27**	**110.26**	**95.18**	**65.65**	**76.45**	**95.19**	**88.93**	**112.10**	**117.60**	**110.81**
NASDAQ Health Services	**100.00**	**112.32**	**108.32**	**88.18**	**79.23**	**71.70**	**89.61**	**80.61**	**92.33**	**96.49**	**77.63**

The stock price performance included in this graph is not necessarily indicative of future stock price performance.

The information in this Performance Graph section shall not be deemed to be soliciting material or to be filed with the Securities and Exchange Commission or subject to Regulation 14A or 14C, or to the liabilities of Section 18 of the Securities Exchange Act of 1934.

Table of Contents

Item 6. Selected Financial Data

The selected consolidated financial data shown below should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and related notes included elsewhere in this report. The consolidated statements of operations data for the year ended December 31, 2011, the seven months ended December 31, 2010 and the years ended May 31, 2010 and 2009, and the consolidated balance sheet data at December 31, 2011 and 2010, are derived from audited consolidated financial statements included elsewhere in this report. The consolidated statements of operations data for the years ended May 31, 2008 and 2007 and the balance sheet data at May 31, 2010, 2009, 2008 and 2007 are derived from audited consolidated financial statements that are not included in this report. The historical results are not necessarily indicative of results to be expected for any future period.

(In thousands, except per share amounts)	Year Ended December 31, 2011[1]	Seven Months Ended December 31, 2010[2]	Year Ended May 31, 2010	2009[2]	2008[2],[3]	2007[2],[3]
Consolidated Statements of Operations Data:						
Revenue	$1,444,077	$613,309	$704,502	$548,439	$383,771	$379,693
Cost of revenue	778,512	315,140	315,658	256,288	176,870	189,128
Gross profit	665,565	298,169	388,844	292,151	206,901	190,565
Selling, general and administrative expenses	387,571	232,788	224,995	199,902	117,566	121,101
Research and development	104,106	43,261	49,206	39,431	37,784	40,880
Amortization of intangible assets	37,344	16,235	10,060	6,884	11,320	22,392
Income from operations	136,544	5,885	104,583	45,934	40,231	6,192
Interest expense	(20,750)	(9,687)	(1,993)	(2,162)	(296)	(272)
Interest income and other, net	1,685	843	946	626	219	94
Income (loss) before income taxes	117,479	(2,959)	103,536	44,398	40,154	6,014
Provision for income taxes	(43,870)	(2,606)	(40,666)	(18,376)	(14,755)	(2,160)
Net income (loss)	$73,609	($5,565)	$62,870	$26,022	$25,399	$3,854
Earnings (loss) per share:						
Basic	$0.39	($0.03)	$0.42	$0.21	$0.31	$0.05
Diluted	$0.39	($0.03)	$0.42	$0.21	$0.31	$0.05
Other Operating Data:						
System sales	$242,869	$113,117	$154,597	$98,469	$64,627	$71,368
Professional services	250,348	93,875	75,439	51,827	30,943	33,422
Maintenance	424,036	191,502	248,501	196,165	141,531	133,440
Transaction processing and other	526,824	214,815	225,965	187,557	146,670	141,463
Total software and related services revenue	1,444,077	613,309	704,502	534,018	383,771	379,693
Prepackaged medications[4]	0	0	0	14,421	0	0
Total revenue	$1,444,077	$613,309	$704,502	$548,439	$383,771	$379,693

Table of Contents

(In thousands)	As of December 31, 2011	2010	2010	As of May 31, 2009	2008	2007
Consolidated Balance Sheet Data:						
Cash, cash equivalents and marketable securities	$159,428	$131,136	$145,335	$73,426	$325	$1,370
Working capital	169,892	144,385	196,061	96,849	(6,776)	(33,875)
Goodwill and intangible assets, net	1,529,212	1,591,673	620,032	646,197	91,043	103,976
Total assets	2,517,341	2,418,587	1,094,690	952,656	179,268	171,247
Long-term debt	322,664	459,750	0	63,699	0	0
Total stockholders equity	1,476,720	1,383,768	806,825	700,370	110,649	81,169

(1) Subsequent to the February 16, 2012 announcement of our financial results for the year ended December 31, 2011, we adjusted our previously reported results for the quarter ended September 30, 2011. Please refer to the discussion of the related adjustments under *Management s Discussion and Analysis of Financial Conditions and Results of Operations Selected Quarterly Operating Results*. The impacts of the adjustments on the results for the year ended December 31, 2011 are reflected in the table above.

(2) Results of operations for the seven months ended December 31, 2010 include the results of operations of Eclipsys for the period subsequent to the date of the merger, August 24, 2010. Results of operations for the year ended May 31, 2009 include the results of operations of legacy MHS for the full year ended May 31, 2009 and the results of operations of legacy Allscripts are included from the completion of the 2008 Transactions on October 10, 2008 through May 31, 2009. Since the 2008 Transactions constitute a reverse acquisition for accounting purposes, the pre-acquisition combined financial statements of MHS are treated as the historical financial statements of Allscripts. Results of operations for the years ended May 31, 2008 and 2007 are the results of operations of legacy MHS only.

(3) For the years ended May 31, 2008 and 2007, the basic and diluted share count includes only the shares issued to Misys in connection with the 2008 Transactions. MHS did not have any shares outstanding prior to the merger, and therefore, the basic and diluted share count is comprised of the Allscripts shares issued on the October 10, 2008 acquisition date for all periods prior to the acquisition date as this reflects the Allscripts shares equivalent of MHS equity prior to the acquisition.

(4) On March 16, 2009, Allscripts closed on the sale of its prepackaged medications business to A-S Medication Solutions LLC (A-S). The results of operations for fiscal 2009 include the prepackaged medications business from the completion of the 2008 Transactions on October 10, 2008 through the March 16, 2009 closing of its sale to A-S. The prepackaged medications business has not been disclosed as discontinued operations due to Allscripts involvement with A-S through a separate Marketing Agreement.

Table of Contents

Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis should be read together with Selected Financial Data , our consolidated financial statements, the accompanying notes to these financial statements, and the other financial information that appears elsewhere in this Annual Report on Form 10-K. The consolidated statements of operations data and the consolidated statements of cash flows data for the twelve months ended December 31, 2010 (year ended December 31, 2010) and for the seven months ended December 31, 2009 are derived from unaudited comparative financial results.

Overview

Eclipsys Merger

On August 24, 2010, Allscripts-Misys Healthcare Solutions, Inc. (which changed its name to Allscripts Healthcare Solutions, Inc., Allscripts or the Company) completed the merger (the Eclipsys Merger) contemplated by an Agreement and Plan of Merger dated June 9, 2010 (Merger Agreement) by and among Allscripts, Arsenal Merger Corp., a wholly-owned subsidiary of Allscripts, and Eclipsys Corporation, an enterprise provider of solutions and services to hospitals and clinicians (Eclipsys). Eclipsys became a wholly-owned subsidiary of Allscripts as a result of the merger. The results of Eclipsys are consolidated with the results of Allscripts from August 24, 2010.

Misys Merger

On October 10, 2008, in accordance with the transactions (the 2008 Transactions) contemplated by the Agreement and Plan of Merger dated as of March 17, 2008 by and among Misys plc (Misys), Allscripts Healthcare Solutions, Inc. (legacy Allscripts), Misys Healthcare Systems (MHS or legacy MHS) and Patriot Merger Company, LLC (Patriot) a reverse acquisition for accounting purposes was completed. As a result of the completion of the 2008 Transactions, MHS became a wholly-owned subsidiary of legacy Allscripts and the newly combined entity was renamed Allscripts-Misys Healthcare Solutions, Inc. The 2008 Transactions were accounted for under the purchase method of accounting for business combinations in accordance with accounting principles generally accepted in the United States. Under the purchase method of accounting, with MHS as the accounting acquirer, the assets and liabilities of legacy Allscripts were recorded, as of October 10, 2008, at their fair values and added to those of MHS, which are carried at their book values.

Basis of Presentation

The merger with Eclipsys has been accounted for as a purchase business combination. Under the acquisition method of accounting, the purchase price was allocated to the tangible and intangible assets acquired and liabilities assumed based on their estimated fair values as of the acquisition date. The operating results of Eclipsys are included in the accompanying consolidated statements of operations for periods subsequent to the completion of the merger, August 24, 2010.

The 2008 Transactions constitute a reverse acquisition for accounting purposes. As such, the pre-acquisition combined financial statements of MHS are treated as the historical financial statements of Allscripts. The results of operations of legacy Allscripts are included in the accompanying consolidated statements of operations for periods subsequent to the date of the completion of the 2008 Transactions, October 10, 2008.

Business Overview

Allscripts is a leading provider of clinical, financial, connectivity and information solutions and related professional services that empower hospitals, physicians and post-acute organizations to deliver world-class outcomes. We deliver innovative solutions that provide physicians and other healthcare professionals with the information, insights and connectivity required to transform healthcare by improving the quality and efficiency of patient care.

Table of Contents

We primarily derive our revenue from sales of our proprietary software and related hardware, professional services and IT outsourcing services. These sales also are the basis for our recurring service contracts for software maintenance and transaction processing services. We currently report our financial results utilizing three business segments: clinical solutions, hospital solutions, and health solutions. The hospital solutions segment reflects the operations, subsequent to the completion of the merger, August 24, 2010, of our acute care hospital solutions acquired in the Eclipsys Merger. On March 16, 2009, we disposed of our prepackaged medications business which was previously reported as a separate operating segment.

We believe a combination of executive and legislative leadership at the federal level, industry standards, and federal incentives that exist today for meaningful use , e-prescribing and pay-for-quality initiatives is quickly making electronic health records as common as practice management systems in all provider offices. We believe that HITECH and other provisions provided by ARRA will continue to be the single biggest driver of healthcare IT adoption in 2012. We believe that we are well positioned in the market to take advantage of the material opportunity presented by HITECH and have seen a positive impact on new orders. We face the following other material opportunities, challenges and risks related to HITECH, which are further described below: (i) developing adequate capacity to satisfy the potential increased demand; (ii) ensuring that all of our products obtain applicable product certifications and our customers are able to achieve meaningful use as required by the Stimulus; (iii) taking advantage of demand trends; and (iv) positioning the Company as a provider to potential government-funded health care providers.

Management has taken steps to position the Company to have what we believe will be adequate capacity to meet the significant additional demand that could result from new orders related to HITECH. These steps include supplementing our internal direct sales force with strategic distribution partners with established sales forces focused on practices with one to five providers. Further, we have taken steps to improve the efficiency of our approach to new system installations. The Company utilizes its Speed-to-Value implementation program, which standardizes certain key processes across customer sites and decreases the number of hours required by our professional services team to enable installations of our clinical and practice management solutions. This strategy is predicated on repeatable, best practice workflows and was designed collaboratively by our services and development teams and is proprietary to the Company. The Speed-to-Value program has significantly reduced installation timeframes for our client base.

In order for our customers to qualify for HITECH funding, our products must meet various requirements for product certification under the HITECH regulations, and must enable our customers to achieve meaningful use , as such term is currently defined under the July 28, 2010 CMS Final Rule and under any future HITECH regulations and guidance that CMS may release. The CMS Final Rule provides for a phased approach to implementation of the meaningful use standards, with Stage 1 set forth in the rule and Stages 2 and 3 reserved for future rulemaking based upon the experiences with Stage 1. Given that CMS will release future regulations related to electronic health records, our industry is presented with a challenge in preparing for compliance. Similarly, our ability to achieve product certification by CCHIT and/or other regulatory bodies, and the length, if any, of additional related development and other efforts required to meet meaningful use standards could materially impact our ability to maximize the market opportunity. All of our market-facing EHR solutions have been certified 2011/2012 compliant by an ONC-ATCB, in accordance with the applicable provider or hospital certification criteria adopted by the Secretary of Health and Human Services. The 2011/2012 criteria support the Stage 1 meaningful use measures required to qualify eligible providers and hospitals for funding under HITECH. Currently, given the maturity of our products, management does not believe the incremental development effort, if any, required for our acute care and ambulatory EHRs to continue to meet the evolving meaningful use standards will be significant. Management has made product development a strategic focus, with gross research and development funding expected to continue to approximate 10% of revenues in the foreseeable future.

The market for acute care solutions is highly competitive. Sales cycles can occur over an extended period of time and require hospitals to secure external funding to finance their purchases of new clinical information

Table of Contents

systems. Several companies that we compete with are privately held which can provide certain advantages in capturing new client relationships. In addition, the market has increasingly moved toward adoption of integrated solutions that connect various venues of care including hospitals, physician offices, clinics, laboratories, post-acute facilities and other care delivery settings. The merger of Allscripts and Eclipsys responded to these emerging market dynamics by providing a full complement of solutions across the community of care. However other vendors may be better known or be perceived as a more integrated solutions provider currently. We have made progress on our integration plans, demonstrating the future direction for integrated solutions as well as current efforts that illustrate interoperability in common client settings. However, it will take more time and resources to finalize the product integration to meet current and evolving market demand for such solutions.

In addition, implementation of clinical systems in hospitals is a highly complex undertaking and can take longer to complete than originally planned. While we believe we have established ourselves as a leading provider of computerized physician order entry and related solutions, the complexities of individual health systems, local health care environments, native IT environments and other factors can extend implementation times and result in delays.

Management believes that to date the HITECH program has resulted in additional related new orders for all of our EHR products. Large physician groups will continue to purchase EHR technology; however, the number of very large practices who have not yet acquired such technology is decreasing. Such practices may choose to replace older EHR technology in the future as adoption increases and meaningful use requirements and business realities dictate updates, upgrades and additional features and functionality.

We believe small and medium size physician offices are increasingly adopting technology driven by a variety of factors including a desire to maximize federal incentive payments, align with local hospitals, consolidate with other practices and other drivers. Additionally, we have seen greater demand in small physician offices for subscription based (SaaS) arrangements as opposed to pure licensing arrangements, which reflects a motivation to reduce capital outlays. This shift to subscription from license (which is the manner in which we have traditionally sold our Professional offering) will result in recurring revenue over a longer period of time than we have achieved historically, as opposed to revenue recognized on license fees. Second, these offices typically require less time to implement and train than larger offices, so the need to plan implementations well in advance is not as acute as in larger physician organizations.

We have also seen an evolution of buying decisions toward an increase in local community-based buying activity whereby individual hospitals, health systems and integrated delivery networks are subsidizing the purchase of EHR licenses or related services for their affiliated physicians in order to leverage buying power and take advantage of the Stimulus across their employed physician base. This activity has also resulted in a pull-through effect where smaller practices affiliated with the community hospital are also incentivized to participate so the subsidizing health system can expand connectivity within the local provider community and optimize its referral base. This pull-through effect has resulted in new orders for our Professional EHR and our MyWay offering. Management believes that the focus on new orders driven by the HITECH program and related to EHR and community-based activity will continue to expand as physicians seek to qualify for the HITECH incentives. The associated challenge we face is to successfully position and sell our products to the hospital, health system or integrated delivery network that is subsidizing its affiliated physicians.

The vast majority of our acute care and ambulatory customers continue to be focused on achieving meaningful use under HITECH. As a result, in 2012 much of our professional services deployment capacity will continue to focus on helping our customers upgrade to the most current release of our EHR products that are certified as meeting meaningful use requirements as well as implement any additional modules required to achieve meaningful use . Our professional services margins could be impacted as we supplement our staff with third party resources to help meet the demand. We expect this trend to continue into the near future as HITECH Stage 2 requirements are defined and customers react to such requirements.

Table of Contents

Although we believe that we have taken and continue to take the proper steps to take advantage of the opportunity presented by HITECH, given the effects the law is having on our customers, there can be no assurance that it will continue to result in significant new orders for us in the near term, and if it does, that we will have the capacity to meet the additional market demand in a timely fashion.

Allscripts today provides one of the most comprehensive solution offerings for healthcare organizations of every size and setting. By combining physician-office and post-acute care solutions with enterprise solutions for hospitals and health systems, the company offers a single platform of clinical, financial, connectivity and information solutions.

Given the unique breadth of our solutions portfolio and customer types, we are uniquely positioned to connect physicians, other care providers and patients across all health care provider settings including hospitals, small or large physician practices, post-acute care facilities, or in a home care setting. We are experiencing increasing success competing for net-new opportunities among community hospitals and health systems that are looking to one information technology vendor to provide a single, end-to-end solution across all points of care. We believe our leading market share in the ambulatory space, in particular, gives us a competitive advantage in this regard as hospitals and health systems increasingly seek to leverage the EHR to build referring relationships with independent physicians across the communities they serve.

Additionally, recently enacted public laws reforming the U.S. healthcare system may have an impact on our business. The Patient Protection and Affordable Care Act (H.R. 3590; Public Law 111-148) (PPACA) and The Health Care and Education and Reconciliation Act of 2010 (H.R. 4872) (the Reconciliation Act), which amends the PPACA (collectively the Health Reform Laws), were signed into law in March 2010. The Health Reform Laws contain various provisions which may impact the Company and the Company s customers. Some of these provisions may have a positive impact, by expanding the use of electronic health records in certain federal programs, for example, while others, such as reductions in reimbursement for certain types of providers, may have a negative impact due to fewer available resources. Increases in fraud and abuse penalties may also adversely affect participants in the health care sector, including the Company.

Cost of revenue for Allscripts clinical solutions segment consists primarily of salaries, bonuses and benefits of Allscripts billable professionals, third-party software costs, hardware costs, third-party transaction processing costs, amortization of acquired proprietary technology, depreciation and amortization and other direct engagement costs. Cost of revenue for Allscripts hospital solutions segment and health solutions segment consists primarily of salaries, bonuses and benefits of Allscripts billable professionals, third-party software costs, hardware costs, depreciation and amortization and other direct engagement costs. Cost of revenue for the prepackaged medications segment consists primarily of the cost of the medications, cost of salaries, bonuses and benefits for repackaging personnel, shipping costs, repackaging facility costs and other costs.

Selling, general and administrative expenses consist primarily of salaries, bonuses and benefits for management and support personnel, commissions, facilities costs, depreciation and amortization, general operating expenses, product solutions management expenses and selling and marketing expenses. Selling, general and administrative expenses for each segment consist of expenses directly related to that segment. In addition, selling, general and administrative expenses include certain services performed by Misys under the Shared Services Agreement and Transition Services Agreement. Refer to Note 17 in the Notes to our Consolidated Financial Statements for information regarding expenses incurred under the two agreements.

Research and development expenses consist primarily of salaries, bonuses and benefits, third party contractor costs and other costs directly related to development of new products and upgrading and enhancing existing products.

Amortization of intangibles consists of amortization of customer relationships, trade names and other intangibles acquired under purchase accounting related business combinations.

Table of Contents

Interest expense consists primarily of interest on our previously outstanding 3.50% Senior Convertible Debentures (the Debentures), interest on capital leases and interest expense on outstanding debt under credit facilities.

Interest income and other, net consists primarily of interest earned on cash and marketable securities, and realized gains on investments.

Recent Accounting Pronouncements

Refer to Note 1 in the Notes to our Consolidated Financial Statements for a description of new accounting pronouncements.

Critical Accounting Policies and Estimates

Management s Discussion and Analysis of Financial Condition and Results of Operations discusses our consolidated financial statements, which have been prepared in accordance with generally accepted accounting principles (GAAP) in the United States of America. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Management bases its estimates and judgments on historical experience and on various other factors that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. Management believes the following critical accounting policies, among others, affect its more significant judgments and estimates used in the preparation of its consolidated financial statements.

Revenue Recognition

Revenue represents the fair value of consideration received or receivable from clients for goods and services provided by the Company. Revenue from system sales includes software and related hardware. Revenue from professional services includes implementation, training and consulting services. Revenue from maintenance includes post contract customer support and maintenance services. Revenue from transaction processing and other includes electronic data interchange (EDI) services, Software-as-a-Service (SaaS) transactions, software hosting services, and outsourcing. For some clients, we host the software applications licensed from us remotely using our own or third party servers, which saves these clients the cost of procuring and maintaining hardware and related facilities. For other clients, we offer an outsourced solution in which we assume partial to total responsibility for a healthcare organization s information technology operations using our employees. Revenue from prepackaged medications includes the sale of medications and pharmaceutical products. Prepackaged medications revenue is only included in operating results during fiscal year 2009, as the related business was part of the 2008 Transactions in the second quarter of fiscal year 2009 and later disposed in the fourth quarter of fiscal year 2009.

Revenue from software licensing arrangements where the service element is not considered essential to the functionality of the other elements of the arrangement is recognized upon delivery of the software or as services are performed, provided persuasive evidence of an arrangement exists, fees are considered fixed or determinable, and collection of the receivable is probable. The revenue recognized for each separate element of a multiple-element software contract is based upon vendor-specific objective evidence of fair value, which is based upon the price the customer is required to pay when the element is sold separately or renewed. For arrangements in which vendor-specific objective evidence of fair value only exists for the undelivered elements, the delivered elements (software license revenues) are accounted for using the residual method.

Revenue from software licensing arrangements, where the service element is considered essential to the functionality of the other elements of the arrangement, is accounted for on an input basis under percentage of

Table of Contents

completion accounting using actual hours worked as a percentage of total expected hours required by the arrangement, provided that persuasive evidence of an arrangement exists, the fee is fixed or determinable and collection of the receivable is probable. Maintenance and support from these agreements is recognized over the term of the support agreement based on vendor-specific objective evidence of fair value of the maintenance revenue, which is based upon contractual renewal rates. For income statement presentation, consideration from agreements accounted for under percentage of completion accounting is allocated between software and services based on vendor specific evidence of our hourly services rate multiplied by the amount of hours performed with the residual amount allocated to software license fee.

Revenue from certain value-added reseller (VAR) relationships in which software is directly sold to VARs is recognized upon delivery of the software assuming all other revenue recognition criteria have been met. Revenue recognition is deferred until the software is delivered to the ultimate end user if the arrangement terms do not satisfy the criteria for revenue recognition upon delivery of the software to the VAR.

We also enter into multiple-element arrangements that may include a combination of various software-related and nonsoftware-related products and services. Management applies judgment to ensure appropriate accounting for multiple deliverables, including the allocation of arrangement consideration among multiple units of accounting, the determination of whether undelivered elements are essential to the functionality of delivered elements, and the timing of revenue recognition, among others. In such arrangements, we first allocate the total arrangement consideration based on a selling price hierarchy at the inception of the arrangement. The selling price for each element is based upon the following selling price hierarchy: vendor-specific objective evidence of fair value if available, third-party evidence of fair value if vendor-specific objective evidence of fair value is not available, or estimated selling price if neither vendor-specific objective evidence or third-party evidence of fair value is available (a description as to how we determine vendor-specific objective evidence of fair value, third-party evidence of fair value and estimated selling price is provided below). Upon allocation of consideration to the software elements as a whole and nonsoftware elements, we then further allocate consideration within the software group to the respective elements following higher-level, industry-specific guidance and our policies described above. After the arrangement consideration has been allocated to the elements, we account for each respective element in the arrangement as described above.

To determine the selling price in multiple-element arrangements, we establish vendor-specific objective evidence of fair value using the price charged for a deliverable when sold separately and contractual renewal rates for maintenance fees. For nonsoftware multiple element arrangements, third-party evidence of fair value is established by evaluating similar and interchangeable competitor products or services in standalone arrangements with similarly situated customers. If we are unable to determine the selling price because vendor-specific objective evidence or third-party evidence of fair value does not exist, we determine an estimated selling price by considering several external and internal factors including, but not limited to, pricing practices, margin objectives, competition, customer demand, internal costs and overall economic trends. The determination of an estimated selling price is made through consultation with and approval by our management, taking into consideration our go-to-market strategy. As our, or our competitors , pricing and go-to-market strategies evolve, we may modify our pricing practices in the future. These events could result in changes to our determination of vendor-specific objective evidence of fair value, third-party evidence of fair value and estimated selling price. Selling prices are analyzed on an annual basis or more frequently if we experience significant changes in our selling prices.

For those arrangements where the deliverables do not qualify as separate units of accounting, revenue recognition is evaluated for the combined deliverables as a single unit of accounting and generally the recognition pattern of the final deliverable will dictate the revenue recognition pattern for the single, combined unit of accounting. Changes in circumstances and customer data may affect management s analysis of separation criteria which may lead to an upward or downward adjustment to the amount of revenue recognized under the arrangement.

We assess whether fees are fixed or determinable at the time of sale and recognize revenues if all other revenue recognition requirements are met. Our payment arrangements with clients typically include milestone-based software license fee payments and payments based upon delivery for services and hardware.

Table of Contents

While most of our arrangements include short-term payment terms, we periodically provide extended payment terms to clients from the date of contract signing. We do not recognize revenue under extended payment term arrangements until such payments become due. In certain circumstances, where all other revenue recognition criteria have been met, we occasionally offer discounts to clients with extended payment terms, in order to accelerate the timing of when payments are made. Changes to extended payment term arrangements have not had a material impact on our consolidated results of operations.

Maintenance fees are recognized ratably over the period of the contract based on vendor specific objective evidence of fair value based upon contractual renewal rates. Revenue from EDI services is recognized as services are provided and is determined based on the volume of transactions processed. Prior to the sale of the Company s prepackaged medications business in March 2009, revenue from the sale of prepackaged medications, net of provisions for estimated returns, was recognized upon shipment of the pharmaceutical products, the point at which the customer took ownership and assumed risk of loss, when no performance obligations remain and collection of the receivable was probable.

Revenue is recognized net of any taxes collected from customers and subsequently remitted to governmental authorities. We record as revenue any amounts billed to customers for shipping and handling costs and record as cost of revenue the actual shipping costs incurred.

The Company records reimbursements for out-of-pocket expenses incurred as professional services revenue in the statement of operations.

Allowance for Doubtful Accounts Receivable

We rely on estimates to determine our bad debt expense and the adequacy of our allowance for doubtful accounts. These estimates are based on our historical experience and the industry in which we operate. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances and related bad debt expense may be required.

Business Combinations

Goodwill as of the acquisition date is measured as the excess of consideration transferred and the net of the acquisition date fair values of the assets acquired and the liabilities assumed. While we use our best estimates and assumptions as a part of the purchase price allocation process to accurately value assets acquired, including intangible assets, and liabilities assumed at the acquisition date, our estimates are inherently uncertain and subject to refinement. As a result, during the measurement period, which may be up to one year from the acquisition date, we record adjustments to the assets acquired and liabilities assumed, with the corresponding offset to goodwill. Upon the conclusion of the measurement period or final determination of the values of assets acquired or liabilities assumed, whichever comes first, any subsequent adjustments are recorded to our consolidated statements of operations.

Goodwill and Intangible Assets

We evaluate the value of intangible assets based upon the present value of the future economic benefits expected to be derived from the assets. We assess the impairment of the identifiable intangibles and goodwill annually, or more frequently if events or changes in circumstances indicate that the asset might be impaired. If we determine that the value of the intangible assets and goodwill may not be recoverable from future cash flows, a write-down of the value of the asset may be required.

We estimate the useful lives of our intangible assets and amortize the value over that estimated life. If the actual useful life is shorter than our estimated useful life, we will amortize the remaining book value over the remaining useful life or the asset may be deemed to be impaired and, accordingly, a write-down of the value of the asset may be required.

Table of Contents

During the three months ended June 30, 2011, we voluntarily changed the date of our annual impairment test for goodwill and indefinite lived intangible assets from May 31 to the first day of the fiscal fourth quarter. This change is preferable under the circumstances as it aligns the timing of the annual goodwill impairment test with our strategic planning and budgeting process, which will allow management to utilize the updated strategic business plans that result from the budget process in the discounted cash flow analyses that it uses to estimate the fair value of our reporting units. The change did not delay, accelerate or avoid an impairment charge. This change is not applied retrospectively as it is impracticable to do so because retrospective application would require the application of significant estimates and assumptions with the use of hindsight. Accordingly, the change will be applied prospectively. We re-performed step one of the annual goodwill impairment test as of October 1, 2011 and no indicators of impairment were identified.

For each reporting unit fair value substantially exceeded its carrying value and no indicators of impairment were identified as a result of the annual impairment test.

Software Capitalization

The carrying value of capitalized software is dependent upon the ability to recover its value through future revenue from the sale of the software. If we determine in the future that the value of the capitalized software could not be recovered, a write-down of the value of the capitalized software to its recoverable value may be required.

We estimate the useful life of our capitalized software and amortize the value over that estimated life. If the actual useful life is shorter than our estimated useful life, we will amortize the remaining book value over the remaining useful life or the asset may be deemed to be impaired and, accordingly, a write-down of the value of the asset may be required.

Income Taxes

We account for income taxes in accordance with authoritative accounting guidance which establishes financial accounting and reporting standards for the effect of income taxes. The objectives of accounting for income taxes are to recognize the amount of taxes payable or refundable for the current year and deferred tax liabilities and assets for the future tax consequences of events that have been recognized in an entity s financial statements or tax returns. Judgment is required in addressing the future tax consequences of events that have been recognized in our consolidated financial statements or tax returns.

In addition, we are subject to the continuous examination of our income tax returns by the Internal Revenue Service and other tax authorities. A change in the assessment of the outcomes of such matters could materially impact our consolidated financial statements. The calculation of tax liabilities involves dealing with uncertainties in the application of complex tax regulations. In accordance with authoritative accounting guidance, we recognize liabilities for anticipated tax audit issues based on our estimate of whether, and the extent to which, additional taxes may be required. If we ultimately determine that payment of these amounts is unnecessary, then we reverse the liability and recognize a tax benefit during the period in which we determine that the liability is no longer necessary. We also recognize tax benefits to the extent that it is more likely than not that our positions will be sustained if challenged by the taxing authorities. To the extent we prevail in matters for which liabilities have been established, or are required to pay amounts in excess of our liabilities, our effective tax rate in a given period may be materially affected. An unfavorable tax settlement would require cash payments and may result in an increase in our effective tax rate in the year of resolution. A favorable tax settlement would be recognized as a reduction in our effective tax rate in the year of resolution. We report interest and penalties related to uncertain income tax positions in the provision for income taxes line of our consolidated statements of operations.

Refer to Note 1 Basis of Presentation and Significant Accounting Policies in the Notes to our Consolidated Financial Statements for further discussions of our accounting policies.

Table of Contents

Overview of Consolidated Results

(Dollar amounts in thousands)	Year Ended December 31, 2011	Year Ended December 31, 2010	% Change	Seven Months Ended December 31, 2010	Seven Months Ended December 31, 2009	% Change	Year Ended May 31, 2010	Year Ended May 31, 2009	% Change
Revenue:									
System sales	$242,869	$193,511	25.5%	$113,117	$74,204	52.4%	$154,597	$98,469	57.0%
Professional services	250,348	130,980	91.1%	93,875	38,335	144.9%	75,439	51,827	45.6%
Maintenance	424,036	299,741	41.5%	191,502	140,263	36.5%	248,501	196,165	26.7%
Transaction processing and other	526,824	310,104	69.9%	214,815	130,677	64.4%	225,965	187,557	20.5%
Total software and related services	1,444,077	934,336	54.6%	613,309	383,479	59.9%	704,502	534,018	31.9%
Prepackaged medications	0	0	NM	0	0	NM	0	14,421	NM
Total revenue	1,444,077	934,336	54.6%	613,309	383,479	59.9%	704,502	548,439	28.5%
Cost of revenue:									
System sales	144,139	104,946	37.3%	63,392	43,516	45.7%	85,070	52,039	63.5%
Professional services	210,614	113,500	85.6%	81,572	35,414	130.3%	66,561	51,327	29.7%
Maintenance	135,570	102,501	32.3%	67,463	47,588	41.8%	82,348	71,913	14.5%
Transaction processing and other	288,189	134,240	114.7%	102,713	47,094	118.1%	81,679	69,479	17.6%
Total software and related services	778,512	455,187	71.0%	315,140	173,612	81.5%	315,658	244,758	29.0%
Prepackaged medications	0	0	NM	0	0	NM	0	11,530	NM
Total cost of revenue	778,512	455,187	71.0%	315,140	173,612	81.5%	315,658	256,288	23.2%
Gross profit	665,565	479,149	38.9%	298,169	209,867	42.1%	388,844	292,151	33.1%
% of Revenue	46.1%	51.3%		48.6%	54.7%		55.2%	53.3%	
Selling, general and administrative expenses	387,571	332,413	16.6%	232,788	126,569	83.9%	224,995	199,902	12.6%
Research and development	104,106	65,419	59.1%	43,261	27,238	58.8%	49,206	39,431	24.8%
Amortization of intangible assets	37,344	20,381	83.2%	16,235	5,914	174.5%	10,060	6,884	46.1%
Income from operations	136,544	60,936	124.1%	5,885	50,146	(88.3%)	104,583	45,934	127.7%
Interest expense	(20,750)	(10,992)	88.8%	(9,687)	(1,302)	644.0%	(1,993)	(2,162)	(7.8%)
Interest income and other, net	1,685	1,549	8.8%	843	240	251.3%	946	626	51.1%
Income (loss) before income taxes	117,479	51,493	128.1%	(2,959)	49,084	(106.0%)	103,536	44,398	133.2%
Provision for income taxes	(43,870)	(24,676)	77.8%	(2,606)	(18,596)	(86.0%)	(40,666)	(18,376)	121.3%
Effective tax rate	37.3%	47.9%		(88.1%)	37.9%		39.3%	41.4%	
Net income (loss)	$73,609	$26,817	174.5%	($5,565)	$30,488	(118.3%)	$62,870	$26,022	141.6%

NM not meaningful

Given the level of integration of the operations and reporting of legacy Allscripts and legacy MHS following the 2008 Transactions, management does not view or manage the business on a legacy business basis. Accordingly, it is not possible or meaningful in every case to quantify the impacts of the inclusion of legacy Allscripts on our financial results on a year-over-year basis within our overview of consolidated results and segment results. The fiscal year ended May 31, 2010 includes the full-year results of both legacy MHS and legacy Allscripts businesses. The fiscal year ended May 31, 2009 includes the full-year results of legacy MHS and the results of operations of legacy Allscripts subsequent to the closing of the 2008 Transactions, October 10, 2008.

Table of Contents

Year Ended December 31, 2011 Compared to Year Ended December 31, 2010

The year ended December 31, 2011 includes the full-year results of Eclipsys, and the year ended December 31, 2010 includes the results of Eclipsys from the date of the merger, August 24, 2010.

Revenue

The increase in total revenue during 2011 is primarily attributable to inclusion of the full-year results of Eclipsys. Also contributing to the increase is higher professional services revenue that was driven by an increase in professional services headcount which increased our ability to provide more billable services. We increased headcount primarily in response to the demand associated with meaningful use upgrade services. Maintenance revenue and transaction processing revenue both increased primarily related to growth in our customer base. Partially offsetting the increase in maintenance revenue is a decrease in hardware maintenance revenue. SaaS revenues are included in transaction processing and other and contributed $17 million of the increase in revenue compared to the year ended December 31, 2010. Partially offsetting the increase in total revenue for the year ended December 31, 2011 is a decrease in system hardware revenue as our system sales shifted to smaller physician practices which typically require less robust hardware solutions.

Gross Profit

In addition to the full-year results of Eclipsys, gross profit was also impacted by an increase in software maintenance revenue attributable to an increase in our customer base which was offset by the decrease in system hardware revenues discussed above combined with an increase in the amortization of software development costs. Additionally, we experienced an increase in professional services revenue that was offset by an increase in costs due to the increased use of third party resources to assist us in meeting demand attributable to meaningful use upgrade services. Gross profit as a percent of revenue declined compared to the prior period due primarily to the increases in amortization of software development costs, professional services costs and additional transaction processing related costs. These increases were partially offset by fewer lower margin hardware sales during the current year as discussed above.

Operating Income

Operating income increased in 2011 primarily due to inclusion of the full-year results of Eclipsys, a decrease in expenses incurred relating to the Eclipsys Merger and other integration-related costs totaling $16 million as compared to the prior period, and a decrease in headcount-related expenses. Partially offsetting these decreases is an increase in stock compensation expense and an increase in legal expenses related to general legal matters, including negotiating transactions with customers and addressing claims asserted against the Company. Research and development expenses increased primarily due to a decrease in the capitalization of software development costs compared to the prior period that was partially offset by a decrease in headcount-related expenses.

The Eclipsys income from operations for the years ended December 31, 2011 and 2010 includes a $20 million and $27 million, respectively, deferred revenue adjustment related to the Eclipsys Merger that negatively impacts revenue, amortization of intangibles acquired in the Eclipsys Merger totaling $46 million and $17 million, respectively, and reflects capitalized software developments costs of $29 million and $8 million, respectively.

Table of Contents

Seven Months Ended December 31, 2010 Compared to Seven Months Ended December 31, 2009

Revenue

Revenue for the seven months ended December 31, 2010 includes the results of Eclipsys from the date of the merger, August 24, 2010. All software and related services revenue categories reflect increases from the prior year comparable period. Excluding the impact of Eclipsys revenue totaling $175 million, as shown below in the Hospital Solutions segment, from August 24, 2010 through December 31, 2010, software and related services revenue for the seven months ended December 31, 2010 consists of the following:

	Seven Months Ended December 31,		
(Dollar amounts in thousands)	**2010**	**2009**	**% Change**
Revenue:			
System sales	$87,107	$74,204	17.4%
Professional services	58,646	38,335	53.0%
Maintenance	152,131	140,263	8.5%
Transaction processing and other	140,748	130,677	7.7%
Total revenue	$438,632	$383,479	14.4%

Excluding the revenues contributed by Eclipsys during the seven months ended December 31, 2010, system sales increased during the seven months ended December 31, 2010 as a result of an increase in customer orders compared to the seven months ended December 31, 2009. Professional services revenue increased primarily from an increase in professional services headcount which increased our ability to provide more billable services. The increase in customer orders also contributed to the increase in professional services revenue. Maintenance revenue and transaction processing revenue both increased primarily related to growth in our customer base and annual maintenance fee increases under existing contracts.

Gross Profit

Consolidated gross profit for the seven months ended December 31, 2010 includes the results of Eclipsys from the date of the merger, August 24, 2010. Excluding the impact of Eclipsys gross profit totaling $66 million for the period August 24, 2010 through December 31, 2010, software and related services gross profit for the seven months ended December 31, 2010 consists of the following:

	Seven Months Ended December 31,		
(Dollar amounts in thousands)	**2010**	**2009**	**% Change**
Total cost of revenue	$206,640	$173,612	19.0%
Gross profit	$231,992	$209,867	10.5%
% of Revenue	52.9%	54.7%	

Excluding the impact of gross profit contributed by Eclipsys, the increase in gross profit is attributable to higher system sales that were driven by an increase in software orders during the seven months ended December 31, 2010 compared to the seven months ended December 31, 2009, an increase in professional services revenue due to the increased capacity to deliver billable services and an increase in maintenance revenue due to growth in our customer base and annual maintenance fee increases under existing contracts. Gross profit as a percent of revenue declined slightly compared to the prior year comparable period due primarily to an increase in the amortization of software development costs of $3 million and additional transaction processing related costs incurred as we increased headcount and improved our infrastructure in response to increased demand for our SaaS solutions.

Table of Contents

Operating Income

Consolidated operating income for the seven months ended December 31, 2010 includes the results of Eclipsys from the date of the merger, August 24, 2010. Excluding the impact of Eclipsys loss from operations totaling $16 million for the period August 24, 2010 through December 31, 2010, operating income for the seven months ended December 31, 2010 consists of the following:

	Seven Months Ended December 31,		
(Dollar amounts in thousands)	**2010**	**2009**	**% Change**
Income from operations	$21,933	$50,146	(56.3%)

Excluding the impact of operating loss by Eclipsys, the decrease in operating income is primarily due to increases in selling, general and administrative expenses and research and development expenses. Selling, general and administrative expenses increased as a result of an increase in headcount and expenses incurred related to the Eclipsys Merger, Coniston Transactions, and other integration-related costs totaling $43 million. Research and development expenses increased as a result of increased headcount. The increase in expenses was partially offset by the increase in gross profit discussed above.

The Eclipsys loss from operations is driven by a $27 million deferred revenue adjustment related to the Eclipsys Merger that negatively impacts revenue, expenses incurred related to the Eclipsys Merger and other integration-related costs totaling $15 million and amortization of intangibles acquired in the Eclipsys Merger totaling $17 million.

Year Ended May 31, 2010 Compared to Year Ended May 31, 2009

Revenue

Revenue increased from the prior year primarily due to the inclusion of full-year results for legacy Allscripts in the fiscal year ended May 31, 2010 as compared to the prior year and an increase in customer orders. All revenue categories reflect increases from the prior year with the exception of prepackaged medications revenue related to the Medications Services segment that was sold during the fourth quarter of fiscal year 2009. System sales and maintenance revenue reflect the most significant increases in revenue. System sales increased as a result of an increase in customer orders compared to the prior year. The increase in maintenance revenue compared to the prior year reflects an overall increase in the customer base as a result of the 2008 Transactions along with continued growth in the customer base from new customer orders.

Gross Profit

Gross profit increased during the year ended May 31, 2010 compared to the prior year due to the inclusion of full-year results for legacy Allscripts and an increase in revenue related to increased customer orders. Excluding the impact of our prepackaged medications business which was sold during the year ended May 31, 2009, gross profit as a percentage of revenue increased compared to the prior year due to improved utilization of professional services resources as well as an improvement in maintenance margins due to better cost management and a slight reduction in headcount. Additionally, a more favorable system sales revenue mix was realized in fiscal year 2010 compared to prior year with more revenue being contributed from software licenses and less from lower margin hardware sales. This improvement was offset by increased amortization of software development costs.

Operating Income

Operating income increased from the prior year primarily due to the inclusion of full-year results for legacy Allscripts in the fiscal year ended May 31, 2010 as compared to the prior year and an improvement in gross profit. The increase in 2010 is partially offset by increased costs related to an increase in research and development headcount and the Eclipsys Merger and the Coniston Transactions. The increase in research and

Table of Contents

development costs is partially offset by an increase in capitalized software development costs. Transaction-related fees and expenses, including legal, investment banking and accounting fees, incurred in connection with announced transactions as well as severance, integration, and certain legal and related settlement amounts totaled approximately $14 million during the year ended May 31, 2010.

Segment Operations

Overview of Segment Results

	Year Ended December 31,			Seven Months Ended December 31,			Year Ended May 31,		
(Dollar amounts in thousands)	**2011**	**2010**	**% Change**	**2010**	**2009**	**% Change**	**2010**	**2009**	**% Change**
Revenue									
Clinical solutions	$686,600	$641,302	7.1%	$369,312	$320,883	15.1%	$593,061	$457,402	29.7%
Hospital solutions	628,314	174,677	NM	174,677	0	NM	0	0	NM
Health solutions	129,163	118,357	9.1%	69,320	62,596	10.7%	111,441	76,616	45.5%
Prepackaged medications	0	0	NM	0	0	NM	0	14,421	NM
Total revenue	$1,444,077	$934,336	54.6%	$613,309	$383,479	59.9%	$704,502	$548,439	28.5%
Income from operations									
Clinical solutions	$168,377	$168,652	(0.2%)	$87,466	$82,569	5.9%	$164,492	$118,552	38.8%
Hospital solutions	138,440	24,236	NM	24,236	0	NM	0	0	NM
Health solutions	70,975	61,388	15.6%	35,590	31,324	13.6%	58,853	30,713	91.6%
Prepackaged medications	0	0	NM	0	0	NM	0	1,121	NM
Unallocated corporate expenses	(241,248)	(193,340)	24.8%	(141,407)	(63,747)	121.8%	(118,762)	(104,452)	13.7%
Total income from operations	$136,544	$60,936	124.1%	$5,885	$50,146	(88.3%)	$104,583	$45,934	127.7%

Clinical Solutions

	Year Ended December 31,			Seven Months Ended December 31,			Year Ended May 31,		
(Dollar amounts in thousands)	**2011**	**2010**	**% Change**	**2010**	**2009**	**% Change**	**2010**	**2009**	**% Change**
Revenue:									
System sales	$134,698	$147,911	(8.9%)	$76,565	$62,444	22.6%	$133,645	$81,867	63.2%
Professional services	119,555	81,550	46.6%	50,079	31,350	59.7%	62,834	43,430	44.7%
Maintenance	234,613	224,597	4.5%	131,509	120,670	9.0%	213,756	169,290	26.3%
Transaction processing and other	197,734	187,244	5.6%	111,159	106,419	4.5%	182,826	162,815	12.3%
Total revenue	686,600	641,302	7.1%	369,312	320,883	15.1%	593,061	457,402	29.7%
Total cost of revenue	372,610	314,323	18.5%	187,413	155,879	20.2%	284,695	222,437	28.0%
Gross profit	313,990	326,979	(4.0%)	181,899	165,004	10.2%	308,366	234,965	31.2%
% of Revenue	45.7%	51.0%		49.3%	51.4%		52.0%	51.4%	
Selling, general and administrative expenses	95,640	112,709	(15.1%)	67,168	59,735	12.4%	103,009	88,634	16.2%
Research and development	49,973	45,618	9.5%	27,265	22,700	20.1%	40,865	27,779	47.1%
Income from operations	$168,377	$168,652	(0.2%)	$87,466	$82,569	5.9%	$164,492	$118,552	38.8%

59

Table of Contents

Year Ended December 31, 2011 Compared to Year Ended December 31, 2010

Revenue

Clinical solutions revenue increased during the year ended December 31, 2011 due to higher professional services revenue that was driven by an increase in professional services headcount which increased our ability to provide more billable services. We increased headcount primarily in response to the demand associated with meaningful use upgrade services. Also, maintenance revenue and transaction processing revenue both increased primarily related to growth in our customer base. Partially offsetting the increase in maintenance revenue is a $4 million decrease in hardware maintenance revenue. SaaS revenues are included in transaction processing and other and contributed $10 million of the increase in revenue compared to the prior period. Partially offsetting the current year increase in total revenue is a decrease in system sales compared to the prior period primarily due to a $10 million decrease in system hardware revenue as our system sales shifted to smaller physician practices which typically require less robust hardware solutions.

Gross Profit

Clinical solutions gross profit decreased during the current year primarily due to the decrease in hardware revenues discussed above combined with a $10 million increase in the amortization of software development costs and an increase in professional services cost of revenue attributable to the increased use of third party resources to assist us in meeting demand attributable to meaningful use upgrade services. The increase in amortization of software development costs is primarily attributable to the increase in capitalized costs related to development efforts associated with initial meaningful use requirements. The increase in professional services cost offset an increase in professional services revenue. Partially offsetting these changes was an increase in maintenance primarily related to growth in our customer base. Gross profit as a percent of revenue declined compared to the prior year due primarily to the increases in amortization of software development costs, the increase in professional services costs described above and additional transaction processing related costs incurred as we increased headcount and improved our infrastructure in response to increased demand for our SaaS and hosting solutions.

Selling, General and Administrative

Clinical solutions selling, general and administrative expenses declined during the current year primarily due to lower headcount-related costs and marketing expenses.

Research and Development

Clinical solutions research and development costs increased during the year ended December 31, 2011 primarily due to a $7 million decrease in the capitalization of software development costs which was partially offset by a decrease in headcount-related costs due to fewer external research and development resources required to achieve our development objectives. Capitalization of software development costs is higher in the prior year as we increased development efforts to address initial meaningful use requirements.

Seven Months Ended December 31, 2010 Compared to Seven Months Ended December 31, 2009

Revenue

Clinical solutions revenue increased during the seven months ended December 31, 2010 primarily due to an increase in customer orders that drove increases in all revenue categories. The increase in professional services was also driven by an increase in professional services headcount which provided additional capacity to deliver more billable services. Additionally, maintenance and transaction processing revenues increased as a result of continued growth in the clinical solutions customer base.

Table of Contents

Gross Profit

Clinical solutions gross profit increased during the seven month period ended December 31, 2010 as compared to the prior year comparable period primarily due to an increase in system sales that was driven by an increase in software orders and an increase in maintenance revenue due to growth in our customer base. Gross profit as a percentage of revenue for the seven months ended December 31, 2010 decreased compared to the prior year comparable period primarily due to a lower gross profit percentage realized by transaction processing. We incurred additional transaction processing related costs as we increased headcount and improved our infrastructure in response to increased demand for our SaaS solutions.

Selling, General and Administrative

The increase in clinical solutions selling, general and administrative expenses during the seven months ended December 31, 2010 is attributable to higher commission expense which was driven by an increase in customer orders and higher overall revenues. This increase was partially offset by a decrease in stock compensation expense as compared to the prior year comparable period.

Research and Development

Clinical solutions research and development costs increased during the seven months ended December 31, 2010 primarily due to an increase in costs related to a higher number of internal and external research and development resources required to achieve new features and functionality and meet the meaningful use guidelines stipulated by healthcare legislation. Increased costs in the current period were partially offset by an increase in the capitalization of software development costs.

Year Ended May 31, 2010 Compared to Year Ended May 31, 2009

Revenue

Clinical solutions revenue increased during the year ended May 31, 2010 primarily due to the inclusion of full-year results for legacy Allscripts in the fiscal year ended May 31, 2010 as compared to the prior year and an increase in customer orders that drove increases in all revenue categories. Additionally, maintenance revenues increased as a result of continued growth in the clinical solutions customer base.

Gross Profit

Clinical solutions gross profit increased in fiscal 2010 as compared to the prior year primarily due to the inclusion of full-year results for legacy Allscripts and an increase in revenue related to increased customer orders. Gross profit as a percentage of revenue increased slightly during the year ended May 31, 2010 compared to the prior year primarily attributable to improved utilization of professional services resources as well as an improvement in maintenance margins due to better cost management. Additionally, a more favorable system sales revenue mix was realized in fiscal year 2010 with more revenue being contributed from software licenses and less from lower margin hardware sales. This improvement was offset by increased amortization of software development costs.

Selling, General and Administrative

The increase in selling, general and administrative costs during the year ended May 31, 2010 was primarily a result of the inclusion of full-year results for legacy Allscripts in the year ended May 31, 2010 as compared to the prior year. Additionally, increases in stock-based compensation and marketing contributed to the overall increase in selling, general and administrative expenses.

Table of Contents

Research and Development

Clinical solutions research and development costs increased during the year ended May 31, 2010 primarily due to costs related to an increase in headcount and increased maintenance efforts related to clinical solutions software applications. These increases were partially offset by increased capitalization of software development costs compared to the prior year.

Hospital Solutions

(Dollar amounts in thousands)	Year Ended December 31, 2011	August 24, 2010 Through December 31, 2010
Revenue:		
System sales	$88,849	$26,010
Professional services	115,421	35,229
Maintenance	151,002	39,371
Transaction processing and other	273,042	74,067
Total revenue	628,314	174,677
Total cost of revenue	370,262	108,500
Gross profit	258,052	66,177
% of Revenue	41.1%	37.9%
Selling, general and administrative expenses	73,048	29,817
Research and development	46,564	12,124
Income from operations	$138,440	$24,236

The hospital solutions segment reflects the operations, subsequent to the completion of our merger with Eclipsys Corporation on August 24, 2010, of our acute care hospital solutions.

System sales and professional services are revenue categories driven by client orders and the mix of such orders (i.e., software, hardware, professional services, etc.). Maintenance and transaction processing and other revenues are also driven by client orders; however, these revenue categories are more recurring in nature and include offerings such as remote hosting and outsourcing.

Total revenue is negatively impacted by the amortization of a deferred revenue adjustment related to the Eclipsys Merger totaling $20 million and $27 million for the year ended December 31, 2011 and 2010, respectively.

Gross profit is also negatively impacted by the deferred revenue adjustment discussed above in addition to amortization of intangibles acquired in the Eclipsys Merger totaling $15 million and $6 million for the years ended December 31, 2011 and 2010, respectively.

Selling, general and administrative expenses, and research and development expenses, reflect recurring costs of the hospital solutions segment, and are net of capitalized software development costs of $29 million and $8 million for the year ended December 31, 2011 and the prior period amount, respectively.

Table of Contents

Health Solutions

(Dollar amounts in thousands)	Year Ended December 31, 2011	2010	% Change	Seven Months Ended December 31, 2010	2009	% Change	Year Ended May 31, 2010	2009	% Change
Revenue:									
System sales	$19,322	$19,590	(1.4%)	$10,542	$11,760	(10.4%)	$20,952	$16,602	26.2%
Professional services	15,372	14,201	8.2%	8,567	6,985	22.6%	12,605	8,397	50.1%
Maintenance	38,421	35,773	7.4%	20,622	19,593	5.3%	34,745	26,875	29.3%
Transaction processing and other	56,048	48,793	14.9%	29,589	24,258	22.0%	43,139	24,742	74.4%
Total revenue	129,163	118,357	9.1%	69,320	62,596	10.7%	111,441	76,616	45.5%
Total cost of revenue	35,640	32,364	10.1%	19,227	17,732	8.4%	30,963	22,321	38.7%
Gross profit	93,523	85,993	8.8%	50,093	44,864	11.7%	80,478	54,295	48.2%
% of Revenue	72.4%	72.7%		72.3%	71.7%		72.2%	70.9%	
Selling, general and administrative expenses	14,979	16,928	(11.5%)	10,632	9,002	18.1%	13,284	16,569	(19.8%)
Research and development	7,569	7,677	(1.4%)	3,871	4,538	(14.7%)	8,341	7,013	18.9%
Income from operations	$70,975	$61,388	15.6%	$35,590	$31,324	13.6%	$58,853	$30,713	91.6%

Year Ended December 31, 2011 Compared to Year Ended December 31, 2010

Revenue

Health solutions revenue increased during the year ended December 31, 2011 primarily as a result of an increase in transaction processing and other revenue driven by increased demand for our SaaS solutions. System sales were flat as our revenue mix continues to shift more to SaaS solutions.

Gross Profit

Health solutions gross profit during the year ended December 31, 2011 increased compared to the prior year due to increases in maintenance and transaction processing and other revenue which was partially offset by an increase in amortization of software development costs and other software-related costs. Gross profit as a percentage of revenue remained in line with the prior period as the increases in amortization of software development costs and other software-related costs were partially offset by lower maintenance-related costs.

Selling, General and Administrative

Health solutions selling, general and administrative expenses for the year ended December 31, 2011 decreased due to lower headcount-related expenses.

Research and Development

Health solutions research and development costs during the year ended December 31, 2011 were in line with the prior period amount.

Seven Months Ended December 31, 2010 Compared to Seven Months Ended December 31, 2009

Revenue

The health solutions revenue increase during the seven months ended December 31, 2010 is primarily attributable to increases in professional services and transaction processing which were driven by an increase in

Table of Contents

health solutions orders compared to the seven months ended December 31, 2009. Transaction processing primarily consists of software sold as a service. Maintenance revenues also increased due to growth in our customer base and annual maintenance fee increases under existing contracts. These increases were partially offset by a decrease in system sales. While customer orders for systems sales increased during the seven months ended December 31, 2010, the increase in customer orders did not result in an increase in revenue due to the timing of related implementation services.

Gross Profit

Health solutions gross profit increased during the seven months ended December 31, 2010 as compared to the prior year comparable period primarily due to the increases in professional services revenue and transaction processing revenue related to increased customer orders. Gross profit as a percentage of revenue for the seven months ended December 31, 2010 increased over the comparable prior year period due to improved utilization of professional services personnel and an improved revenue mix driven by higher margin transaction processing revenue.

Selling, General and Administrative

The increase in health solutions selling, general and administrative expenses during the seven months ended December 31, 2010 is attributable to higher commission expense which was driven by an increase in customer orders, and an increase in stock compensation expense as compared to the prior year comparable period.

Research and Development

Health solutions research and development costs decreased in the seven months ended December 31, 2010 primarily due to an increase in capitalization of software development costs relating to increased feature and functionality development efforts that commenced in 2010. This increase was partially offset by an increase in costs related to a higher number of internal and external research and development resources compared to the prior year comparable period.

Year Ended May 31, 2010 Compared to Year Ended May 31, 2009

Revenue

Health solutions revenue increased during the year ended May 31, 2010 primarily due to the inclusion of full-year results for legacy Allscripts in the fiscal year ended May 31, 2010 as compared to the prior year and an increase in customer orders.

Gross Profit

The health solutions gross profit increase during the year ended May 31, 2010 is primarily due to the inclusion of full-year results for legacy Allscripts. Gross profit as a percentage of revenue increased slightly during fiscal year 2010 compared to the prior year. The slight increase is primarily attributable to improved utilization of professional services resources. Additionally, a more favorable system sales revenue mix was realized during fiscal year 2010 with more revenue being contributed from software licenses and less from lower margin hardware sales. This improvement was partially offset by increased amortization of software development costs.

Selling, General and Administrative

The decline in health solutions selling, general and administrative expenses during the year ended May 31, 2010 was primarily a result of lower stock-based compensation and marketing expenses.

Table of Contents

Research and Development

The increase in health solutions research and development expenses was primarily due to the inclusion of full-year results for legacy Allscripts in the fiscal year ended May 31, 2010 as compared to the prior year and an increase in headcount. Partially offsetting these increases was an increase in capitalized software development costs.

Prepackaged Medications

	Year Ended May 31, 2009
Total prepackaged medications revenue	$14,421
Total prepackaged medications cost of revenue	11,530
Gross profit	2,891
Selling general and administrative expenses	1,770
Income from operations	$1,121

Prepackaged medications revenue is only included in operating results during the year ended May 31, 2009, as the related business was acquired as part of the 2008 Transactions in the second quarter of fiscal year 2009 and on March 16, 2009, Allscripts completed the sale of its Medications Services business pursuant to the Asset Purchase Agreement (the Meds Agreement) with A-S Medication Solutions LLC (A-S).

Unallocated Corporate Expenses

	Year Ended December 31,			Seven Months Ended December 31,			Year Ended May 31,		
(Dollar amounts in thousands)	2011	2010	% Change	2010	2009	% Change	2010	2009	% Change
Unallocated corporate expenses									
Selling, general and administrative expenses	($203,904)	($172,959)	17.9%	($125,172)	($57,833)	116.4%	($108,702)	($97,568)	11.4%
Amortization of intangible assets	(37,344)	(20,381)	83.2%	(16,235)	(5,914)	174.5%	(10,060)	(6,884)	46.1%
Total unallocated corporate expenses included in income from operations	($241,248)	($193,340)	24.8%	($141,407)	($63,747)	121.8%	($118,762)	($104,452)	13.7%

Year Ended December 31, 2011 Compared to Year Ended December 31, 2010

Unallocated corporate selling, general and administrative expenses for 2011 include the full-year impact of expenses incurred by the operations of Eclipsys. Other increases during the current year include stock compensation expense and legal expenses incurred related to general legal matters, including negotiating transactions with customers and addressing claims asserted against the Company. These increases were partially offset by a decrease in expenses incurred relating to the Eclipsys Merger and other integration-related costs totaling $16 million.

Unallocated corporate amortization of intangible assets increased during the year ended December 31, 2011 as a result of amortization expense related to intangible assets acquired in the Eclipsys Merger totaling $31 million and $11 million for the years ended December 31, 2011 and 2010, respectively.

Table of Contents

Seven Months Ended December 31, 2010 Compared to Seven Months Ended December 31, 2009

The increase in unallocated corporate selling, general and administrative expenses during the seven months ended December 31, 2010 as compared to the seven months ended December 31, 2009 is attributable to an increase in headcount and expenses incurred related to the Eclipsys Merger, Coniston Transactions, and other integration-related costs totaling $57 million, in addition to unallocated corporate expenses incurred by legacy Eclipsys from the date of the merger, August 24, 2010.

Unallocated corporate amortization of intangible assets increased during the seven months ended December 31, 2010 as a result of increased amortization related to intangible assets acquired in the Eclipsys Merger.

Year Ended May 31, 2010 Compared to Year Ended May 31, 2009

The increase in unallocated corporate selling, general and administrative expenses during 2010 is primarily attributable to the inclusion of full-year results for legacy Allscripts in the fiscal year ended May 31, 2010 as compared to the prior year and an increase in headcount and employee-related compensation expenses. Additionally, we have incurred increased costs related to the proposed Eclipsys Merger and Coniston Transactions. Offsetting these increases are lower costs incurred in 2010 related to the 2008 Transactions and an impairment charge of $14 million related to the investment in Aprima recognized in the prior year which did not recur in 2010.

Unallocated corporate amortization of intangible assets increased during the year ended May 31, 2010 as a result of recognizing transaction-related expenses for a full year as compared to the prior year when amortization commenced in conjunction with the closing of the 2008 Transactions on October 10, 2008.

Interest Expense

	Year Ended December 31,			Seven Months Ended December 31,			Year Ended May 31,		
(Dollar amounts in thousands)	**2011**	**2010**	**% Change**	**2010**	**2009**	**% Change**	**2010**	**2009**	**% Change**
Interest expense	($20,750)	($10,992)	88.8%	($9,687)	($1,302)	644.0%	($1,993)	($2,162)	(7.8%)

Year Ended December 31, 2011 Compared to Year Ended December 31, 2010

Interest expense increased during the year ended December 31, 2011 as compared to the prior comparable period due to interest incurred on the amounts drawn against our credit facilities in order to fund the Coniston Transactions, and the write-off during the current year of previously deferred debt issuance costs totaling $2 million in connection with executing an amendment to our credit facilities.

Seven Months Ended December 31, 2010 Compared to Seven Months Ended December 31, 2009

Interest expense increased during the seven months ended December 31, 2010 as compared to the prior year comparable period primarily due to interest incurred on the amounts drawn against the Senior Secured Credit Facilities in order to fund the Coniston Transactions.

Year Ended May 31, 2010 Compared to Year Ended May 31, 2009

Interest expense decreased during the year ended May 31, 2010 as compared to the prior year due to the conversion of outstanding Debentures to common stock in the first fiscal quarter of 2010 and the repayment of the outstanding balance under the Credit Facility during 2010.

Table of Contents

Interest Income and Other, Net

(Dollar amounts in thousands)	Year Ended December 31, 2011	Year Ended December 31, 2010	% Change	Seven Months Ended December 31, 2010	Seven Months Ended December 31, 2009	% Change	Year Ended May 31, 2010	Year Ended May 31, 2009	% Change
Interest income and other, net	$1,685	$1,549	8.8%	$843	$240	251.3%	$946	$626	51.1%

Year Ended December 31, 2011 Compared to Year Ended December 31, 2010

The increase in interest income and other, net during the year ended December 31, 2011 is primarily due to an increase in the imputed interest income from the indemnification asset provided in connection with the acquired tax positions from the Coniston Transactions.

Seven Months Ended December 31, 2010 Compared to Seven Months Ended December 31, 2009

The increase in interest income and other, net during the seven month period ended December 31, 2010 is partially due to realized gains on investments and an increase in the cash and marketable securities balance, net of decreases due to lower interest rates earned.

Year Ended May 31, 2010 Compared to Year Ended May 31, 2009

The increase during 2010 is partially due to realized gains on investments and an increase in the cash and marketable securities balance, net of decreases due to lower interest rates earned on cash in 2010.

Income Tax Expense

(Dollar amounts in thousands)	Year Ended December 31, 2011	Year Ended December 31, 2010	% Change	Seven Months Ended December 31, 2010	Seven Months Ended December 31, 2009	% Change	Year Ended May 31, 2010	Year Ended May 31, 2009	% Change
Provision for income taxes	($43,870)	($24,676)	77.8%	($2,606)	($18,596)	(86.0%)	($40,666)	($18,376)	121.3%
Effective tax rate	37.3%	47.9%		(88.1%)	37.9%		39.3%	41.4%	

Year Ended December 31, 2011 Compared to Year Ended December 31, 2010

The effective tax rate for the year ended December 31, 2011 is lower compared to the prior year primarily due to nondeductible expenses incurred in 2010 related to the Eclipsys Merger and Coniston Transactions which increased the effective rate for 2010. The effective rate for 2011 also reflects lower state tax expense, which is expected to recur, compared to the prior year.

Seven Months Ended December 31, 2010 Compared to Seven Months Ended December 31, 2009

The effective tax rate increased significantly for the seven months ended December 31, 2010 compared to the prior year comparable period primarily due to nondeductible expenses incurred related to the Eclipsys Merger and Coniston Transactions and changes in state tax rates.

Year Ended May 31, 2010 Compared to Year Ended May 31, 2009

The decrease in the effective tax rate during 2010 is primarily due to a reduction in state income tax expense and the utilization of federal research and development credits.

Table of Contents

Contract Backlog

As of December 31, 2011 and 2010, we had a committed contract backlog of $2.9 billion and $2.7 billion, respectively. A portion of the contracts in the committed contract backlog are accounted for under the percentage of completion accounting method. The determination of the revenue related to percentage of completion contracts which is expected to be recognized over the next twelve months is based upon the projected implementation period for such contracts. We estimate that approximately 41% of the total backlog at December 31, 2011 will be recognized as revenue during 2012.

Bookings

Bookings reflect the value of executed contracts for software, hardware, services, remote hosting, outsourcing and SaaS, and totaled $1.1 billion and $0.9 billion in the year ended December 31, 2011 and 2010, respectively. Bookings amounts for the year ended December 31, 2010 include booking amounts of legacy Eclipsys for the full year.

Selected Quarterly Operating Results

The following tables set forth a summary of our quarterly financial information for our last eight quarters. We believe that all necessary adjustments, which consisted only of normal recurring adjustments, have been included in the amounts stated below to present fairly the results of such periods when read in conjunction with the consolidated financial statements and related notes included elsewhere in this Annual Report. The operating results for any quarter should not be relied upon to predict the results for any subsequent period or for the entire fiscal year. You should be aware of possible variances in our future quarterly results. See Risk Factors Risks Related to Our Stock Our quarterly operating results may vary. Please refer to the disclosure below the following table regarding data for the quarter ended September 30, 2011.

	Quarter Ended							
(In thousands, except per share amounts)	**December 31, 2011**	**September 30, 2011**	**June 30, 2011**	**March 31, 2011**	**December 31, 2010**	**September 30, 2010**	**June 30, 2010**	**March 31, 2010**
				(Unaudited)				
Consolidated Statements of Operations Data:		**(As Adjusted)**						
Revenue	$388,202	$363,736	$356,831	$335,308	$316,178	$242,393	$191,373	$184,392
Cost of revenue	212,255	201,763	189,036	175,458	170,071	117,981	86,800	80,335
Gross profit	175,947	161,973	167,795	159,850	146,107	124,412	104,573	104,057
Selling, general and administrative expenses	89,739	92,152	101,532	104,148	105,862	103,358	66,224	56,969
Research and development	31,306	26,032	24,764	22,004	20,874	16,697	15,314	12,534
Amortization of intangible assets	9,273	9,422	9,422	9,227	9,829	5,576	2,488	2,488
Income (loss) from operations	45,629	34,367	32,077	24,471	9,542	(1,219)	20,547	32,066
Interest expense	(4,027)	(3,746)	(5,050)	(7,927)	(6,527)	(3,537)	(294)	(634)
Interest income and other, net	501	425	355	404	570	250	638	91
Income (loss) before income taxes	42,103	31,046	27,382	16,948	3,585	(4,506)	20,891	31,523
(Provision) benefit for income taxes	(16,120)	(11,909)	(11,506)	(4,335)	(9,808)	5,879	(7,801)	(12,946)
Net income (loss)	$25,983	$19,137	$15,876	$12,613	($6,223)	$1,373	$13,090	$18,577
Earnings (loss) per share:								
Basic	$0.14	$0.10	$0.08	$0.07	($0.03)	$0.01	$0.09	$0.12
Diluted	$0.14	$0.10	$0.08	$0.07	($0.03)	$0.01	$0.09	$0.12

68

Table of Contents

Consolidated Statement of Operations for the quarter ended September 30, 2011

Subsequent to the third quarter, we re-evaluated our conclusions with regards to the accounting for a software transaction that occurred in the three month period ended September 30, 2011. The transaction involved the bulk sale and delivery of software licenses through a complex structure and involving multiple parties engaged in the sale and distribution of such software and future related deliverables such as support, services and maintenance. Such transactions are a new and emerging trend in our industry. Upon further consideration of the transaction, we noted other performance obligations in the arrangement which require the deferral of revenue until such obligations are satisfied. Accordingly, we have concluded that the earnings process for this isolated transaction was not complete at the time of software delivery and, as such, the associated revenue of $5 million should not have been recorded as of September 30, 2011.

In conjunction with this correction, we also determined that an adjustment was required to reduce selling, general and administrative expenses by approximately $2 million related to variable compensation, which includes sales commissions directly related to this sales transaction and bonus expense as a result of the adjusted financial results for the third quarter since our bonus structure is contingent on the achievement of certain annual earnings metrics. As a result, we have adjusted our third quarter 2011 financial statements to reflect the $2 million reduction in selling, general and administrative expenses.

Although the adjustments are not deemed material to the previously reported interim revenues and operating results, we have included the effects of the adjustments in the table above. These adjustments had the following impact on our previously reported results for the three months ended September 30, 2011:

$5 million reduction in revenue system sales

$2 million reduction in selling, general and administrative expense

$1 million reduction in provision for income taxes

$2 million reduction in net income

$0.01 reduction in earnings per share basic and diluted

We have reconciled the effects of the adjustments to our previously reported interim statements of operations for the three and nine month periods ended September 30, 2011 in the condensed consolidated statements of operations presented in Note 1 to the accompanying consolidated financial statements.

There was no impact to our previously reported cash flows from operating, investing, and financing activities for the nine months ended September 30, 2011 as a result of adjustments described above. In addition, the adjustments do not have impact on our compliance with the Senior Secured Credit Facility covenants.

We will not amend our previously filed Form 10-Q for the quarterly period ended September 30, 2011 since the adjustments are not considered material to the consolidated financial statements. The as adjusted amounts above will be reflected in our statements of operations for the three and nine month periods ended September 30, 2011 within our third quarter 2012 Quarterly Report on Form 10-Q.

Table of Contents

Liquidity and Capital Resources

As of December 31, 2011 and 2010, our principal sources of liquidity consisted of cash, cash equivalents and marketable securities of $159 million and $131 million, respectively, and our revolving credit facility described below. The change in our cash balance is reflective of the following:

Operating Cash Flow Activities

	Year Ended December 31,			Seven Months Ended December 31,			Year Ended May 31,		
(In thousands)	**2011**	**2010**	**$ Change**	**2010**	**2009**	**$ Change**	**2010**	**2009**	**$ Change**
Net income (loss)	$73,609	$26,817	$46,792	($5,565)	$30,488	($36,053)	$62,870	$26,022	$36,848
Non-cash adjustments to net income	211,301	118,977	92,324	72,253	37,555	34,698	84,007	45,257	38,750
Cash impact of changes in operating assets and liabilities	(16,156)	33,107	(49,263)	9,093	(31,269)	40,362	(6,959)	(35,202)	28,243
Net cash provided by operating activities	$268,754	$178,901	$89,853	$75,781	$36,774	$39,007	$139,918	$36,077	$103,841

Year Ended December 31, 2011 Compared to Year Ended December 31, 2010

Net cash provided by operating activities increased in the current year primarily due to an increase in our overall profitability in 2011, in part, attributable to the inclusion of Eclipsys operations for all of 2011 and an increase in cash received from customers attributable to the cash contribution by Eclipsys. This increase was partially offset by an increase in operating disbursements also attributable to the full-year effect of the Eclipsys Merger.

Seven Months Ended December 31, 2010 Compared to Seven Months Ended December 31, 2009

Net cash provided by operating activities increased in the seven months ended December 31, 2010 primarily due to a decrease in the utilization of cash by working capital activities as compared to the prior year comparable period and the cash contribution by Eclipsys operations from the date of the merger, August 24, 2010. The additional cash provided by Eclipsys operations was partially offset by an increase in expenses related to the Eclipsys Merger, Coniston Transactions, and other integration-related costs incurred during the seven months ended December 31, 2010.

Year Ended May 31, 2010 Compared to Year Ended May 31, 2009

Cash flow from operations increased in 2010 due to an increase in cash received from customers attributable to the inclusion of full-year results for legacy Allscripts in the fiscal year ended May 31, 2010 as compared to the prior year in addition to fewer payments in 2010 for costs related to the 2008 Transactions. The increase in 2010 was partially offset by an increase in payments for costs related to the proposed Eclipsys Merger and the Coniston Transactions.

Table of Contents

Investing Cash Flow Activities

(In thousands)	Year Ended December 31, 2011	2010	$ Change	Seven Months Ended December 31, 2010	2009	$ Change	Year Ended May 31, 2010	2009	$ Change
Capital expenditures	($44,306)	($33,378)	($10,928)	($24,552)	($5,069)	($19,483)	($13,919)	($4,970)	($8,949)
Capitalized software	(60,748)	(47,761)	(12,987)	(36,936)	(10,272)	(26,664)	(21,097)	(14,001)	(7,096)
Net (purchases) sales and maturities of marketable securities and other investments	(12,845)	4,214	(17,059)	1,589	383	1,206	3,009	6,181	(3,172)
Proceeds received from sale of fixed assets	20,000	0	20,000	0	0	0	0	0	0
Change in restricted cash	2,225	2,216	9	2,216	0	2,216	0	0	0
Net cash acquired in merger with Eclipsys	0	170,102	(170,102)	170,102	0	170,102	0	0	0
Payment for acquisition of Allscripts, net of cash acquired	0	0	0	0	0	0	0	(263,766)	263,766
Net proceeds received from sale of building	0	0	0	0	0	0	0	6,450	(6,450)
Net proceeds received from sale of prepackaged medications business	0	0	0	0	0	0	0	8,000	(8,000)
Net cash (used in) provided by investing activities	($95,674)	$95,393	($191,067)	$112,419	($14,958)	$127,377	($32,007)	($262,106)	$230,099

Year Ended December 31, 2011 Compared to Year Ended December 31, 2010

Net cash used in investing activities increased during the year ended December 31, 2011 primarily due to increases in capital expenditures and software development expenditures. Also, the prior period includes cash and restricted cash acquired in the Eclipsys Merger. The increase in capital expenditures is related to the acquisition of computer equipment and software to improve our information systems infrastructure and to accommodate data management and hosting related to our SaaS and hosting solutions. The capitalization of software development costs increased as a result of the increased level of research and development expenditures during the current year that was driven by new product initiatives and regulatory updates to existing products related to initial meaningful use requirements. Capital expenditures and capitalized software expenditures are also higher in the current year due to the inclusion of a full year of Eclipsys operations. Our investments in dbMotion Ltd. and Humedica, Inc. also contributed to the increase. These increases were partially offset by proceeds received from the sale of a portion of our hosting equipment and infrastructure related to our Sunrise acute care clients to Affiliated Computer Services, Inc. (ACS), and the elimination of our restricted cash balance due to the expiration of certain letters of credit.

Seven Months Ended December 31, 2010 Compared to Seven Months Ended December 31, 2009

Cash provided by investing activities increased during the seven months ended December 31, 2010 due to the cash and restricted cash acquired in the Eclipsys Merger. This increase was partially offset by increases in capital expenditures and software development expenditures. The increase in capital expenditures is related to the acquisition of computer equipment and software to improve our information systems infrastructure and to accommodate data management and hosting related to our products. The capitalization of software development costs increased as a result of the increased level of research and development expenditures during the seven months ended December 31, 2010 that was driven by new product initiatives and regulatory updates to existing products related to meaningful use . Capital expenditures and capitalized software expenditures are also higher during the seven months ended December 31, 2010 due to the inclusion of amounts related to Eclipsys operations from the merger date, August 24, 2010, totaling $14 million and $8 million, respectively.

Year Ended May 31, 2010 Compared to Year Ended May 31, 2009

Cash used for investing activities decreased compared to the prior year primarily due to the payment in 2009 for the acquisition of legacy Allscripts which did not recur in 2010. This decrease was partially offset by

71

Table of Contents

increases in capital expenditures and software development expenditures in 2010. The increase in capital expenditures is related to the acquisition of computer equipment and software to improve our information systems infrastructure and to accommodate data management and hosting related to our products. The capitalization of software development costs increased as a result of the increased level of research and development expenditures during fiscal year 2010 that was driven by new product initiatives.

Financing Cash Flow Activities

	Year Ended December 31,			Seven Months Ended December 31,			Year Ended May 31,		
(In thousands)	**2011**	**2010**	**$ Change**	**2010**	**2009**	**$ Change**	**2010**	**2009**	**$ Change**
Proceeds from issuance of common stock	$35,119	$11,558	$23,561	$10,426	$2,462	$7,964	$3,594	$5,620	($2,026)
Excess tax benefits from stock-based compensation	8,818	(1,063)	9,881	(457)	6,857	(7,314)	6,251	5,463	788
Taxes paid related to net share settlement of equity awards	(11,456)	0	(11,456)	0	0	0	0	0	0
Net payments on debt instruments	(171,851)	(106,216)	(65,635)	(81,705)	(20,993)	(60,712)	(45,505)	(21,475)	(24,030)
Credit facility borrowings, net of issuance costs	47,193	547,744	(500,551)	547,744	0	547,744	0	0	0
Change in parent s net investment	0	0	0	0	0	0	0	358,802	(358,802)
Repurchase of common stock	(51,462)	(679,000)	627,538	(679,000)	0	(679,000)	0	(51,547)	51,547
Net cash (used in) provided by financing activities	($143,639)	($226,977)	$83,338	($202,992)	($11,674)	($191,318)	($35,660)	$296,863	($332,523)

Year Ended December 31, 2011 Compared to Year Ended December 31, 2010

Net cash used in financing activities decreased during the year ended December 31, 2011 compared to the prior period primarily due to the current year increase in proceeds from stock-based compensation activities and considering the prior period effects of the repurchase of common stock related to the reduction of Misys share ownership in Allscripts and proceeds from the Senior Secured Credit Facilities which were used to fund the Coniston Transactions in connection with the Eclipsys Merger which did not recur in 2011. Payments on debt instruments increased due to repayment of borrowings under the Senior Secured Credit Facilities which originated in August 2010. Also, additional payments and borrowings, each totaling $49 million, net of $1 million in debt issuance costs, occurred in the current year in connection with the Amended and Restated Credit Agreement. We repurchased approximately 3 million shares of our common stock for $51 million during the current year pursuant to our stock repurchase program. As of December 31, 2011, the amount available for repurchase of common stock under the program was $149 million. Finally, during the current year the majority of restricted stock units and awards that vested were net-share settled such that we withheld shares with a value equivalent to the employees minimum statutory obligation for the applicable income and other employment taxes and remitted the cash to the appropriate taxing authorities. These net-share settlements had the effect of share repurchases by us as they reduced the number of shares that would have otherwise been issued as a result of the vesting.

Seven Months Ended December 31, 2010 Compared to Seven Months Ended December 31, 2009

Cash used for financing activities increased during the seven months ended December 31, 2010 compared to the prior year comparable period primarily due to the repurchase of common stock related to the reduction of Misys

72

Table of Contents

ownership in Allscripts. The increase is partially offset by proceeds from the Senior Secured Credit Facilities which were used to fund the Coniston Transactions and working capital needs. Payments on debt instruments primarily increased due to repayment of borrowings under the Senior Secured Credit Facilities. Additionally, an increase in proceeds from issuance of common stock partially offsets the increases in cash used for financing activities.

Year Ended May 31, 2010 Compared to Year Ended May 31, 2009

Cash used for financing activities increased compared to the prior year primarily due to the receipt of cash from Misys in 2009 in connection with the 2008 Transactions that did not recur in 2010. Contributing to the increase were payments made to fully liquidate outstanding balances under the Credit Facility during 2010. Partially offsetting these increases are payments in 2009 for the repurchase of senior convertible notes and common stock that did not recur in 2010.

Free Cash Flow

To supplement our statements of cash flows presented on a GAAP basis, we use a non-GAAP measure of free cash flow which we believe is also useful as one of the bases for evaluating our performance. We believe free cash flow is an important liquidity metric, as it measures the amount of cash generated that is available to repay our current debt obligations, make investments, fund acquisitions, repurchase our common stock and for certain other activities. The presentation of non-GAAP free cash flow is not meant to be considered in isolation and should not be considered a substitute for income from operations, net income, net cash provided by operating activities or any other measure determined in accordance with GAAP. Operating asset and liability balances can fluctuate significantly from period to period and there can be no assurance that free cash flow will not be negatively impacted by material changes in operating assets and liabilities in future periods, since these changes depend upon, among other things, management s timing of payments and cash receipts. In addition to fluctuations resulting from changes in operating assets and liabilities, free cash flow can vary significantly from period to period depending upon, among other things, operating efficiencies, increases or decreases in capital expenditures and capitalized software, and other factors.

We calculate free cash flow as follows:

	Year Ended December 31,			Seven Months Ended December 31,			Year Ended May 31,		
(In thousands)	**2011**	**2010**	**$ Change**	**2010**	**2009**	**$ Change**	**2010**	**2009**	**$ Change**
Net cash provided by operating activities	$268,754	$178,901	$89,853	$75,781	$36,774	$39,007	$139,918	$36,077	$103,841
Capital expenditures	(44,306)	(33,378)	(10,928)	(24,552)	(5,069)	(19,483)	(13,919)	(4,970)	(8,949)
Capitalized software	(60,748)	(47,761)	(12,987)	(36,936)	(10,272)	(26,664)	(21,097)	(14,001)	(7,096)
Free cash flow	$163,700	$97,762	$65,938	$14,293	$21,433	($7,140)	$104,902	$17,106	$87,796

Amounts for each element of the table above are as reported in our consolidated statements of cash flows presented in accordance with GAAP.

Future Capital Requirements

In connection with the Coniston Transactions, on August 20, 2010 (the Closing Date), Allscripts entered into a Credit Agreement with JPMorgan Chase Bank, N.A., as administrative agent, UBS Securities LLC and Barclays Capital, as co-syndication agents, and a syndicate of banks as co-documentation agents (the Credit Agreement).

The Credit Agreement provides for a $470 million senior secured term loan facility (the Term Facility) and a $250 million senior secured revolving facility (the Revolving Facility), each of which has a five year

Table of Contents

term (collectively the Senior Secured Credit Facilities). In connection with the closing of the Coniston Transactions, Allscripts borrowed $470 million under the Term Facility and $100 million under the Revolving Facility. Allscripts incurred $22 million in debt issuance costs related to the Senior Secured Credit Facilities. The net proceeds were used by Allscripts to finance a portion of the Coniston Transactions. The Revolving Facility is available to finance working capital needs and general corporate purposes.

On March 31, 2011, we entered into an agreement (the Amended and Restated Credit Agreement) with participating lenders to amend and restate the Credit Agreement among the Company and certain parties. The Amended and Restated Credit Agreement includes certain changes to the terms of the Credit Agreement. Certain members of the syndicate of banks supporting the Senior Secured Credit Facilities withdrew upon execution of the Amended and Restated Credit Agreement. Accordingly, funds provided by the withdrawing banks totaling $49 million were repaid and the same amount was subsequently borrowed from other banks. We incurred additional debt issuance costs totaling $1 million and wrote off previously deferred debt issuance costs totaling $2 million to interest expense on the consolidated statement of operations during the year ended December 31, 2011 in connection with executing the Amended and Restated Credit Agreement. The additional debt issuance costs incurred were deferred and are included in other assets on the balance sheet at December 31, 2011.

The Amended and Restated Credit Agreement reduces the applicable interest margin for borrowings under the senior credit facilities by 75 basis points at each level of the leverage based pricing grid. In addition, the Commitment Fee was reduced at certain levels of the leverage based pricing grid. The Amended and Restated Credit Agreement also allows the Company to borrow up to $100 million under its revolving credit facility in certain foreign currencies and increases the leverage ratio in which the Company can make unlimited Restricted Payments from 1.75 to 1 to 2.00 to 1.

The maturity date and principal amount of the senior secured credit facilities remains the same as in the Credit Agreement. In addition, the prepayment provisions and covenants included in the Credit Agreement have not changed, except as discussed above.

The Term Facility matures in quarterly installments which commenced on December 31, 2010, provided that, notwithstanding the above, the remaining principal balance shall be due and payable on the fifth anniversary of the Closing Date. The remaining quarterly installment payments, as adjusted for any prepayments on the Term Facility through December 31, 2011, are as follows (in thousands):

Quarterly Installments	Quarterly Principal Amount
March 31, 2012 to September 30, 2012	$9,928
December 31, 2012 to September 30, 2013	14,893
December 31, 2013 to September 30, 2014	19,856
December 31, 2014 to June 30, 2015	24,820
August 20, 2015	Remaining balance

A total of $50 million of the Revolving Facility is available for the issuance of letters of credit and $10 million of the Revolving Facility is available for swingline loans. Allscripts is also permitted to add one or more incremental revolving and/or term loan facilities in an aggregate amount of up to $250 million, subject to certain conditions.

Borrowings under the Senior Secured Credit Facilities bear interest, at Allscripts option, at a rate per annum equal to either (1) the highest of (a) the rate of interest publicly announced by JPMorgan Chase Bank, N.A. as its prime rate in effect at its principal office in New York City, (b) the federal funds effective rate from time to time plus 0.5%, and (c) the rate for Eurodollar deposits as reflected on the applicable Reuters Screen LIBOR01 for a one month interest period, as such rate may be adjusted for certain reserve requirements, plus 1.0%, or (2) the rate for Eurodollar deposits as reflected on the applicable Reuters Screen LIBOR01 for the interest period relevant to such borrowing, as such rate may be adjusted for certain reserve requirements, plus, in

Table of Contents

each case, the applicable margin. The applicable margin for borrowings under the Senior Secured Credit Facilities was fixed until the date that was three business days after Allscripts financial statements were delivered to lenders with respect to the first fiscal period ending after September 30, 2010, and thereafter the applicable margin for borrowings under the Senior Secured Credit Facilities is subject to further adjustment based on an agreed upon leverage grid.

Subject to certain agreed upon exceptions, all obligations under the Senior Secured Credit Facilities are guaranteed by each of Allscripts existing and future direct and indirect material domestic subsidiaries, other than Coniston Exchange LLC (successor to Coniston, Inc.) (the Guarantors).

The obligations of Allscripts and each Guarantor under the Senior Secured Credit Facilities, any swap agreements and any cash management arrangements provided by any lender, are secured, subject to permitted liens and other agreed upon exceptions, by a perfected first priority security interest in all of the tangible and intangible assets (including, without limitation, intellectual property, material owned real property and all of the capital stock of each Guarantor and, in the case of foreign subsidiaries, up to 65% of the capital stock of first tier material foreign subsidiaries) of Allscripts and the Guarantors.

Subject to certain exceptions, Allscripts is required to prepay the Term Facility: (i) with 100% of the net cash proceeds received from the incurrence of certain indebtedness for borrowed money; (ii) with 100% of the net cash proceeds of the sale of any assets in excess of $5 million outside the ordinary course of business (including, without limitation, insurance and condemnation proceeds) in any fiscal year, subject to reinvestment rights; and (iii) with 50% of Allscripts excess cash flow for each fiscal year, beginning with the 2012 fiscal year. No prepayments under clauses (ii) or (iii) above are required to the extent that Allscripts total leverage ratio is less than 2.5 to 1.0. Allscripts may voluntarily prepay outstanding loans under the Senior Secured Credit Facilities, in whole or in part, at Allscripts option at any time upon prior notice.

The Senior Secured Credit Facilities contain a number of covenants that, among other things, restrict, subject to certain exceptions, Allscripts ability to:

- incur indebtedness (including guarantee obligations);
- create liens on and sell assets;
- engage in mergers or consolidations;
- declare dividends and other payments in respect of our capital stock;
- make investments, loans and advances;
- engage in transactions with affiliates;
- enter into sale and leaseback transactions; and
- change lines of business.

In addition, the Senior Secured Credit Facilities include a maximum leverage ratio of 3.0 to 1.0 and a minimum interest coverage ratio of 4.5 to 1.0. The leverage ratio is calculated by dividing total indebtedness by earnings before interest expense, income tax expense, depreciation and amortization expense. The minimum interest coverage ratio is calculated by dividing earnings before interest expense and income tax expense by cash interest expense.

The facilities also contain certain customary events of default, including relating to non-payment, breach of covenants, cross-default, bankruptcy and change of control.

As of December 31, 2011, $367 million in borrowings and $2 million in letters of credit were outstanding under the Amended and Restated Credit Agreement. As of December 31, 2011, the interest rate on the Senior Secured Credit Facilities was LIBOR plus 1.75%, which totaled 2.05%. Refer to Quantitative and Qualitative

Table of Contents

Disclosures About Market Risk for the interest rate swap agreement. There was no default under the Amended and Restated Credit Agreement as of December 31, 2011.

As of December 31, 2011, we had $248 million available, net of outstanding letters of credit, under the Revolving Facility. There can be no assurance that we will be able to draw on the full available balance of our Amended and Restated Credit Agreement if the financial institutions that have extended such credit commitments become unwilling or unable to fund such borrowings.

We believe that our cash, cash equivalents and marketable securities of $159 million as of December 31, 2011, our future cash flows, and our borrowing capacity under our Amended and Restated Credit Agreement, taken together, provide adequate resources to fund ongoing cash requirements for the next twelve months. We cannot provide assurance that our actual cash requirements will not be greater than we expect as of the date of this report. We will, from time to time, consider the acquisition of, or investment in, complementary businesses, products, services and technologies, and the purchase of our common stock under our stock repurchase program which might impact our liquidity requirements or cause us to issue additional equity or debt securities.

If sources of liquidity are not available or if we cannot generate sufficient cash flow from operations during the next twelve months, we might be required to obtain additional sources of funds through additional operating improvements, capital market transactions, asset sales or financing from third parties, a combination thereof or otherwise. We cannot provide assurance that these additional sources of funds will be available or, if available, would have reasonable terms.

Contractual Obligations, Commitments and Off Balance Sheet Arrangements

We have various contractual obligations, which are recorded as liabilities in our consolidated financial statements. Other items, such as operating lease contract obligations are not recognized as liabilities in our consolidated financial statements but are required to be disclosed.

The following table summarizes our significant contractual obligations as of December 31, 2011 and the effect such obligations are expected to have on our liquidity and cash in future periods assuming all obligations reach maturity:

(In thousands)	Total	2012	2013	2014	2015	2016	Thereafter
Contractual obligations:							
Debt:[1]							
Principal payments	$367,341	$44,676	$64,532	$84,388	$173,745	$0	$0
Interest payments	26,163	9,574	7,921	5,821	2,847	0	0
Capital leases	2,547	961	674	554	244	114	0
Non-cancelable operating leases	88,040	19,151	17,273	13,209	12,252	11,912	14,243
Unconditional purchase obligations[2]	25,819	13,182	8,395	4,242	0	0	0
Agreement with Affiliated Computer Services, Inc.[3]	432,947	53,413	52,223	50,136	49,063	47,350	180,762
Other contractual obligations[4]	1,747	1,747	0	0	0	0	0
Total contractual obligations	$944,604	$142,704	$151,018	$158,350	$238,151	$59,376	$195,005

The Company believes it has income tax exposure totaling $43 million as of December 31, 2011 primarily related to tax exposure acquired in connection with the Eclipsys Merger and Coniston Transactions and pre-acquisition NOL s for the legacy Allscripts group. Liabilities that may result from this exposure have been excluded from the table above since we cannot predict with reasonable reliability the outcome of discussions with the respective taxing jurisdictions, which may or may not result in cash settlements. We have excluded net deferred tax liabilities of $74 million from the amounts presented in the table as the amounts that will be settled in cash are not known and the timing of any payments is uncertain.

Table of Contents

The acquired tax position related to the Misys share repurchase totaling $26 million is indemnified by Misys.

(1) As described in Future Capital Requirements, the Company entered into a credit agreement whereby we borrowed $570 million to finance the repurchase of Allscripts shares held by Misys. The term facility provided under the credit agreement matures in quarterly installments commencing on December 31, 2010, and the revolving facility matures on August 20, 2015. As described in Quantitative and Qualitative Disclosures About Market Risk, the Company entered into an interest rate swap agreement that converts the one-month LIBOR rate on the corresponding notional amount of debt to an effective fixed rate of 0.896%. Interest payments on borrowings presented in the contractual obligations table above have been estimated using the effective fixed rate, which represented our effective interest rate after consideration of the interest rate swap agreement, and assumes the LIBOR rate and applicable margin are consistent with the actual rate at December 31, 2011.

(2) The unconditional purchase obligations consist of minimum purchase commitments for telecommunication services, computer equipment, maintenance, consulting and other commitments.

(3) On March 31, 2011, we entered into a ten year agreement with Affiliated Computer Services, Inc. (ACS) to provide services to support our remote hosting services for our Sunrise acute care clients. We will maintain all customer relationships and domain expertise with respect to the hosted applications. The agreement encompasses our payment to ACS for current Allscripts employees to be retained by ACS from our hosting staff, new remote hosting staff and technology infrastructure, as well as other data center and hosting services.

(4) As of December 31, 2011, we had letters of credit outstanding under our Credit Agreement. The letters of credit are provided as security for a corporate facilities lease and to support workers compensation insurance policies. No amounts had been drawn on the letters of credit at December 31, 2011.

Table of Contents

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to market risks, primarily changes in U.S. and LIBOR interest rates. Allscripts is exposed to the risk that our earnings and cash flows could be adversely impacted by fluctuations in interest rates due to the cash borrowed under our Senior Secured Credit Facilities. Based upon our balance of $367 million of debt under our Senior Secured Credit Facilities as of December 31, 2011, an increase in interest rates of 1.0% would cause a corresponding increase in our annual interest expense of $4 million. We entered into an interest rate swap agreement with an effective date of October 29, 2010 that has the economic effect of modifying the variable rate component of the interest obligations associated with a portion of our variable rate debt. The initial notional amount of the interest rate swap agreement is $300 million, with scheduled step downs in the future, and a final termination date of October 31, 2014. The interest rate swap agreement converts the one-month LIBOR rate on the corresponding notional amount of debt to an effective fixed rate of 0.896% (exclusive of the applicable margin currently charged under the Senior Secured Credit Facilities). The interest rate swap agreement protects us against changes in interest payments due to benchmark interest rate movements.

Allscripts has international operations; therefore, we are exposed to risks related to foreign currency fluctuations. Foreign currency fluctuations through December 31, 2011 have not had a material impact on our financial position or results of operations. We continually monitor our exposure to foreign currency fluctuations and may use derivative financial instruments and hedging transactions in the future if, in our judgment, the circumstances warrant their use. We believe most of our international operations are naturally hedged for foreign currency risk as our foreign subsidiaries invoice their clients and satisfy their obligations primarily in their local currencies with the exception of our development center in India. Our development center in India is not naturally hedged for foreign currency risk since their obligations are paid in their local currency but are funded in U.S. dollars. There can be no guarantee that the impact of foreign currency fluctuations in the future will not be significant and will not have a material impact on our financial position or results of operations.

As of December 31, 2011, we had cash, cash equivalents and marketable securities in financial instruments of $159 million. Declines in interest rates over time will reduce our interest income from our investments. Based upon our balance of cash, cash equivalents and marketable securities as of December 31, 2011, a decrease in interest rates of 1.0% would cause a corresponding decrease in our annual interest income of $2 million.

Table of Contents

Item 8. Financial Statements and Supplementary Data

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders

Allscripts Healthcare Solutions, Inc.

We have audited the consolidated balance sheet of Allscripts Healthcare Solutions, Inc. as of December 31, 2011, and the related statements of operations, comprehensive income, stockholders equity, and cash flows for the year then ended. Our audit also included the financial statement schedule listed in the Index at Item 15(a)(2). These financial statements and schedule are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). 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 financial statements referred to above present fairly, in all material respects, the consolidated financial position of Allscripts Healthcare Solutions, Inc. at December 31, 2011, and the consolidated results of its operations and its cash flows for the year then ended, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Allscripts Healthcare Solutions, Inc. s internal control over financial reporting as of December 31, 2011, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 29, 2012 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Chicago, Illinois

February 29, 2012

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders

Allscripts Healthcare Solutions, Inc.

We have audited Allscripts Healthcare Solutions, Inc. s internal control over financial reporting as of December 31,2011 based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Allscripts Healthcare Solutions, Inc. s management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management s Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the company s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Allscripts Healthcare Solutions, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2011, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Allscripts Healthcare Solutions, Inc. as of December 31, 2011, and the related statements of operations, comprehensive income, stockholders equity, and cash flows for the year then ended, and our report dated February 29, 2012 expressed an unqualified opinion thereon.

- (240) (72)

Proceeds from the sale of assets and businesses (F)

615 38 4

Additions to investments (I & N)

(300) (374) (352)

Sales of investments (I)

31 54 141

Net change in restricted cash (P)

87	(4)	7
Other		
69	(39)	15
Cash used for investing activities		
(759)	(1,852)	(1,272)
Effect of exchange rate changes on cash and cash equivalents		
(18)	(7)	25
Net change in cash and cash equivalents		
(78)	396	62
Cash and cash equivalents at beginning of year		
1,939	1,543	1,481
Cash and cash equivalents at end of year		
$1,861	$1,939	$1,543

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

Alcoa and subsidiaries

Statement of Changes in Consolidated Equity

(in millions, except per-share amounts)

	Alcoa Shareholders							
	Preferred stock	Common stock	Additional capital	Retained earnings	Treasury stock	Accumulated other comprehensive loss	Noncontrolling interests	Total equity
Balance at December 31, 2009	$ 55	$ 1,097	$ 6,608	$ 11,020	$ (4,268)	$ (2,092)	$ 3,100	$ 15,520
Net income	-	-	-	254	-	-	138	392
Other comprehensive income	-	-	-	-	-	417	334	751
Cash dividends declared:								
Preferred @ $3.75 per share	-	-	-	(2)	-	-	-	(2)
Common @ $0.12 per share	-	-	-	(123)	-	-	-	(123)
Stock-based compensation (R)	-	-	84	-	-	-	-	84
Common stock issued: compensation plans (R)	-	-	(139)	-	122	-	-	(17)
Issuance of common stock (R)	-	44	556	-	-	-	-	600
Distributions	-	-	-	-	-	-	(256)	(256)
Contributions (M)	-	-	-	-	-	-	162	162
Purchase of equity from noncontrolling interest (P)	-	-	(2)	-	-	-	(4)	(6)
Other (P)	-	-	(20)	-	-	-	1	(19)
Balance at December 31, 2010	55	1,141	7,087	11,149	(4,146)	(1,675)	3,475	17,086
Net income	-	-	-	611	-	-	194	805
Other comprehensive loss	-	-	-	-	-	(952)	(229)	(1,181)
Cash dividends declared:								
Preferred @ $3.75 per share	-	-	-	(2)	-	-	-	(2)
Common @ $0.12 per share	-	-	-	(129)	-	-	-	(129)
Stock-based compensation (R)	-	-	83	-	-	-	-	83
Common stock issued: compensation plans (R)	-	-	(172)	-	194	-	-	22
Issuance of common stock (R)	-	37	563	-	-	-	-	600
Distributions	-	-	-	-	-	-	(257)	(257)
Contributions (M)	-	-	-	-	-	-	169	169
Other	-	-	-	-	-	-	(1)	(1)
Balance at December 31, 2011	55	1,178	7,561	11,629	(3,952)	(2,627)	3,351	17,195
Net income (loss)	-	-	-	191	-	-	(29)	162
Other comprehensive loss	-	-	-	-	-	(775)	(73)	(848)
Cash dividends declared:								
Preferred @ $3.75 per share	-	-	-	(2)	-	-	-	(2)
Common @ $0.12 per share	-	-	-	(129)	-	-	-	(129)
Stock-based compensation (R)	-	-	67	-	-	-	-	67
Common stock issued: compensation plans (R)	-	-	(68)	-	71	-	-	3
Distributions	-	-	-	-	-	-	(95)	(95)
Contributions (M)	-	-	-	-	-	-	171	171
Other	-	-	-	-	-	-	(1)	(1)
Balance at December 31, 2012	$ 55	$ 1,178	$ 7,560	$ 11,689	$ (3,881)	$ (3,402)	$ 3,324	$ 16,523

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

Alcoa and subsidiaries

Notes to the Consolidated Financial Statements

(dollars in millions, except per-share amounts)

A. Summary of Significant Accounting Policies

Basis of Presentation. The Consolidated Financial Statements of Alcoa Inc. and subsidiaries (Alcoa or the Company) are prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) and require management to make certain judgments, estimates, and assumptions. These may affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements. They also may affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates upon subsequent resolution of identified matters. Certain amounts in previously issued financial statements were reclassified to conform to the 2012 presentation (see Note B).

Principles of Consolidation. The Consolidated Financial Statements include the accounts of Alcoa and companies in which Alcoa has a controlling interest. Intercompany transactions have been eliminated. The equity method of accounting is used for investments in affiliates and other joint ventures over which Alcoa has significant influence but does not have effective control. Investments in affiliates in which Alcoa cannot exercise significant influence are accounted for on the cost method.

Management also evaluates whether an Alcoa entity or interest is a variable interest entity and whether Alcoa is the primary beneficiary. Consolidation is required if both of these criteria are met. Alcoa does not have any variable interest entities requiring consolidation.

Related Party Transactions. Alcoa buys products from and sells products to various related companies, consisting of entities in which Alcoa retains a 50% or less equity interest, at negotiated arms-length prices between the two parties. These transactions were not material to the financial position or results of operations of Alcoa for all periods presented.

Cash Equivalents. Cash equivalents are highly liquid investments purchased with an original maturity of three months or less.

Inventory Valuation. Inventories are carried at the lower of cost or market, with cost for a substantial portion of U.S. and Canadian inventories determined under the last-in, first-out (LIFO) method. The cost of other inventories is principally determined under the average-cost method.

Properties, Plants, and Equipment. Properties, plants, and equipment are recorded at cost. Depreciation is recorded principally on the straight-line method at rates based on the estimated useful lives of the assets. For greenfield assets, which refer to the construction of new assets on undeveloped land, the units of production method is used to record depreciation. These assets require a significant period (generally greater than one-year) to ramp-up to full production capacity. As a result, the units of production method is deemed a more systematic and rational method for recognizing depreciation on these assets. Depreciation is recorded on temporarily idled facilities until such time management approves a permanent shutdown. The following table details the weighted-average useful lives of structures and machinery and equipment by reporting segment (numbers in years):

Segment	Structures	Machinery and equipment
Alumina:		
Alumina refining	30	25
Bauxite mining	33	19
Primary Metals:		
Aluminum smelting	35	21
Power generation	34	24
Global Rolled Products	32	21
Engineered Products and Solutions	29	18

Gains or losses from the sale of assets are generally recorded in other income or expenses (see policy that follows for assets classified as held for sale and discontinued operations). Repairs and maintenance are charged to expense as incurred. Interest related to the construction of qualifying assets is capitalized as part of the construction costs.

Properties, plants, and equipment are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets (asset group) may not be recoverable. Recoverability of assets is determined by comparing the estimated undiscounted net cash flows of the operations related to the assets (asset group) to their carrying amount. An impairment loss would be recognized when the carrying amount of the assets (asset group) exceeds the estimated undiscounted net cash flows. The amount of the impairment loss to be recorded is calculated as the excess of the carrying value of the assets (asset group) over their fair value, with fair value determined using the best information available, which generally is a discounted cash flow model (DCF model). The determination of what constitutes an asset group, the associated estimated undiscounted net cash flows, and the estimated useful lives of assets also require significant judgments.

Mineral Rights. Alcoa recognizes mineral rights upon specific acquisitions of land that include such underlying rights, primarily in Jamaica. This land is purchased for the sole purpose of mining bauxite. The underlying bauxite reserves are known at the time of acquisition based on associated drilling and analysis and are considered to be proven reserves. The acquisition cost of the land and mineral rights are amortized as the bauxite is produced based on the level of minable tons determined at the time of purchase. Mineral rights are included in Properties, plants, and equipment on the accompanying Consolidated Balance Sheet.

Deferred Mining Costs. Alcoa recognizes deferred mining costs during the development stage of a mine life cycle. Such costs include the construction of access and haul roads, detailed drilling and geological analysis to further define the grade and quality of the known bauxite, and overburden removal costs. These costs relate to sections of the related mines where Alcoa is either currently extracting bauxite or is preparing for production in the near term. These sections are outlined and planned incrementally and generally are mined over periods ranging from one to five years, depending on mine specifics. The amount of geological drilling and testing necessary to determine the economic viability of the bauxite deposit being mined is such that the reserves are considered to be proven, and the mining costs are amortized based on this level of reserves. Deferred mining costs are included in Other noncurrent assets on the accompanying Consolidated Balance Sheet.

Goodwill and Other Intangible Assets. Goodwill is not amortized; instead, it is reviewed for impairment annually (in the fourth quarter) or more frequently if indicators of impairment exist or if a decision is made to sell a business. A significant amount of judgment is involved in determining if an indicator of impairment has occurred. Such indicators may include deterioration in general economic conditions, negative developments in equity and credit markets, adverse changes in the markets in which an entity operates, increases in input costs that have a negative effect on earnings and cash flows, or a trend of negative or declining cash flows over multiple periods, among others. The fair value that could be realized in an actual transaction may differ from that used to evaluate the impairment of goodwill.

Goodwill is allocated among and evaluated for impairment at the reporting unit level, which is defined as an operating segment or one level below an operating segment. Alcoa has nine reporting units, of which five are included in the Engineered Products and Solutions segment. The remaining four reporting units are the Alumina segment, the Primary Metals segment, the Global Rolled Products segment, and the soft alloy extrusions business in Brazil, which is included in Corporate. Almost 90% of Alcoa s total goodwill is allocated to three reporting units as follows: Alcoa Fastening Systems (AFS) ($1,160) and Alcoa Power and Propulsion (APP) ($1,628) businesses, both of which are included in the Engineered Products and Solutions segment, and Primary Metals ($1,748). These amounts include an allocation of Corporate s goodwill.

In September 2011, the Financial Accounting Standards Board issued new accounting guidance for testing goodwill for impairment (see Recently Adopted Accounting Guidance section of Note A below). The guidance provides an entity the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not (more than 50%) that the estimated fair value of a reporting unit is less than

its carrying amount. If an entity elects to perform a qualitative assessment and determines that an impairment is more likely than not, the entity is then required to perform the existing two-step quantitative impairment test (described below), otherwise no further analysis is required. An entity also may elect not to perform the qualitative assessment and, instead, proceed directly to the two-step quantitative impairment test. The ultimate outcome of the goodwill impairment review for a reporting unit should be the same whether an entity chooses to perform the qualitative assessment or proceeds directly to the two-step quantitative impairment test.

In the 2011 fourth quarter, in conjunction with management s annual review of goodwill, Alcoa early adopted the new guidance. As a result, Alcoa instituted a policy for its annual review of goodwill to perform the qualitative assessment for all reporting units not subjected directly to the two-step quantitative impairment test. Management will proceed directly to the two-step quantitative impairment test for a minimum of three reporting units (based on facts and circumstances) during each annual review of goodwill. This policy will result in each of the nine reporting units being subjected to the two-step quantitative impairment test at least once during every three-year period.

Under the qualitative assessment, various events and circumstances (or factors) that would affect the estimated fair value of a reporting unit are identified (similar to impairment indicators above). These factors are then classified by the type of impact they would have on the estimated fair value using positive, neutral, and adverse categories based on current business conditions. Additionally, an assessment of the level of impact that a particular factor would have on the estimated fair value is determined using high, medium, and low weighting. Furthermore, management considers the results of the most recent two-step quantitative impairment test completed for a reporting unit (this would be 2011 and 2010 in which the estimated fair values of three and nine reporting units, respectively, were substantially in excess of their carrying values) and compares the weighted average cost of capital (WACC) between the current and prior years for each reporting unit.

During the 2012 annual review of goodwill, management performed the qualitative assessment for six reporting units. Management concluded that it was not more likely than not that the estimated fair values of the six reporting units were less than their carrying values. As such, no further analysis was required.

Under the two-step quantitative impairment test, the evaluation of impairment involves comparing the current fair value of each reporting unit to its carrying value, including goodwill. Alcoa uses a DCF model to estimate the current fair value of its reporting units when testing for impairment, as management believes forecasted cash flows are the best indicator of such fair value. A number of significant assumptions and estimates are involved in the application of the DCF model to forecast operating cash flows, including markets and market share, sales volumes and prices, costs to produce, tax rates, capital spending, discount rate, and working capital changes. Most of these assumptions vary significantly among the reporting units. Cash flow forecasts are generally based on approved business unit operating plans for the early years and historical relationships in later years. The betas used in calculating the individual reporting units WACC rate are estimated for each business with the assistance of valuation experts.

In the event the estimated fair value of a reporting unit per the DCF model is less than the carrying value, additional analysis would be required. The additional analysis would compare the carrying amount of the reporting unit s goodwill with the implied fair value of that goodwill, which may involve the use of valuation experts. The implied fair value of goodwill is the excess of the fair value of the reporting unit over the fair value amounts assigned to all of the assets and liabilities of that unit as if the reporting unit was acquired in a business combination and the fair value of the reporting unit represented the purchase price. If the carrying value of goodwill exceeds its implied fair value, an impairment loss equal to such excess would be recognized, which could significantly and adversely impact reported results of operations and shareholders equity.

During the 2012 annual review of goodwill, management proceeded directly to the two-step quantitative impairment test for three reporting units as follows: the Primary Metals segment, the Alumina segment, and the Global Rolled Products segment. For Global Rolled Products, the estimated fair value exceeded carrying value by more than 150%, resulting in no impairment. For Primary Metals and Alumina, the estimated fair values exceeded their carrying values by 9.2% and 7.4%, respectively, resulting in no impairment. These two reporting units have goodwill of $1,748 and

$171, respectively. In developing the fair value of these reporting units, the Company estimates future cash flows using London Metal Exchange (LME) forward curve pricing and operating cost assumptions management believes are reasonable based on expected and historical performance. The following could have a negative impact on the estimated fair values of Primary Metals and Alumina: a significant, protracted decrease in LME and alumina prices; decrease in long-term profitability; decrease in the long-term demand for aluminum; substantial reductions in Alcoa s end markets and volume assumptions; and an increase in discount rates.

As part of the 2012 annual review of goodwill, management considered the market capitalization of Alcoa s common stock in relation to the Company s total shareholders equity. At December 31, 2012, the market capitalization of Alcoa s common stock was $9,263. While this amount is less than the Company s total shareholders equity at December 31, 2012, the estimated aggregate fair value of Alcoa s reporting units was substantially in excess of the aforementioned market capitalization amount. In management s judgment, the main reason for the difference between Alcoa s market capitalization and total shareholders equity at December 31, 2012 is significantly lower commodity prices for aluminum. Management believes these commodity prices are being adversely impacted by turmoil in the macroeconomic environment, which do not necessarily reflect aluminum industry fundamentals. For example, there was, and continues to be, significant uncertainty of the sovereign debt of many European countries. This uncertainty has affected the liquidity of many companies that either operate or are located in Europe, although, Alcoa has not been impacted significantly. Additionally, during 2012, there was great concern over what was labeled the fiscal cliff in the U.S. and a slowdown in the growth of China. The combination of this economic uncertainty and the continuing decline in commodity prices caused the price of Alcoa s common stock to remain depressed. As a result, management believes the quoted market price of Alcoa s common stock does not fully reflect the underlying value of the future aggregate cash flows of the Company s reporting units. Accordingly, management does not believe that the comparison of Alcoa s market capitalization and total shareholders equity as of December 31, 2012 is an indication that goodwill is impaired.

Intangible assets with indefinite useful lives are not amortized while intangible assets with finite useful lives are amortized generally on a straight-line basis over the periods benefited. The following table details the weighted-average useful lives of software and other intangible assets by reporting segment (numbers in years):

Segment	Software	Other intangible assets
Alumina	10	-
Primary Metals	9	36
Global Rolled Products	10	13
Engineered Products and Solutions	9	19

Equity Investments. Alcoa invests in a number of privately-held companies, primarily through joint ventures and consortia, which are accounted for on the equity method. The equity method is applied in situations where Alcoa has the ability to exercise significant influence, but not control, over the investee. Management reviews equity investments for impairment whenever certain indicators are present suggesting that the carrying value of an investment is not recoverable. This analysis requires a significant amount of judgment from management to identify events or circumstances indicating that an equity investment is impaired. The following items are examples of impairment indicators: significant, sustained declines in an investee s revenue, earnings, and cash flow trends; adverse market conditions of the investee s industry or geographic area; the investee s ability to continue operations measured by several items, including liquidity; and other factors. Once an impairment indicator is identified, management uses considerable judgment to determine if the impairment is other than temporary, in which case the equity investment is written down to its estimated fair value. An impairment that is other than temporary could significantly and adversely impact reported results of operations.

Revenue Recognition. Alcoa recognizes revenue when title, ownership, and risk of loss pass to the customer, all of which occurs upon shipment or delivery of the product and is based on the applicable shipping terms. The shipping terms vary across all businesses and depend on the product, the country of origin, and the type of transportation (truck, train, or vessel).

Alcoa periodically enters into long-term supply contracts with alumina and aluminum customers and receives advance payments for product to be delivered in future periods. These advance payments are recorded as deferred revenue, and revenue is recognized as shipments are made and title, ownership, and risk of loss pass to the customer during the term of the contracts. Deferred revenue is included in Other current liabilities and Other noncurrent liabilities and deferred credits on the accompanying Consolidated Balance Sheet.

Environmental Matters. Expenditures for current operations are expensed or capitalized, as appropriate. Expenditures relating to existing conditions caused by past operations, which will not contribute to future revenues, are expensed. Liabilities are recorded when remediation costs are probable and can be reasonably estimated. The liability may include costs such as site investigations, consultant fees, feasibility studies, outside contractors, and monitoring expenses. Estimates are generally not discounted or reduced by potential claims for recovery. Claims for recovery are recognized as agreements are reached with third parties. The estimates also include costs related to other potentially responsible parties to the extent that Alcoa has reason to believe such parties will not fully pay their proportionate share. The liability is continuously reviewed and adjusted to reflect current remediation progress, prospective estimates of required activity, and other factors that may be relevant, including changes in technology or regulations.

Litigation Matters. For asserted claims and assessments, liabilities are recorded when an unfavorable outcome of a matter is deemed to be probable and the loss is reasonably estimable. Management determines the likelihood of an unfavorable outcome based on many factors such as the nature of the matter, available defenses and case strategy, progress of the matter, views and opinions of legal counsel and other advisors, applicability and success of appeals processes, and the outcome of similar historical matters, among others. Once an unfavorable outcome is deemed probable, management weighs the probability of estimated losses, and the most reasonable loss estimate is recorded. If an unfavorable outcome of a matter is deemed to be reasonably possible, then the matter is disclosed and no liability is recorded. With respect to unasserted claims or assessments, management must first determine that the probability that an assertion will be made is likely, then, a determination as to the likelihood of an unfavorable outcome and the ability to reasonably estimate the potential loss is made. Legal matters are reviewed on a continuous basis to determine if there has been a change in management s judgment regarding the likelihood of an unfavorable outcome or the estimate of a potential loss.

Asset Retirement Obligations. Alcoa recognizes asset retirement obligations (AROs) related to legal obligations associated with the normal operation of Alcoa s bauxite mining, alumina refining, and aluminum smelting facilities. These AROs consist primarily of costs associated with spent pot lining disposal, closure of bauxite residue areas, mine reclamation, and landfill closure. Alcoa also recognizes AROs for any significant lease restoration obligation, if required by a lease agreement, and for the disposal of regulated waste materials related to the demolition of certain power facilities. The fair values of these AROs are recorded on a discounted basis, at the time the obligation is incurred, and accreted over time for the change in present value. Additionally, Alcoa capitalizes asset retirement costs by increasing the carrying amount of the related long-lived assets and depreciating these assets over their remaining useful life.

Certain conditional asset retirement obligations (CAROs) related to alumina refineries, aluminum smelters, and fabrication facilities have not been recorded in the Consolidated Financial Statements due to uncertainties surrounding the ultimate settlement date. A CARO is a legal obligation to perform an asset retirement activity in which the timing and (or) method of settlement are conditional on a future event that may or may not be within Alcoa s control. Such uncertainties exist as a result of the perpetual nature of the structures, maintenance and upgrade programs, and other factors. At the date a reasonable estimate of the ultimate settlement date can be made, Alcoa would record an ARO for the removal, treatment, transportation, storage, and (or) disposal of various regulated assets and hazardous materials such as asbestos, underground and aboveground storage tanks, polychlorinated biphenyls (PCBs), various process residuals, solid wastes, electronic equipment waste, and various other materials. Such amounts may be material to the Consolidated Financial Statements in the period in which they are recorded.

Income Taxes. The provision for income taxes is determined using the asset and liability approach of accounting for income taxes. Under this approach, the provision for income taxes represents income taxes paid or payable (or received

or receivable) for the current year plus the change in deferred taxes during the year. Deferred taxes represent the future tax consequences expected to occur when the reported amounts of assets and liabilities are recovered or paid, and result from differences between the financial and tax bases of Alcoa s assets and liabilities and are adjusted for changes in tax rates and tax laws when enacted.

Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized. In evaluating the need for a valuation allowance, management considers all potential sources of taxable income, including income available in carryback periods, future reversals of taxable temporary differences, projections of taxable income, and income from tax planning strategies, as well as all available positive and negative evidence. Positive evidence includes factors such as a history of profitable operations, projections of future profitability within the carryforward period, including from tax planning strategies, and the Company s experience with similar operations. Existing favorable contracts and the ability to sell products into established markets are additional positive evidence. Negative evidence includes items such as cumulative losses, projections of future losses, or carryforward periods that are not long enough to allow for the utilization of a deferred tax asset based on existing projections of income. Deferred tax assets for which no valuation allowance is recorded may not be realized upon changes in facts and circumstances, resulting in a future charge to establish a valuation allowance.

Tax benefits related to uncertain tax positions taken or expected to be taken on a tax return are recorded when such benefits meet a more likely than not threshold. Otherwise, these tax benefits are recorded when a tax position has been effectively settled, which means that the statute of limitation has expired or the appropriate taxing authority has completed their examination even though the statute of limitations remains open. Interest and penalties related to uncertain tax positions are recognized as part of the provision for income taxes and are accrued beginning in the period that such interest and penalties would be applicable under relevant tax law until such time that the related tax benefits are recognized.

Stock-Based Compensation. Alcoa recognizes compensation expense for employee equity grants using the non-substantive vesting period approach, in which the expense (net of estimated forfeitures) is recognized ratably over the requisite service period based on the grant date fair value. The fair value of new stock options is estimated on the date of grant using a lattice-pricing model. Determining the fair value of stock options at the grant date requires judgment, including estimates for the average risk-free interest rate, dividend yield, volatility, annual forfeiture rate, and exercise behavior. These assumptions may differ significantly between grant dates because of changes in the actual results of these inputs that occur over time.

Most plan participants can choose whether to receive their award in the form of stock options, stock awards, or a combination of both. This choice is made before the grant is issued and is irrevocable.

Derivatives and Hedging. Derivatives are held for purposes other than trading and are part of a formally documented risk management program. For derivatives designated as fair value hedges, Alcoa measures hedge effectiveness by formally assessing, at least quarterly, the historical high correlation of changes in the fair value of the hedged item and the derivative hedging instrument. For derivatives designated as cash flow hedges, Alcoa measures hedge effectiveness by formally assessing, at least quarterly, the probable high correlation of the expected future cash flows of the hedged item and the derivative hedging instrument. The ineffective portions of both types of hedges are recorded in sales or other income or expense in the current period. If the hedging relationship ceases to be highly effective or it becomes probable that an expected transaction will no longer occur, future gains or losses on the derivative instrument are recorded in other income or expense.

Alcoa accounts for interest rate swaps related to its existing long-term debt and hedges of firm customer commitments for aluminum as fair value hedges. As a result, the fair values of the derivatives and changes in the fair values of the underlying hedged items are reported in other current and noncurrent assets and liabilities in the Consolidated Balance Sheet. Changes in the fair values of these derivatives and underlying hedged items generally offset and are recorded each period in sales or interest expense, consistent with the underlying hedged item.

Alcoa accounts for hedges of foreign currency exposures and certain forecasted transactions as cash flow hedges. The fair values of the derivatives are recorded in other current and noncurrent assets and liabilities in the Consolidated Balance Sheet. The effective portions of the changes in the fair values of these derivatives are recorded in other comprehensive income and are reclassified to sales, cost of goods sold, or other income or expense in the period in which earnings are impacted by the hedged items or in the period that the transaction no longer qualifies as a cash flow hedge. These contracts cover the same periods as known or expected exposures, generally not exceeding five years.

If no hedging relationship is designated, the derivative is marked to market through earnings.

Cash flows from derivatives are recognized in the Statement of Consolidated Cash Flows in a manner consistent with the underlying transactions.

Foreign Currency. The local currency is the functional currency for Alcoa s significant operations outside the U.S., except for certain operations in Canada, Russia and Iceland, where the U.S. dollar is used as the functional currency. The determination of the functional currency for Alcoa s operations is made based on the appropriate economic and management indicators.

Effective January 1, 2010, the functional currency of a subsidiary located in Brazil (that is part of Alcoa World Alumina and Chemicals, which is 60% owned by Alcoa and 40% owned by Alumina Limited) was changed from the U.S. dollar to the Brazilian real (BRL). This change was made as a result of changes in the operations of the business following the completion of the São Luís refinery expansion and Juruti bauxite mine development. In connection with this change, on January 1, 2010, an adjustment of $309 was recorded as an increase to the net nonmonetary assets of this subsidiary (primarily properties, plants, and equipment) with a corresponding adjustment to the foreign currency translation component of Accumulated other comprehensive loss. The functional currency of all of Alcoa s Brazilian operations is now BRL.

Acquisitions. Alcoa s business acquisitions are accounted for using the acquisition method. The purchase price is allocated to the assets acquired and liabilities assumed based on their estimated fair values. Any excess purchase price over the fair value of the net assets acquired is recorded as goodwill. For all acquisitions, operating results are included in the Statement of Consolidated Operations since the dates of the acquisitions.

Discontinued Operations and Assets Held For Sale. For those businesses where management has committed to a plan to divest, each business is valued at the lower of its carrying amount or estimated fair value less cost to sell. If the carrying amount of the business exceeds its estimated fair value, an impairment loss is recognized. Fair value is estimated using accepted valuation techniques such as a DCF model, valuations performed by third parties, earnings multiples, or indicative bids, when available. A number of significant estimates and assumptions are involved in the application of these techniques, including the forecasting of markets and market share, sales volumes and prices, costs and expenses, and multiple other factors. Management considers historical experience and all available information at the time the estimates are made; however, the fair value that is ultimately realized upon the divestiture of a business may differ from the estimated fair value reflected in the Consolidated Financial Statements. Depreciation, depletion, and amortization expense is not recorded on assets of a business to be divested once they are classified as held for sale. Businesses to be divested are classified in the Consolidated Financial Statements as either discontinued operations or held for sale.

For businesses classified as discontinued operations, the balance sheet amounts and results of operations are reclassified from their historical presentation to assets and liabilities of operations held for sale on the Consolidated Balance Sheet and to discontinued operations on the Statement of Consolidated Operations, respectively, for all periods presented. The gains or losses associated with these divested businesses are recorded in discontinued operations on the Statement of Consolidated Operations. The Statement of Consolidated Cash Flows is also reclassified for assets and liabilities of operations held for sale and discontinued operations for all periods presented. Additionally, segment information does not include the assets or operating results of businesses classified as discontinued operations for all

periods presented. Management does not expect any continuing involvement with these businesses following their divestiture, and these businesses are expected to be disposed of within one year.

For businesses classified as held for sale that do not qualify for discontinued operations treatment, the balance sheet and cash flow amounts are reclassified from their historical presentation to assets and liabilities of operations held for sale for all periods presented. The results of operations continue to be reported in continuing operations. The gains or losses associated with these divested businesses are recorded in restructuring and other charges on the Statement of Consolidated Operations. The segment information includes the assets and operating results of businesses classified as held for sale for all periods presented. Management expects that Alcoa will have continuing involvement with these businesses following their divestiture, primarily in the form of equity participation, or ongoing aluminum or other significant supply contracts.

Recently Adopted Accounting Guidance.

Fair Value Accounting On January 1, 2012, Alcoa adopted changes issued by the Financial Accounting Standards Board (FASB) to conform existing guidance regarding fair value measurement and disclosure between GAAP and International Financial Reporting Standards. These changes both clarify the FASB s intent about the application of existing fair value measurement and disclosure requirements and amend certain principles or requirements for measuring fair value or for disclosing information about fair value measurements. The clarifying changes relate to the application of the highest and best use and valuation premise concepts, measuring the fair value of an instrument classified in a reporting entity s shareholders equity, and disclosure of quantitative information about unobservable inputs used for Level 3 fair value measurements. The amendments relate to measuring the fair value of financial instruments that are managed within a portfolio; application of premiums and discounts in a fair value measurement; and additional disclosures concerning the valuation processes used and sensitivity of the fair value measurement to changes in unobservable inputs for those items categorized as Level 3, a reporting entity s use of a nonfinancial asset in a way that differs from the asset s highest and best use, and the categorization by level in the fair value hierarchy for items required to be measured at fair value for disclosure purposes only. Other than the additional disclosure requirements (see Note X), the adoption of these changes had no impact on the Consolidated Financial Statements.

On January 1, 2011, Alcoa adopted changes issued by the FASB to disclosure requirements for fair value measurements. Specifically, the changes require a reporting entity to disclose, in the reconciliation of fair value measurements using significant unobservable inputs (Level 3), separate information about purchases, sales, issuances, and settlements (that is, on a gross basis rather than as one net number). These changes were applied to the disclosures in Note W and the Derivatives section of Note X to the Consolidated Financial Statements.

Effective January 1, 2010, Alcoa adopted changes issued by the FASB on January 21, 2010 to disclosure requirements for fair value measurements. Specifically, the changes require a reporting entity to disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers. The changes also clarify existing disclosure requirements related to how assets and liabilities should be grouped by class and valuation techniques used for recurring and nonrecurring fair value measurements. The adoption of these changes had no impact on the Consolidated Financial Statements.

Business Combinations and Consolidation Accounting On January 1, 2011, Alcoa adopted changes issued by the FASB to the disclosure of pro forma information for business combinations. These changes clarify that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only. Also, the existing supplemental pro forma disclosures were expanded to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. The adoption of these changes had no impact on the Consolidated Financial Statements.

On January 1, 2010, Alcoa adopted changes issued by the FASB to accounting for variable interest entities. These changes require an enterprise to perform an analysis to determine whether the enterprise s variable interest or interests

give it a controlling financial interest in a variable interest entity; to require ongoing reassessments of whether an enterprise is the primary beneficiary of a variable interest entity; to eliminate the solely quantitative approach previously required for determining the primary beneficiary of a variable interest entity; to add an additional reconsideration event for determining whether an entity is a variable interest entity when any changes in facts and circumstances occur such that holders of the equity investment at risk, as a group, lose the power from voting rights or similar rights of those investments to direct the activities of the entity that most significantly impact the entity s economic performance; and to require enhanced disclosures that will provide users of financial statements with more transparent information about an enterprise s involvement in a variable interest entity. The adoption of these changes had no impact on the Consolidated Financial Statements.

Effective January 1, 2010, Alcoa adopted changes issued by the FASB on January 6, 2010 for a scope clarification to the FASB s previously-issued guidance (in December 2007) on accounting for noncontrolling interests in consolidated financial statements. These changes clarify the accounting and reporting guidance for noncontrolling interests and changes in ownership interests of a consolidated subsidiary. An entity is required to deconsolidate a subsidiary when the entity ceases to have a controlling financial interest in the subsidiary. Upon deconsolidation of a subsidiary, an entity recognizes a gain or loss on the transaction and measures any retained investment in the subsidiary at fair value. The gain or loss includes any gain or loss associated with the difference between the fair value of the retained investment in the subsidiary and its carrying amount at the date the subsidiary is deconsolidated. In contrast, an entity is required to account for a decrease in its ownership interest of a subsidiary that does not result in a change of control of the subsidiary as an equity transaction. The adoption of these changes had no impact on the Consolidated Financial Statements.

Goodwill and Other Intangible Assets On January 1, 2011, Alcoa adopted changes issued by the FASB to the testing of goodwill for impairment. These changes require an entity to perform all steps in the test for a reporting unit whose carrying value is zero or negative if it is more likely than not (more than 50%) that a goodwill impairment exists based on qualitative factors. This will result in the elimination of an entity s ability to assert that such a reporting unit s goodwill is not impaired and additional testing is not necessary despite the existence of qualitative factors that indicate otherwise. Based on the then most recent impairment review of Alcoa s goodwill (2011 fourth quarter), the adoption of these changes had no impact on the Consolidated Financial Statements.

In September 2011, the FASB issued changes to the testing of goodwill for impairment. These changes provide an entity the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not (more than 50%) that the fair value of a reporting unit is less than its carrying amount. Such qualitative factors may include the following: macroeconomic conditions; industry and market considerations; cost factors; overall financial performance; and other relevant entity-specific events. If an entity elects to perform a qualitative assessment and determines that an impairment is more likely than not, the entity is then required to perform the existing two-step quantitative impairment test, otherwise no further analysis is required. An entity also may elect not to perform the qualitative assessment and, instead, proceed directly to the two-step quantitative impairment test. Under either option, the ultimate outcome of the goodwill impairment test should be the same. These changes are required to become effective for Alcoa for any goodwill impairment test performed on January 1, 2012 or later; however, early adoption is permitted. Alcoa elected to early adopt these changes in conjunction with management s annual review of goodwill in the fourth quarter of 2011 (see the Goodwill and Other Intangible Assets section of Note A above). The adoption of these changes had no impact on the Consolidated Financial Statements.

Other On January 1, 2012, Alcoa adopted changes issued by the FASB to the presentation of comprehensive income. These changes give an entity the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements; the option to present components of other comprehensive income as part of the statement of changes in stockholders equity was eliminated. The items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income were not changed. Additionally, no changes were made to the calculation and presentation of earnings per share. Management elected to present the two-statement option. Other than the change in presentation, the adoption of these changes had no impact on the Consolidated Financial Statements.

On January 1, 2011, Alcoa adopted changes issued by the FASB to revenue recognition for multiple-deliverable arrangements. These changes require separation of consideration received in such arrangements by establishing a selling price hierarchy (not the same as fair value) for determining the selling price of a deliverable, which will be based on available information in the following order: vendor-specific objective evidence, third-party evidence, or estimated selling price; eliminate the residual method of allocation and require that the consideration be allocated at the inception of the arrangement to all deliverables using the relative selling price method, which allocates any discount in the arrangement to each deliverable on the basis of each deliverable s selling price; require that a vendor determine its best estimate of selling price in a manner that is consistent with that used to determine the price to sell the deliverable on a standalone basis; and expand the disclosures related to multiple-deliverable revenue arrangements. The adoption of these changes had no impact on the Consolidated Financial Statements, as Alcoa does not currently have any such arrangements with its customers.

On January 1, 2011, Alcoa adopted changes issued by the FASB to the classification of certain employee share-based payment awards. These changes clarify that there is not an indication of a condition that is other than market, performance, or service if an employee share-based payment award s exercise price is denominated in the currency of a market in which a substantial portion of the entity s equity securities trade and differs from the functional currency of the employer entity or payroll currency of the employee. An employee share-based payment award is required to be classified as a liability if the award does not contain a market, performance, or service condition. Prior to this guidance, the difference between the currency denomination of an employee share-based payment award s exercise price and the functional currency of the employer entity or payroll currency of the employee was not a factor considered by management when determining the proper classification of a share-based payment award. The adoption of these changes had no impact on the Consolidated Financial Statements.

On January 1, 2010, Alcoa adopted changes issued by the FASB to accounting for transfers of financial assets. These changes remove the concept of a qualifying special-purpose entity and remove the exception from the application of variable interest accounting to variable interest entities that are qualifying special-purpose entities; limit the circumstances in which a transferor derecognizes a portion or component of a financial asset; define a participating interest; require a transferor to recognize and initially measure at fair value all assets obtained and liabilities incurred as a result of a transfer accounted for as a sale; and require enhanced disclosure. The adoption of these changes had no impact on the Consolidated Financial Statements. In March 2010, management terminated the Company s accounts receivable securitization program; had this program not been terminated, the adoption of these changes would have resulted in a $250 increase to both Receivables from customers and Short-term borrowings on the accompanying Consolidated Balance Sheet.

Effective January 1, 2010, Alcoa adopted changes issued by the FASB on February 24, 2010 to accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or available to be issued, otherwise known as subsequent events. Specifically, these changes clarify that an entity that is required to file or furnish its financial statements with the Securities and Exchange Commission is not required to disclose the date through which subsequent events have been evaluated, as had been previously required by changes issued by the FASB in May 2009. Other than the elimination of disclosing the date through which management has performed its evaluation for subsequent events (see Note Y), the adoption of these changes had no impact on the Consolidated Financial Statements.

On July 1, 2010, Alcoa adopted changes to existing accounting requirements for embedded credit derivatives. Specifically, the changes clarify the scope exception regarding when embedded credit derivative features are not considered embedded derivatives subject to potential bifurcation and separate accounting. The adoption of these changes had no impact on the Consolidated Financial Statements.

Recently Issued Accounting Guidance. In July 2012, the FASB issued changes to the testing of indefinite-lived intangible assets for impairment, similar to the goodwill changes issued in September 2011. These changes provide an entity the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not (more than 50%) that the fair value of an indefinite-lived intangible asset is less than its carrying amount. Such qualitative factors may include the following: macroeconomic conditions; industry and

market considerations; cost factors; overall financial performance; and other relevant entity-specific events. If an entity elects to perform a qualitative assessment and determines that an impairment is more likely than not, the entity is then required to perform the existing two-step quantitative impairment test, otherwise no further analysis is required. An entity also may elect not to perform the qualitative assessment and, instead, proceed directly to the two-step quantitative impairment test. These changes become effective for Alcoa for any indefinite-lived intangible asset impairment test performed on January 1, 2013 or later, although early adoption is permitted. Upon adoption of these changes, management plans to proceed directly to the two-step quantitative test for Alcoa s indefinite-lived intangible assets. As these changes should not affect the outcome of the impairment analysis of an indefinite-lived intangible asset, management has determined these changes will not have an impact on the Consolidated Financial Statements.

In December 2011, the FASB issued changes to the disclosure of offsetting assets and liabilities. These changes require an entity to disclose both gross information and net information about both instruments and transactions eligible for offset in the statement of financial position and instruments and transactions subject to an agreement similar to a master netting arrangement. The enhanced disclosures will enable users of an entity s financial statements to understand and evaluate the effect or potential effect of master netting arrangements on an entity s financial position, including the effect or potential effect of rights of setoff associated with certain financial instruments and derivative instruments. These changes become effective for Alcoa on January 1, 2013. Other than the additional disclosure requirements, management has determined that the adoption of these changes will not have an impact on the Consolidated Financial Statements.

B. Discontinued Operations and Assets Held for Sale

For the years ended December 31, 2012, 2011, and 2010, there were no active businesses classified as discontinued operations in the accompanying Statement of Consolidated Operations.

The following table details selected financial information of discontinued operations:

	2012	2011	2010
Sales	$ -	$ -	$ -
Loss from operations before income taxes	$ -	$ (4)	$ (11)
Benefit for income taxes	-	1	3
Loss from discontinued operations	$ -	$ (3)	$ (8)

In 2011, discontinued operations included an additional loss of $3 ($5 pretax) related to the wire harness and electrical portion (divested in June 2009) of the Electrical and Electronic Solutions (EES) business as a result of a negotiated preliminary settlement related to claims filed in 2010 against Alcoa by Platinum Equity in an insolvency proceeding in Germany, a net gain of $2 ($3 pretax) related to both the wire harness and electrical portion and the electronics portion (divested in December 2009) of the EES business for a number of small post-closing and other adjustments, and a $2 ($2 pretax) reversal of the gain recognized in 2006 related to the sale of the home exteriors business for an adjustment to an outstanding obligation, which was part of the terms of sale. In 2010, discontinued operations included an additional loss of $6 ($9 pretax) related to the wire harness and electrical portion of the EES business as a result of a contract settlement with a former customer of this business and an additional loss of $2 ($4 pretax) related to the electronics portion of the EES business for the settling of working capital, which was not included in the divestiture transaction.

For both periods presented in the accompanying Consolidated Balance Sheet, the assets and liabilities of operations classified as held for sale included the electronics portion of the EES business (working capital components) and the Hawesville, KY automotive casting facility. Additionally, assets of the Tapoco Hydroelectric Project (Tapoco), along with an allocation of goodwill from the Primary Metals reporting unit, were classified as held for sale as of December 31, 2011.

In June 2012, management committed to a plan to sell the assets, consisting of properties, plants, and equipment and intangible assets, of Tapoco. As a result, these assets were reclassified to held for sale. The Consolidated Financial Statements for all prior periods presented were reclassified to reflect this change. In November 2012, Alcoa completed the sale of Tapoco (see Note F).

The major classes of assets and liabilities of operations held for sale were as follows:

December 31,	2012	2011
Assets:		
Properties, plants, and equipment	$ 2	$ 136
Goodwill	-	94
Other assets	-	13
Assets held for sale*	$ 2	$ 243
Liabilities:		
Accounts payable, trade	$ -	$ 1
Accrued expenses	1	5
Liabilities of operations held for sale*	$ 1	$ 6

* Assets held for sale were included in Other noncurrent assets and Liabilities of operations held for sale were included in Other noncurrent liabilities and deferred credits on the accompanying Consolidated Balance Sheet.

C. Asset Retirement Obligations

Alcoa has recorded AROs related to legal obligations associated with the normal operations of bauxite mining, alumina refining, and aluminum smelting facilities. These AROs consist primarily of costs associated with spent pot lining disposal, closure of bauxite residue areas, mine reclamation, and landfill closure. Alcoa also recognizes AROs for any significant lease restoration obligation, if required by a lease agreement, and for the disposal of regulated waste materials related to the demolition of certain power facilities.

In addition to AROs, certain CAROs related to alumina refineries, aluminum smelters, and fabrication facilities have not been recorded in the Consolidated Financial Statements due to uncertainties surrounding the ultimate settlement date. Such uncertainties exist as a result of the perpetual nature of the structures, maintenance and upgrade programs, and other factors. At the date a reasonable estimate of the ultimate settlement date can be made (e.g., planned demolition), Alcoa would record an ARO for the removal, treatment, transportation, storage, and (or) disposal of various regulated assets and hazardous materials such as asbestos, underground and aboveground storage tanks, PCBs, various process residuals, solid wastes, electronic equipment waste, and various other materials. If Alcoa was required to demolish all such structures immediately, the estimated CARO as of December 31, 2012 ranges from less than $1 to $52 per structure (132 structures) in today s dollars.

The following table details the carrying value of recorded AROs by major category (of which $75 and $76 was classified as a current liability as of December 31, 2012 and 2011, respectively):

December 31,	2012	2011
Spent pot lining disposal	$ 182	$ 187
Closure of bauxite residue areas	190	173
Mine reclamation	189	164
Demolition*	28	34
Landfill closure	17	17
Other	4	4
	$ 610	$ 579

* In 2011, AROs were recorded as a result of management s decision to permanently shut down and demolish certain structures, each of which was previously temporarily idled for different reasons (see Note D).

The following table details the changes in the total carrying value of recorded AROs:

December 31,	2012	2011
Balance at beginning of year	$ 579	$ 534
Accretion expense	25	22
Payments	(81)	(86)
Liabilities incurred	80	115
Foreign currency translation and other	7	(6)
Balance at end of year	$ 610	$ 579

D. Restructuring and Other Charges

Restructuring and other charges for each year in the three-year period ended December 31, 2012 were comprised of the following:

	2012	2011	2010
Asset impairments	$ 40	$ 150	$ 139
Layoff costs	47	93	43
Other exit costs	21	61	58
Reversals of previously recorded layoff and other exit costs	(21)	(23)	(33)
Restructuring and other charges	$ 87	$ 281	$ 207

Layoff costs were recorded based on approved detailed action plans submitted by the operating locations that specified positions to be eliminated, benefits to be paid under existing severance plans, union contracts or statutory requirements, and the expected timetable for completion of the plans.

2012 Actions. In 2012, Alcoa recorded Restructuring and other charges of $87 ($73 after-tax and noncontrolling interests), which were comprised of the following components: $47 ($29 after-tax and noncontrolling interests) for the layoff of approximately 800 employees (390 in the Engineered Products and Solutions segment, 250 in the Primary Metals segment, 85 in the Alumina segment, and 75 in Corporate), including $10 ($7 after-tax) for the layoff of an additional 170 employees related to the previously reported smelter curtailments in Spain (see 2011 Actions below); $30 ($30 after-tax) in asset impairments and $6 ($6 after-tax) for lease and contract termination costs due to a decision to exit the lithographic sheet business in Bohai, China; $11 ($11 after-tax) in costs to idle the Portovesme smelter (see 2011 Actions below); $10 ($8 after-tax) in other asset impairments; a net charge of $4 ($4 after-tax and noncontrolling interests) for other miscellaneous items; and $21 ($15 after-tax and noncontrolling interests) for the reversal of a number of layoff reserves related to prior periods, including $10 ($7 after-tax) related to the smelters in Spain. The reversal related to the smelters in Spain is due to lower than expected costs based on agreements with employee representatives and the government, as well as a reduction of 55 in the number of layoffs due to the anticipation of the restart of a portion of the previously curtailed capacity based on an agreement with the Spanish government that will provide interruptibility rights (i.e. compensation for power interruptions when grids are overloaded) to the smelters during 2013. A portion of this reversal relates to layoff costs recorded at the end of 2011 (see 2011 Actions below) and a portion of this reversal relates to layoff costs recorded during 2012 (see above).

As of December 31, 2012, approximately 270 of the 800 employees were separated. The remaining separations for the 2012 restructuring programs are expected to be completed by the end of 2013. In 2012, cash payments of $16 were made against layoff reserves related to the 2012 restructuring programs.

2011 Actions. In 2011, Alcoa recorded Restructuring and other charges of $281 ($181 after-tax and noncontrolling interests), which were comprised of the following components: $127 ($82 after-tax) in asset impairments and $36 ($23 after-tax) in other exit costs related to the permanent shutdown and planned demolition of certain idled structures at two U.S. locations (see below); $93 ($68 after-tax and noncontrolling interests) for the layoff of approximately 1,600 employees (820 in the Primary Metals segment, 470 in the Global Rolled Products segment, 160 in the Alumina

segment, 20 in the Engineered Products and Solutions segment, and 130 in Corporate), including the effects of planned smelter curtailments (see below); $23 ($12 after-tax and noncontrolling interests) for other asset impairments, including the write-off of the carrying value of an idled structure in Australia that processed spent pot lining and adjustments to the fair value of the one remaining foil location while it was classified as held for sale due to foreign currency movements; $20 ($8 after-tax and noncontrolling interests) for a litigation matter related to the former St. Croix location (see the Litigation section of Note N); a net charge of $5 ($4 after-tax) for other small items; and $23 ($16 after-tax) for the reversal of previously recorded layoff reserves due to normal attrition and changes in facts and circumstances, including a change in plans for Alcoa s aluminum powder facility in Rockdale, TX.

In late 2011, management approved the permanent shutdown and demolition of certain facilities at two U.S. locations, each of which was previously temporarily idled for various reasons. The identified facilities are the smelter located in Alcoa, TN (capacity of 215 kmt-per-year) and two potlines (capacity of 76 kmt-per-year) at the smelter located in Rockdale, TX (remaining capacity of 191 kmt-per-year composed of four potlines). Demolition and remediation activities related to these actions began in 2012 and are expected to be completed in 2015 for the Tennessee smelter and in 2013 for the two potlines at the Rockdale smelter. This decision was made after a comprehensive strategic analysis was performed to determine the best course of action for each facility. Factors leading to this decision were in general focused on achieving sustained competitiveness and included, among others: lack of an economically viable, long-term power solution; changed market fundamentals; cost competitiveness; required future capital investment; and restart costs. The asset impairments of $127 represent the write off of the remaining book value of properties, plants, and equipment related to these facilities. Additionally, remaining inventories, mostly operating supplies, were written down to their net realizable value resulting in a charge of $6 ($4 after-tax), which was recorded in Cost of goods sold on the accompanying Statement of Consolidated Operations. The other exit costs of $36 represent $18 ($11 after-tax) in environmental remediation (see Note N) and $17 ($11 after-tax) in asset retirement obligations (see Note C), both triggered by the decision to permanently shut down and demolish these structures, and $1 ($1 after-tax) in other related costs.

Also, at the end of 2011, management approved a partial or full curtailment of three European smelters as follows: Portovesme, Italy (150 kmt-per-year); Avilés, Spain (46 kmt out of 93 kmt-per-year); and La Coruña, Spain (44 kmt out of 87 kmt-per-year). These curtailments were completed by the end of 2012. The curtailment of the Portovesme smelter may lead to the permanent closure of the facility, which would result in future charges, while the curtailments at the two smelters in Spain are planned to be temporary. These actions were the result of uncompetitive energy positions, combined with rising material costs and falling aluminum prices (mid-2011 to late 2011). As a result of these decisions, Alcoa recorded costs of $33 ($31 after-tax) for the layoff of approximately 650 employees. As Alcoa engaged in discussions with the respective employee representatives and governments, additional charges were recognized in 2012 (see 2012 Actions above).

As of December 31, 2012, approximately 895 of the 1,475 employees were separated. The total number of employees associated with the 2011 restructuring programs was updated to reflect changes in plans (agreement related to the smelters in Spain see 2012 Actions above), better than expected operating performance at certain locations, and natural attrition. The remaining separations for the 2011 restructuring programs are expected to be completed by the end of 2013. In 2012 and 2011, cash payments of $23 and $24, respectively, were made against layoff reserves related to the 2011 restructuring programs.

2010 Actions. In 2010, Alcoa recorded Restructuring and other charges of $207 ($130 after-tax and noncontrolling interests), which were comprised of the following components: $127 ($80 after-tax and noncontrolling interests) in asset impairments and $46 ($29 after-tax and noncontrolling interests) in other exit costs related to the permanent shutdown and planned demolition of certain idled structures at five U.S. locations (see below); $43 ($29 after-tax and noncontrolling interests) for the layoff of approximately 875 employees (625 in the Engineered Products and Solutions segment; 75 in the Primary Metals segment; 60 in the Alumina segment; 25 in the Global Rolled Products segment; and 90 in Corporate); $22 ($14 after-tax) in net charges (including $12 ($8 after-tax) for asset impairments) related to divested and to be divested businesses (Automotive Castings, Global Foil, Transportation Products Europe, and Packaging and Consumer) for, among other items, the settlement of a contract with a former customer, foreign currency movements, working capital adjustments, and a tax indemnification; $2 ($2 after-tax and noncontrolling interests) for various other exit costs; and $33 ($24 after-tax and noncontrolling interests) for the reversal of prior

periods layoff reserves, including a portion of those related to the Portovesme smelter in Italy due to the execution of a new power agreement (see the European Commission Matters section of Note N).

In early 2010, management approved the permanent shutdown and demolition of the following structures, each of which was previously temporarily idled for different reasons: the Eastalco smelter located in Frederick, MD (capacity of 195 kmt-per-year); the smelter located in Badin, NC (capacity of 60 kmt-per-year); an aluminum fluoride plant in Point Comfort, TX; a paste plant and cast house in Massena, NY; and one potline at the smelter in Warrick, IN (capacity of 40 kmt-per-year). This decision was made after a comprehensive strategic analysis was performed to determine the best course of action for each facility. Factors leading to this decision included current market fundamentals, cost competitiveness, other existing idle capacity, required future capital investment, and restart costs, as well as the elimination of ongoing holding costs. The asset impairments of $127 represent the write off of the remaining book value of properties, plants, and equipment related to these facilities. Additionally, remaining inventories, mostly operating supplies, were written down to their net realizable value resulting in a charge of $8 ($5 after-tax and noncontrolling interests), which was recorded in Cost of goods sold on the accompanying Statement of Consolidated Operations. The other exit costs of $46 represent $30 ($19 after-tax and noncontrolling interests) in asset retirement obligations and $14 ($9 after-tax) in environmental remediation, both triggered by the decision to permanently shut down and demolish these structures, and $2 ($1 after-tax and noncontrolling interests) in other related costs.

As of December 31, 2012, the separations associated with 2010 restructuring programs were essentially complete. In 2012 and 2011, cash payments of $3 and $7, respectively, were made against layoff reserves related to 2010 restructuring programs.

Alcoa does not include Restructuring and other charges in the results of its reportable segments. The pretax impact of allocating such charges to segment results would have been as follows:

	2012	2011	2010
Alumina	$ 3	$ 39	$ 12
Primary Metals	20	212	145
Global Rolled Products	43	19	(11)
Engineered Products and Solutions	13	(3)	18
Segment total	79	267	164
Corporate	8	14	43
Total restructuring and other charges	$ 87	$ 281	$ 207

Activity and reserve balances for restructuring charges were as follows:

	Layoff costs	Other exit costs	Total
Reserve balances at December 31, 2009	$ 160	$ 66	$ 226
2010:			
Cash payments	(93)	(15)	(108)
Restructuring charges	43	53	96
Other*	(57)	(41)	(98)
Reserve balances at December 31, 2010	53	63	116
2011:			
Cash payments	(45)	(9)	(54)
Restructuring charges	93	37	130
Other*	(24)	(34)	(58)
Reserve balances at December 31, 2011	77	57	134
2012:			
Cash payments	(44)	(13)	(57)
Restructuring charges	47	13	60
Other*	(21)	(5)	(26)
Reserve balances at December 31, 2012	$ 59	$ 52	$ 111

* Other includes reversals of previously recorded restructuring charges and the effects of foreign currency translation. In 2011, Other for other exit costs also included a reclassification of the following restructuring charges: $18 in environmental and $17 in asset retirement obligations, as these liabilities are included in Alcoa s separate reserves for environmental remediation (see Note N) and asset retirement obligations (see Note C), respectively. In 2010, Other for other exit costs also included a reclassification of the following restructuring charges: $30 in asset retirement and $14 in environmental obligations, as these liabilities are included in Alcoa s separate reserves for asset retirement obligations and environmental remediation, respectively.

The remaining reserves are expected to be paid in cash during 2013, with the exception of approximately $50 to $55, which is expected to be paid over the next several years for lease termination costs, special separation benefit payments, and ongoing site remediation work.

E. Goodwill and Other Intangible Assets

The following table details the changes in the carrying amount of goodwill:

	Alumina	Primary Metals	Global Rolled Products	Engineered Products and Solutions	Corporate*	Total
Balance at December 31, 2010:						
Goodwill	$ 12	$ 993	$ 207	$ 2,551	$ 1,293	$ 5,056
Accumulated impairment losses	-	-	-	(28)	-	(28)
	12	993	207	2,523	1,293	5,028
Acquisition of businesses	-	-	-	150	-	150
Translation	(1)	(2)	1	(7)	(12)	(21)
Balance at December 31, 2011:						
Goodwill	11	991	208	2,694	1,281	5,185
Accumulated impairment losses	-	-	-	(28)	-	(28)
	11	991	208	2,666	1,281	5,157
Acquisition of businesses	-	-	-	(1)	-	(1)
Translation	(1)	6	6	12	(9)	14
Balance at December 31, 2012:						
Goodwill	10	997	214	2,705	1,272	5,198
Accumulated impairment losses	-	-	-	(28)	-	(28)
	$ 10	$ 997	$ 214	$ 2,677	$ 1,272	$ 5,170

* As of December 31, 2012, $1,247 of the amount reflected in Corporate is allocated to each of Alcoa s four reportable segments ($161 to Alumina, $751 to Primary Metals, $62 to Global Rolled Products, and $273 to Engineered Products and Solutions) included in the table above for purposes of impairment testing (see Note A). This goodwill is reflected in Corporate for segment reporting purposes because it is not included in management s assessment of performance by the four reportable segments.

Other intangible assets, which are included in Other noncurrent assets on the accompanying Consolidated Balance Sheet, were as follows:

December 31, 2012	Gross carrying amount	Accumulated amortization
Computer software	$ 907	$ (664)
Patents and licenses	133	(88)
Other intangibles	101	(28)
Total amortizable intangible assets	1,141	(780)
Indefinite-lived trade names and trademarks	46	-
Total other intangible assets	$ 1,187	$ (780)

December 31, 2011	Gross carrying amount	Accumulated amortization
Computer software	$ 902	$ (595)
Patents and licenses	133	(83)
Other intangibles*	101	(23)
Total amortizable intangible assets	1,136	(701)
Indefinite-lived trade names and trademarks*	46	-
Total other intangible assets	$ 1,182	$ (701)

* In 2011, customer relationships were identified as an intangible asset ($31) related to the acquisition of an aerospace fastener business (see Note F) and were preliminarily classified as indefinite-lived in the table above. Upon the completion of the final valuation in 2012, it was determined that the customer relationships should have a finite life. As a result, the 2011 gross carrying amounts for indefinite-lived intangible assets and other intangible assets were revised to conform to the 2012 presentation.

Computer software consists primarily of software costs associated with an enterprise business solution (EBS) within Alcoa to drive common systems among all businesses.

Amortization expense related to the intangible assets in the tables above for the years ended December 31, 2012, 2011, and 2010 was $82, $86, and $86, respectively, and is expected to be in the range of approximately $80 to $90 annually from 2013 to 2017.

F. Acquisitions and Divestitures

Pro forma results of the Company, assuming all acquisitions described below were made at the beginning of the earliest prior period presented, would not have been materially different from the results reported.

2012 Divestitures. In November 2012, Alcoa completed the sale of its 351-megawatt Tapoco Hydroelectric Project (Tapoco) to Brookfield Renewable Energy Partners for $597 in cash. Alcoa recognized a gain of $320 ($173 after-tax) in Other income, net on the accompanying Statement of Consolidated Operations, of which a gain of $426 ($275 after-tax) was reflected in the Primary Metals segment and a loss of $106 ($102 after-tax) was reflected in Corporate. The amount in Corporate represents the write-off of goodwill and capitalized interest related to Tapoco that were not included in the assets of the Primary Metals segment. This transaction is subject to certain post-closing adjustments as defined in the purchase agreement. Tapoco is a four-station hydroelectric project located on the Little Tennessee and Cheoah Rivers in eastern Tennessee and western North Carolina. The transaction included four generating stations and dams, 86 miles of transmission lines, and approximately 14,500 acres of land associated with and surrounding Tapoco. The power generated by Tapoco was primarily consumed by Alcoa s smelter in Tennessee, which was temporarily idled in 2009 and permanently shut down in 2011. Since 2009, the power generated from Tapoco was sold into the

open market. Prior to November 2012, the carrying value of the assets sold, which consisted of properties, plants, and equipment and intangible assets, along with an allocation of goodwill ($94) from the Primary Metals reporting unit, were classified as held for sale (see Note B).

2011 Acquisitions. On March 9, 2011, Alcoa completed an acquisition of the aerospace fastener business of TransDigm Group Inc. for $240 (cash acquired and post-closing adjustments resulted in a net purchase price of $239). This business is a leading global designer, producer, and supplier of highly engineered aircraft components, with three locations (one in the state of California and two in the United Kingdom) that employ a combined 400 people. Specifically, this business provides a wide variety of high-strength, high temperature nickel alloy specialty engine fasteners, airframe bolts, and slotted entry bearings. In 2010, this business generated sales of $61. The assets and liabilities of this business were included in the Engineered Products and Solutions segment as of March 31, 2011; this business results of operations were included in this segment beginning March 9, 2011. Based on the preliminary purchase price allocation, goodwill of $154 was recorded for this transaction. In 2012, the purchase price allocation was finalized based on the completion of a valuation study resulting in a $1 reduction of the initial goodwill amount. Approximately $60 of goodwill is deductible for income tax purposes. No other intangible assets were identified as a result of the final valuation. This transaction is no longer subject to post-closing adjustments. This acquisition is part of a strategic plan to accelerate the growth of Alcoa s fastener business, while adding efficiencies, broadening the existing technology base, and expanding product offerings to better serve customers and increase shareholder value.

2010 Acquisitions. In July 2010, Alcoa completed an acquisition of the commercial building and construction business of a privately-held company, Traco, for $77. This business, located in Cranberry, Pennsylvania, employing 650 people, is a premier manufacturer of windows and doors for the commercial building and construction market and generated sales of approximately $100 in 2009. The assets and liabilities of this business were included in the Engineered Products and Solutions segment as of the end of July 2010 and this business results of operations were included in this segment since the beginning of August 2010. Based on the preliminary purchase price allocation, goodwill of $28 was recorded for this transaction. In 2011, the purchase price allocation was finalized based on the completion of a valuation study resulting in a reduction in the initial goodwill amount of $4. All of the $24 in goodwill is deductible for income tax purposes. Also in 2011, Alcoa paid an additional $1 to settle working capital, as provided for in the acquisition agreement, reflecting an adjustment to the purchase price. This transaction is no longer subject to post-closing adjustments.

2010 Divestitures. In April 2010, Alcoa completed the divestiture of the Transportation Products Europe business, the assets and liabilities of which were classified as held for sale in 2008, to two separate buyers. Combined, this business sold for $14, which was included in Proceeds from the sale of assets and businesses on the accompanying Statement of Consolidated Cash Flows; a gain of $5 ($5 after-tax) was recognized in Restructuring and other charges on the accompanying Statement of Consolidated Operations. These two transactions are no longer subject to post-closing adjustments. This business generated sales of $78 in 2009 and, at the time of divestiture, had approximately 360 employees at three locations.

Contingent Payments. In connection with the 2005 acquisition of two fabricating facilities in Russia, Alcoa could be required to make contingent payments of approximately $50 through 2015 based upon the achievement of various financial and operating targets. Any such payment would be reflected as additional goodwill.

G. Inventories

December 31,	**2012**	**2011**
Finished goods	$ 542	$ 537
Work-in-process	866	911
Bauxite and alumina	618	656
Purchased raw materials	536	532
Operating supplies	263	263
	$ 2,825	$ 2,899

At December 31, 2012 and 2011, the total amount of inventories valued on a LIFO basis was 35%. If valued on an average-cost basis, total inventories would have been $770 and $801 higher at December 31, 2012 and 2011, respectively. During the three-year period ended December 31, 2012, reductions in LIFO inventory quantities caused partial liquidations of the lower cost LIFO inventory base. These liquidations resulted in the recognition of income of $1 ($1 after-tax) in 2012, $2 ($1 after-tax) in 2011, and $27 ($17 after-tax) in 2010.

H. Properties, Plants, and Equipment, Net

December 31,	2012	2011
Land and land rights, including mines	$ 676	$ 665
Structures:		
Alumina:		
Alumina refining	3,319	3,280
Bauxite mining	1,563	1,597
Primary Metals:		
Aluminum smelting	4,042	3,950
Power generation	604	667
Global Rolled Products	1,232	1,204
Engineered Products and Solutions	678	648
Other	760	714
	12,198	12,060
Machinery and equipment:		
Alumina:		
Alumina refining	5,279	5,223
Bauxite mining	650	661
Primary Metals:		
Aluminum smelting	8,114	8,266
Power generation	994	1,012
Global Rolled Products	5,174	5,059
Engineered Products and Solutions	2,415	2,252
Other	883	764
	23,509	23,237
	36,383	35,962
Less: accumulated depreciation, depletion, and amortization	19,190	18,326
	17,193	17,636
Construction work-in-progress	1,754	1,646
	$ 18,947	$ 19,282

As of December 31, 2012 and 2011, the net carrying value of temporarily idled smelting assets was $325 and $166, representing 591 kmt and 353 kmt of idle capacity, respectively. Additionally, the net carrying value of permanently idled smelting assets, representing 291 kmt, was written off at the end of 2011 (see Note D). Also, the net carrying value of temporarily idled refining assets was $68 and $65 as of December 31, 2012 and 2011, representing 1,277 and 1,177 kmt of idle capacity, respectively.

I. Investments

December 31,	2012	2011
Equity investments	$ 1,782	$ 1,524
Other investments	78	102
	$ 1,860	$ 1,626

Equity Investments. As of December 31, 2012 and 2011, Equity investments included an interest in a project to develop a fully-integrated aluminum complex in Saudi Arabia (see below), hydroelectric power projects in Brazil (see Note N), a smelter operation in Canada (50% of Pechiney Reynolds Quebec, Inc.), bauxite mining interests in Guinea (45% of Halco Mining, Inc.) and Brazil (18.2% of Mineração Rio do Norte S.A.), and a natural gas pipeline in Australia (see Note N). Pechiney Reynolds Quebec, Inc. owns a 50.1% interest in the Bécancour smelter in Quebec, Canada thereby entitling Alcoa to a 25.05% interest in the smelter. Through two wholly-owned Canadian subsidiaries, Alcoa also owns 49.9% of the Bécancour smelter. Halco Mining, Inc. owns 100% of Boké Investment Company, which owns 51% of Compagnie des Bauxites de Guinée. The investments in the bauxite mining interests in Guinea and Brazil and the natural gas pipeline in Australia are held by wholly-owned subsidiaries of Alcoa World Alumina and Chemicals (AWAC), which is owned 60% by Alcoa and 40% by Alumina Limited. In 2012, 2011, and 2010, Alcoa received $101, $100, and $33, respectively, in dividends from its equity investments.

Alcoa and Saudi Arabian Mining Company (known as Ma aden) have a 30-year joint venture shareholders agreement (automatic extension for an additional 20 years, unless the parties agree otherwise or unless earlier terminated) setting forth the terms for the development, construction, ownership, and operation of an integrated bauxite mine, alumina refinery, aluminum smelter, and rolling mill, in Saudi Arabia. Specifically, the project to be developed by the joint venture will consist of: (i) a bauxite mine for the extraction of approximately 4,000 kmt of bauxite from the Al Ba itha bauxite deposit near Quiba in the northern part of Saudi Arabia; (ii) an alumina refinery with an initial capacity of 1,800 kmt; (iii) a primary aluminum smelter with an initial capacity of 740 kmt; and (iv) a rolling mill with an initial capacity of 380 kmt. The refinery, smelter, and rolling mill are being constructed in an industrial area at Ras Al Khair (formerly Ras Az Zawr) on the east coast of Saudi Arabia. The facilities will use critical infrastructure, including power generation derived from reserves of natural gas, as well as port and rail facilities, developed by the government of Saudi Arabia. First production from the smelter occurred in December 2012. For the rolling mill and mine and refinery, first production is expected in 2013 and 2014, respectively.

In 2012, Alcoa and Ma aden agreed to expand the capabilities of the rolling mill to include a capacity of 100 kmt dedicated to supplying aluminum automotive, building and construction, and foil stock sheet. First production related to the expanded capacity is expected in 2014. This expansion is not expected to result in additional equity investment (see below) due to significant savings anticipated from a change in the project execution strategy of the initial 380 kmt capacity of the rolling mill.

The joint venture is owned 74.9% by Ma aden and 25.1% by Alcoa and consists of three separate companies as follows: one each for the mine and refinery, the smelter, and the rolling mill. Following the signing of the joint venture shareholders agreement, Alcoa paid Ma aden $80 representing the initial investment in the project. In addition, Alcoa paid $22 and $34 to Ma aden in 2011 and 2010, respectively, representing Alcoa s pro rata share of certain agreed upon pre-incorporation costs incurred by Ma aden before formation of the joint venture.

Ma aden and Alcoa have put and call options, respectively, whereby Ma aden can require Alcoa to purchase from Ma aden, or Alcoa can require Ma aden to sell to Alcoa, a 14.9% interest in the joint venture at the then fair market value. These options may only be exercised in a six-month window that opens five years after the Commercial Production Date (as defined in the joint venture shareholders agreement) and, if exercised, must be exercised for the full 14.9% interest.

The Alcoa affiliate that holds Alcoa s interests in the smelting company and the rolling mill company is wholly owned by Alcoa, and the Alcoa affiliate that holds Alcoa s interests in the mining and refining company is wholly owned by AWAC. Except in limited circumstances, Alcoa may not sell, transfer or otherwise dispose of or encumber or enter into any agreement in respect of the votes or other rights attached to its interests in the joint venture without Ma aden s prior written consent.

A number of Alcoa employees perform various types of services for the smelting, rolling mill, and refining and mining companies as part of the construction of the fully-integrated aluminum complex. At December 31, 2012 and 2011, Alcoa had an outstanding receivable of $28 and $25, respectively, from the smelting, rolling mill, and refining and mining companies for labor and other employee-related expenses.

Capital investment in the project is expected to total approximately $10,800 (SAR 40.5 billion). Alcoa s equity investment in the joint venture will be approximately $1,100 over a five-year period (2010 through 2014), and Alcoa will be responsible for its pro rata share of the joint venture s project financing. Alcoa has contributed $661, including $253 and $249 in 2012 and 2011, respectively, towards the $1,100 commitment. As of December 31, 2012 and 2011, the carrying value of Alcoa s investment in this project was $816 and $565, respectively.

In late 2010, the smelting and rolling mill companies entered into project financing totaling $4,035, of which $1,013 represents Alcoa s share (the equivalent of Alcoa s 25.1% interest in the smelting and rolling mill companies). Also, in late 2012, the smelting and rolling mill companies entered into additional project financing totaling $480, of which $120 represents Alcoa s share. In conjunction with the financings, Alcoa issued guarantees on behalf of the smelting and rolling mill companies to the lenders in the event that such companies default on their debt service requirements through June 2017 and December 2018, respectively, (Ma aden issued similar guarantees for its 74.9% interest). Alcoa s guarantees for the smelting and rolling mill companies cover total debt service requirements of $121 in principal and up to a maximum of approximately $60 in interest per year (based on projected interest rates). At December 31, 2012 and 2011, the combined fair value of the guarantees was $10 and $8, respectively, and was included in Other noncurrent liabilities and deferred credits on the accompanying Consolidated Balance Sheet. Under the project financings, a downgrade of Alcoa s credit ratings below investment grade by at least two agencies would require Alcoa to provide a letter of credit or fund an escrow account for a portion or all of Alcoa s remaining equity commitment to the joint venture project in Saudi Arabia.

In late 2011, the refining and mining company entered into project financing totaling $1,992, of which $500 represents AWAC s 25.1% interest in the refining and mining company. In conjunction with the financing, Alcoa, on behalf of AWAC, issued guarantees to the lenders in the event that the refining and mining company defaults on its debt service requirements through June 2019 (Ma aden issued similar guarantees for its 74.9% interest). Alcoa s guarantees for the refining and mining company cover total debt service requirements of $60 in principal and up to a maximum of approximately $25 in interest per year (based on projected interest rates). At December 31, 2012 and 2011, the combined fair value of the guarantees was $4. In the event Alcoa would be required to make payments under the guarantees, 40% of such amount would be contributed to Alcoa by Alumina Limited, consistent with its ownership interest in AWAC. Under the project financing, a downgrade of Alcoa s credit ratings below investment grade by at least two agencies would require Alcoa to provide a letter of credit or fund an escrow account for a portion or all of Alcoa s remaining equity commitment to the joint venture project in Saudi Arabia.

Power for the refinery, smelter, and rolling mill will be supplied under a gas allocation from Saudi Aramco, based on authorization of the Ministry of Petroleum and Mineral Resources of Saudi Arabia (the Ministry of Petroleum). The letter authorizing the gas allocation provides for gas to be tolled and power to be supplied to the refinery, smelter, and rolling mill from an adjacent power and water desalination plant being constructed by a company ultimately owned by the government of Saudi Arabia, with the major tolling elements fixed at cost. The gas allocation is contingent on the finalization of implementing contractual arrangements and on the achievement of certain milestones, as defined in the joint venture shareholders agreement, and includes possible penalties if the milestones are not met, including the following: (i) potential forfeiture of a $350 letter of credit required to be provided to the Ministry of Petroleum by Ma aden (with Alcoa responsible for its pro rata share) to ensure completion of the refinery, (ii) potential forfeiture of the gas allocation if the smelter is not completed, (iii) a potential requirement for the smelter to allocate 275 kmt of aluminum to other entities determined by the Ministry of Petroleum if the rolling mill is not constructed, and (iv) under a new version of the gas allocation (issued in early 2011 and further extended in May 2012), forfeiture of a $60 letter of credit if certain auxiliary rolling facilities are not completed.

The parties subject to the joint venture shareholders agreement may not sell, transfer, or otherwise dispose of, pledge, or encumber any interests in the joint venture until certain milestones have been met as defined in both agreements. Under the joint venture shareholders agreement, upon the occurrence of an unremedied event of default by Alcoa, Ma aden may purchase, or, upon the occurrence of an unremedied event of default by Ma aden, Alcoa may sell, its interest for consideration that varies depending on the time of the default.

Other Investments. As of December 31, 2012 and 2011, Other investments included $67 and $92, respectively, in exchange-traded fixed income and equity securities, which are classified as available-for-sale and are carried at fair value with unrealized gains and losses recognized in other comprehensive income. Unrealized and realized gains and losses related to these securities were immaterial in 2012, 2011, and 2010.

J. Other Noncurrent Assets

December 31,	2012	2011
Intangibles, net (E)	$ 407	$ 481
Cash surrender value of life insurance	464	455
Value-added tax receivable	408	510
Fair value of derivative contracts (X)	364	44
Prepaid gas transmission contract (N)	363	346
Deferred mining costs, net	223	221
Prepaid pension benefit (W)	86	109
Unamortized debt expense	86	98
Assets held for sale (B)	2	243
Other	309	289
	$ 2,712	$ 2,796

K. Debt

Long-Term Debt.

December 31,	2012	2011
6% Notes, due 2012	$ -	$ 322
6% Notes, due 2013	422	422
5.25% Convertible Notes, due 2014	575	575
5.55% Notes, due 2017	750	750
6.5% Bonds, due 2018	250	250
6.75% Notes, due 2018	750	750
5.72% Notes, due 2019	750	750
6.15% Notes, due 2020	1,000	1,000
5.40% Notes, due 2021	1,250	1,250
5.87% Notes, due 2022	627	627
5.9% Notes, due 2027	625	625
6.75% Bonds, due 2028	300	300
5.95% Notes due 2037	625	625
BNDES Loans, due 2013-2029 (see below for weighted average rates)	397	627
Iowa Finance Authority Loan, due 2042 (4.75%)	250	-
Other*	205	212
	8,776	9,085
Less: amount due within one year	465	445
	$ 8,311	$ 8,640

* Other includes various financing arrangements related to subsidiaries, unamortized debt discounts related to the outstanding notes and bonds listed in the table above, a beneficial conversion feature related to the convertible notes, and adjustments to the carrying value of long-term debt related to interest swap contracts accounted for as fair value hedges (see the Derivatives section of Note X).

The principal amount of long-term debt maturing in each of the next five years is $465 in 2013, $661 in 2014, $34 in 2015, $33 in 2016, and $780 in 2017.

Public Debt In January 2012, Alcoa repaid the $322 in outstanding principal of its 6% Notes as scheduled using available cash on hand.

In August 2012, Alcoa and the Iowa Finance Authority entered into a loan agreement for the proceeds from the issuance of $250 in Midwestern Disaster Area Revenue Bonds Series 2012 due 2042 (the Bonds). The Bonds were issued by the Iowa Finance Authority pursuant to the Heartland Disaster Tax Relief Act of 2008 for the purpose of financing all or part of the cost of acquiring, constructing, reconstructing, and renovating certain facilities at Alcoa s rolling mill plant in Davenport, IA. Alcoa received $248 in net proceeds (reflecting payment of financing costs), which was classified as restricted cash. This transaction is not reflected in the accompanying Statement of Consolidated Cash Flows as it represents a non-cash financing and investing activity. At December 31, 2012, Alcoa had $171 of restricted cash remaining, all of which was classified in Prepaid expenses and other current assets on the accompanying Consolidated Balance Sheet. Interest on the Bonds is at a rate of 4.75% per annum and will be paid semi-annually in February and August, which will commence in February 2013. Alcoa has the option through the loan agreement to redeem the Bonds, as a whole or in part, on or after August 1, 2022, on at least 30 days, but not more than 60 days, prior notice to the holders of the Bonds at a redemption price equal to 100% of the principal amount thereof, without premium, plus accrued interest, if any, to the redemption date. The loan agreement ranks *pari passu* with Alcoa s other unsecured senior unsubordinated indebtedness.

In February 2011, Alcoa filed an automatic shelf registration statement with the Securities and Exchange Commission for an indeterminate amount of securities for future issuance. This shelf registration statement replaced Alcoa s existing shelf registration statement (filed in March 2008). As of December 31, 2012 and 2011, $1,250 in senior debt securities were issued under the current shelf registration statement.

In April 2011, Alcoa completed a public debt offering under its current shelf registration statement (dated February 18, 2011) for $1,250 of 5.40% Notes due 2021 (the 2021 Notes). Alcoa received $1,241 in net proceeds from the public debt offering reflecting an original issue discount and payment of financing costs. The net proceeds were used for the early retirement of $881 in outstanding notes (see below), early repayment of $101 in outstanding loans related to the bauxite mine development in Brazil (see BNDES Loans below), and the remainder was used for general corporate purposes. The original issue discount and financing costs were deferred and are being amortized to interest expense over the term of the 2021 Notes. Interest on the 2021 Notes is paid semi-annually in April and October, which commenced in October 2011. Alcoa has the option to redeem the 2021 Notes, as a whole or in part, at any time or from time to time, on at least 30 days, but not more than 60 days, prior notice to the holders of the 2021 Notes at a redemption price specified in the 2021 Notes. The 2021 Notes are subject to repurchase upon the occurrence of a change in control repurchase event (as defined in the 2021 Notes) at a repurchase price in cash equal to 101% of the aggregate principal amount of the 2021 Notes repurchased, plus any accrued and unpaid interest on the 2021 Notes repurchased. The 2021 Notes rank *pari passu* with Alcoa s other unsecured senior unsubordinated indebtedness.

In May 2011, Alcoa completed the following tender offers: (i) any and all of its 5.375% Notes due 2013 (the 5.375% Notes) and (ii) up to $400 of its 6.00% Notes due 2013 (the 6.00% Notes and collectively with the 5.375% Notes, the Notes). Upon expiration of the tender offers, $269 and $328 of the aggregate outstanding principal amount of the 5.375% Notes and 6.00% Notes, respectively, were validly tendered and accepted. Additionally in May 2011, subsequent to the expiration of the tender offer for the 5.375% Notes, Alcoa elected to call for redemption the remaining outstanding principal of $284 under the provisions of the 5.375% Notes. The total cash paid to the holders of the tendered 5.375% Notes and 6.00% Notes and the called 5.375% Notes was $972, which consisted of $881 in debt principal, $74 in purchase premiums, and $17 in accrued and unpaid interest from the respective last interest payment dates up to, but not including, the respective settlement dates. The $74 was recorded in Interest expense on the accompanying Statement of Consolidated Operations. Subsequent to the respective tender offer, the 6.00% Notes had a remaining outstanding principal of $422.

In conjunction with the early retirement of the 5.375% Notes, Alcoa terminated interest rate swaps with a notional amount totaling $550. These swaps were accounted for as fair value hedges and were used to convert the stated interest rate of the 5.375% Notes from fixed to floating. At the time of termination, the swaps were in-the-money resulting in a gain of $33, which was recorded in Interest expense on the accompanying Statement of Consolidated Operations.

BNDES Loans In March 2008, Alcoa Alumínio (Alumínio) entered into two separate loan agreements (the First Loans) with Brazil s National Bank for Economic and Social Development (BNDES) related to the Juruti bauxite mine development and the São Luís refinery expansion.

The first loan agreement provides for a commitment of $248 (R$500), which is divided into five subloans, and was used to pay for certain expenditures of the Juruti bauxite mine development. Interest on four of the subloans totaling $233 (R$470) is a Brazil real rate of interest equal to BNDES long-term interest rate, 5.00% and 6.00% as of December 31, 2012 and 2011, respectively, plus a weighted-average margin of 2.13%. Interest on the fifth subloan of $15 (R$30) is a U.S. dollar rate of interest equal to the average cost incurred by BNDES in raising capital outside of Brazil, 3.56% and 3.59% as of December 31, 2012 and 2011, respectively, plus a margin of 2.40%.

Principal and interest were payable monthly beginning in September 2009 and ending in November 2014 for the four subloans totaling $233 (R$470) and beginning in November 2009 and ending in January 2015 for the subloan of $15 (R$30). Prior to these dates, interest was payable quarterly on borrowed amounts.

As of December 31, 2012, Alumínio had no outstanding borrowings under any of the subloans. During 2012, Alumínio repaid $51 (R$102) and $3 (R$7) of outstanding borrowings related to the subloans totaling $233 (R$470) and the subloan of $15 (R$30), respectively.

As of December 31, 2011, Alumínio s outstanding borrowings were $55 (R$102) and $3 (R$7) and the weighted-average interest rate was 8.13% and 5.99% for the subloans totaling $233 (R$470) and the subloan of $15 (R$30), respectively. During 2011, Alumínio repaid $131 (R$209) and $7 (R$11) of outstanding borrowings related to the subloans totaling $233 (R$470) and the subloan of $15 (R$30), respectively.

The second loan agreement provides for a commitment of $374 (R$650), which is divided into three subloans, and was used to pay for certain expenditures of the São Luís refinery expansion. Interest on two of the subloans totaling $339 (R$589) is a Brazil real rate of interest equal to BNDES long-term interest rate plus a weighted-average margin of 1.99%. Interest on the third subloan of $35 (R$61) is a U.S. dollar rate of interest equal to the average cost incurred by BNDES in raising capital outside of Brazil plus a margin of 2.02%.

Principal and interest were payable monthly beginning in December 2009 and ending in February 2015 for the two subloans totaling $339 (R$589) and beginning in February 2010 and ending in April 2015 for the subloan of $35 (R$61). Prior to these dates, interest was payable quarterly on borrowed amounts.

As of December 31, 2012, Alumínio had no outstanding borrowings under any of the subloans. During 2012, Alumínio repaid $176 (R$356) and $22 (R$46) of outstanding borrowings related to the subloans totaling $339 (R$589) and the subloan of $35 (R$61), respectively.

As of December 31, 2011, Alumínio s outstanding borrowings were $191 (R$356) and $23 (R$42) and the weighted-average interest rate was 7.99% and 5.61% for the subloans totaling $339 (R$589) and the subloan of $35 (R$61), respectively. During 2011, Alumínio repaid $67 (R$113) and $7 (R$11) of outstanding borrowings related to the subloans totaling $339 (R$589) and the subloan of $35 (R$61), respectively.

The First Loans were repaid early without penalty under the approval of BNDES. With the full repayment of the First Loans, the commitments were effectively terminated.

In June 2008, Alumínio finalized certain documents related to another loan agreement with BNDES. This loan agreement provides for a commitment of $397 (R$687), which is divided into three subloans, and is being used to pay for certain expenditures of the Estreito hydroelectric power project. Interest on the three subloans is a Brazil real rate of interest equal to BNDES long-term interest rate plus a weighted-average margin of 1.48%. Principal and interest are payable monthly beginning in October 2011 and ending in September 2029 for two of the subloans totaling R$667 and beginning in July 2012 and ending in June 2018 for the subloan of R$20. This loan may be repaid early without penalty with the approval of BNDES.

As of December 31, 2012 and 2011, Alumínio s outstanding borrowings were $311 (R$637) and $355 (R$661), respectively, and the weighted-average interest rate was 6.49% and 7.50%, respectively. During 2012 and 2011, Alumínio repaid $20 (R$38) and $5 (R$9), respectively, of outstanding borrowings. Additionally, Alumínio borrowed $7 (R$13) and $5 (R$8), under the loan in 2012 and 2011, respectively.

In December 2012, Alumínio finalized certain documents related to another loan agreement with BNDES. This loan agreement provides for a commitment of $85 (R$177) and is being used to pay for certain expenditures of the Estreito hydroelectric power project. Due to the timing of the finalization of the loan documents and the expenditures of the project, Alumínio advanced the cash necessary to the consortium to pay for the expenditures supported by this loan. Interest on the loan is a Brazil real rate of interest equal to BNDES long-term interest rate plus a margin of 1.55%. Principal and interest are payable monthly beginning in January 2013 and ending in September 2029. This loan may be repaid early without penalty with the approval of BNDES. As of December 31, 2012, Alumínio s outstanding borrowings were $86 (R$177) and the interest rate was 6.55%.

Commercial Paper. Alcoa had no outstanding commercial paper at December 31, 2012. Outstanding commercial paper was $224 at December 31, 2011. In 2012 and 2011, the average outstanding commercial paper was $354 and $197. Commercial paper matures at various times within one year and had an annual weighted average interest rate of 0.8%, 0.6%, and 0.7% during 2012, 2011, and 2010, respectively.

On July 25, 2011, Alcoa entered into a Five-Year Revolving Credit Agreement (the Credit Agreement) with a syndicate of lenders and issuers named therein. The Credit Agreement provides a $3,750 senior unsecured revolving credit facility (the Credit Facility), the proceeds of which are to be used to provide working capital or for other general corporate purposes of Alcoa, including support of Alcoa s commercial paper program. Subject to the terms and conditions of the Credit Agreement, Alcoa may from time to time request increases in lender commitments under the Credit Facility, not to exceed $500 in aggregate principal amount, and may also request the issuance of letters of credit, subject to a letter of credit sublimit of $1,000 under the Credit Facility.

The Credit Facility was scheduled to mature on July 25, 2016; however, on December 7, 2012, Alcoa received approval for a one-year extension of the maturity date by the lenders and issuers that support $3,700 of the Credit Facility (approval for the remaining $50 was received on January 8, 2013). As such, the Credit Facility now matures on July 25, 2017, unless extended or earlier terminated in accordance with the provisions of the Credit Agreement. Alcoa may make one additional one-year extension request during the remaining term of the Credit Facility, subject to the lender consent requirements set forth in the Credit Agreement. Under the provisions of the Credit Agreement, Alcoa will pay a fee of 0.25% (based on Alcoa s long-term debt ratings as of December 31, 2012) of the total commitment per annum to maintain the Credit Facility.

The Credit Facility is unsecured and amounts payable under it will rank *pari passu* with all other unsecured, unsubordinated indebtedness of Alcoa. Borrowings under the Credit Facility may be denominated in U.S. dollars or euros. Loans will bear interest at a base rate or a rate equal to LIBOR, plus, in each case, an applicable margin based on the credit ratings of Alcoa s outstanding senior unsecured long-term debt. The applicable margin on base rate loans and LIBOR loans will be 0.50% and 1.50% per annum, respectively, based on Alcoa s long-term debt ratings as of December 31, 2012. Loans may be prepaid without premium or penalty, subject to customary breakage costs.

The Credit Facility replaces Alcoa s Five-Year Revolving Credit Agreement, dated as of October 2, 2007 (the Former Credit Agreement), which was scheduled to mature on October 2, 2012. The Former Credit Agreement, which had a

total capacity (excluding the commitment of Lehman Commercial Paper Inc.) of $3,275 and was undrawn, was terminated effective July 25, 2011.

The Credit Agreement includes covenants substantially similar to those in the Former Credit Agreement, including, among others, (a) a leverage ratio, (b) limitations on Alcoa s ability to incur liens securing indebtedness for borrowed money, (c) limitations on Alcoa s ability to consummate a merger, consolidation or sale of all or substantially all of its assets, and (d) limitations on Alcoa s ability to change the nature of its business. As of December 31, 2012 and 2011, Alcoa was in compliance with all such covenants.

The obligation of Alcoa to pay amounts outstanding under the Credit Facility may be accelerated upon the occurrence of an Event of Default as defined in the Credit Agreement. Such Events of Default include, among others, (a) Alcoa s failure to pay the principal of, or interest on, borrowings under the Credit Facility, (b) any representation or warranty of Alcoa in the Credit Agreement proving to be materially false or misleading, (c) Alcoa s breach of any of its covenants contained in the Credit Agreement, and (d) the bankruptcy or insolvency of Alcoa.

There were no amounts outstanding at December 31, 2012 and 2011 and no amounts were borrowed during 2012 or 2011 under the Credit Facility.

Short-Term Borrowings. At December 31, 2012 and 2011, Short-term borrowings were $53 and $62, respectively. These amounts included $48 and $53 at December 31, 2012 and 2011, respectively, related to accounts payable settlement arrangements with certain vendors and third-party intermediaries. These arrangements provide that, at the vendor s request, the third-party intermediary advances the amount of the scheduled payment to the vendor, less an appropriate discount, before the scheduled payment date and Alcoa makes payment to the third-party intermediary on the date stipulated in accordance with the commercial terms negotiated with its vendors. Alcoa records imputed interest related to these arrangements as interest expense in the Statement of Consolidated Operations.

In January 2012, Alcoa entered into two term loan agreements, totaling $350, with two separate financial institutions. Additionally, throughout 2012, Alcoa entered into six revolving credit agreements, providing a combined $640 in credit facilities, with six different financial institutions. The purpose of any borrowings under all eight arrangements will be to provide working capital and for other general corporate purposes, including contributions to Alcoa s pension plans ($561 was contributed in 2012).

The two term loans were fully drawn on the same dates as the agreements and were subject to an interest rate equivalent to the 1-month LIBOR (changed from the 3-month LIBOR in April 2012) plus a 1.5% margin. A $150 term loan was repaid between October and November 2012 and a $200 term loan was repaid in December 2012, effectively terminating both agreements. In February 2012, Alcoa fully borrowed $100 under one of the credit facilities, which was repaid in August 2012. This borrowing was subject to an interest rate equivalent to the 6-month LIBOR plus a 1.25% margin. In July 2012, Alcoa fully borrowed $150 under one of the credit facilities, which was repaid in December 2012. This borrowing was subject to an interest rate equivalent to the 3-month LIBOR plus a 1.375% margin.

The six revolving credit facilities expire as follows: $150 in March 2013; $100 in September 2013 (originally December 2012, extended in September 2012); $100 in September 2013; $140 in October 2013; $100 in December 2013 (originally December 2012, extended in December 2012); and $50 in December 2015. The covenants contained in all eight arrangements are the same as the Credit Agreement (see the Commercial Paper section above).

During 2012, Alcoa s subsidiary, Alumínio, borrowed and repaid a total of $280 in new loans with a weighted-average interest rate of 2.32% and a weighted-average maturity of 172 days from two financial institutions. The purpose of these borrowings was to support Alumínio s export operations.

L. Other Noncurrent Liabilities and Deferred Credits

December 31,	2012	2011
Fair value of derivative contracts (X)	$ 606	$ 624
Asset retirement obligations (C)	535	503
Environmental remediation (N)	458	289
Deferred income taxes (T)	460	395
Deferred credit related to derivative contract (X)	330	-
Accrued compensation and retirement costs	322	304
Deferred alumina sales revenue	108	116
Other	259	197
	$ 3,078	$ 2,428

M. Noncontrolling Interests

The following table summarizes the noncontrolling shareholders interests in the equity of Alcoa s majority-owned consolidated subsidiaries:

December 31,	2012	2011
Alcoa World Alumina and Chemicals	$ 3,295	$ 3,324
Other	29	27
	$ 3,324	$ 3,351

In 2012, 2011, and 2010, Alcoa received $171, $169, and $162, respectively, in contributions from the noncontrolling shareholder (Alumina Limited) of Alcoa World Alumina and Chemicals.

N. Contingencies and Commitments

Contingencies

Litigation

Alba Civil Suit

On February 27, 2008, Alcoa Inc. (Alcoa) received notice that Aluminium Bahrain B.S.C. (Alba) had filed suit against Alcoa, Alcoa World Alumina LLC (AWA), and William Rice (collectively, the Alcoa Parties), and others, in the U.S. District Court for the Western District of Pennsylvania (the Court), Civil Action number 08-299, styled Aluminium Bahrain B.S.C. v. Alcoa Inc., Alcoa World Alumina LLC, William Rice, and Victor Phillip Dahdaleh. The complaint alleged that certain Alcoa entities and their agents, including Victor Phillip Dahdaleh, had engaged in a conspiracy over a period of 15 years to defraud Alba. The complaint further alleged that Alcoa and its employees or agents (1) illegally bribed officials of the government of Bahrain and/or officers of Alba in order to force Alba to purchase alumina at excessively high prices, (2) illegally bribed officials of the government of Bahrain and/or officers of Alba and issued threats in order to pressure Alba to enter into an agreement by which Alcoa would purchase an equity interest in Alba, and (3) assigned portions of existing supply contracts between Alcoa and Alba for the sole purpose of facilitating alleged bribes and unlawful commissions. The complaint alleged that Alcoa and the other defendants violated the Racketeer Influenced and Corrupt Organizations Act (RICO) and committed fraud. Alba claimed damages in excess of $1,000. Alba s complaint sought treble damages with respect to its RICO claims; compensatory, consequential, exemplary, and punitive damages; rescission of the 2005 alumina supply contract; and attorneys fees and costs.

In response to a motion filed by the U.S. Department of Justice (DOJ) on March 27, 2008 (see Government Investigations below), the Court ordered the Alba civil suit administratively closed and stayed all discovery to allow the DOJ to fully conduct an investigation. On November 8, 2011, at Alcoa s request, the Court removed the case from

administrative stay and ordered Alba to file an Amended Complaint by November 28, 2011, and a RICO Case Statement 30 days thereafter for the limited purpose of allowing Alcoa to move to dismiss Alba s lawsuit. Alcoa filed a motion to dismiss, which was denied on June 11, 2012.

During the second quarter of 2012, Alcoa proposed to settle the suit by offering Alba a cash payment of $45. Alcoa also offered Alba a long-term alumina supply contract. Based on the cash offer, Alcoa recorded a $45 ($18 after-tax and noncontrolling interest) charge in the 2012 second quarter representing Alcoa s estimate of the minimum end of the range probable to settle the case, and estimated an additional reasonably possible charge of up to $75 to settle the suit.

On October 9, 2012, the Alcoa Parties, without admitting any liability, entered into a settlement agreement with Alba. The agreement called for AWA to pay Alba $85 in two equal installments, one-half at time of settlement and one-half one year later, and for the case against the Alcoa Parties to be dismissed with prejudice. Additionally, AWA and Alba entered into a long-term alumina supply agreement. On October 9, 2012, pursuant to the settlement agreement, AWA paid Alba $42.5, and all claims against the Alcoa Parties were dismissed with prejudice. Under the agreement, AWA is obligated to pay an additional $42.5, without interest or contingency, on October 9, 2013. Based on the settlement agreement, in the 2012 third quarter, Alcoa recorded a $40 ($15 after-tax and noncontrolling interest) charge in addition to the $45 ($18 after-tax and noncontrolling interest) charge it recorded in the 2012 second quarter in respect of the suit. In addition, based on an agreement between Alcoa and Alumina Limited (which holds a 40% equity interest in AWA), Alcoa estimates an additional reasonably possible after-tax charge of between $25 to $30 to reallocate a portion of the costs (including legal fees) of the Alba civil settlement from AWA to Alcoa, but this would occur only if a settlement is reached with the DOJ and the Securities and Exchange Commission (the SEC) regarding their investigations (see Government Investigations below).

Government Investigations

On February 26, 2008, Alcoa Inc. advised the DOJ and the SEC that it had recently become aware of the claims by Alba as alleged in the Alba civil suit, had already begun an internal investigation, and intended to cooperate fully in any investigation that the DOJ or the SEC may commence. On March 17, 2008, the DOJ notified Alcoa that it had opened a formal investigation and Alcoa has been cooperating with the government since that time.

Alcoa is actively negotiating with the DOJ and the SEC to reach a resolution of their investigations of the Alba matter; however, Alcoa has not reached any agreement with either agency. Given the uncertainty regarding whether a settlement can be reached and, if reached, on what terms, Alcoa is not able to estimate a range of reasonably possible loss with regard to any such settlement. If a settlement of the government investigations is reached, Alcoa believes that the settlement amount would be material to Alcoa s results of operations for the relevant fiscal period. If a settlement cannot be reached, Alcoa will proceed to trial with the DOJ and the SEC and under those circumstances is unable to predict an outcome or to estimate its reasonably possible loss. There can be no assurance that the final outcome of the government s investigations will not have a material adverse effect on Alcoa.

Other Matters

In November 2006, in Curtis v. Alcoa Inc., Civil Action No. 3:06cv448 (E.D. Tenn.), a class action was filed by plaintiffs representing approximately 13,000 retired former employees of Alcoa or Reynolds Metals Company and spouses and dependents of such retirees alleging violation of the Employee Retirement Income Security Act (ERISA) and the Labor-Management Relations Act by requiring plaintiffs, beginning January 1, 2007, to pay health insurance premiums and increased co-payments and co-insurance for certain medical procedures and prescription drugs. Plaintiffs alleged these changes to their retiree health care plans violated their rights to vested health care benefits. Plaintiffs additionally alleged that Alcoa had breached its fiduciary duty to plaintiffs under ERISA by misrepresenting to them that their health benefits would never change. Plaintiffs sought injunctive and declaratory relief, back payment of benefits, and attorneys fees. Alcoa had consented to treatment of plaintiffs claims as a class action. During the fourth quarter of 2007, following briefing and argument, the court ordered consolidation of the plaintiffs motion for

preliminary injunction with trial, certified a plaintiff class, bifurcated and stayed the plaintiffs breach of fiduciary duty claims, struck the plaintiffs jury demand, but indicated it would use an advisory jury, and set a trial date of September 17, 2008. In August 2008, the court set a new trial date of March 24, 2009 and, subsequently, the trial date was moved to September 22, 2009. In June 2009, the court indicated that it would not use an advisory jury at trial. Trial in the matter was held over eight days commencing September 22, 2009 and ending on October 1, 2009 in federal court in Knoxville, TN before the Honorable Thomas Phillips, U.S. District Court Judge. At the conclusion of evidence, the court set a post-hearing briefing schedule for submission of proposed findings of fact and conclusions of law by the parties and for replies to the same. Post trial briefing was submitted on December 4, 2009.

On March 9, 2011, the court issued a judgment order dismissing plaintiffs lawsuit in its entirety with prejudice for the reasons stated in its Findings of Fact and Conclusions of Law. On March 23, 2011, plaintiffs filed a motion for clarification and/or amendment of the judgment order, which seeks, among other things, a declaration that plaintiffs retiree benefits are vested subject to an annual cap and an injunction preventing Alcoa, prior to 2017, from modifying the plan design to which plaintiffs are subject or changing the premiums and deductibles that plaintiffs must pay. Also on March 23, 2011, plaintiffs filed a motion for award of attorney s fees and expenses. Alcoa filed its opposition to both motions on April 11, 2011. On June 11, 2012, the court issued its memorandum and order denying plaintiffs motion for clarification and/or amendment to the original judgment order. On July 6, 2012, plaintiffs filed a notice of appeal of the court s March 9, 2011 judgment. On July 12, 2012, the trial court stayed Alcoa s motion for assessment of costs pending resolution of plaintiffs appeal. The appeal is docketed in the United States Court of Appeals for the Sixth Circuit as case number 12-5801. On July 26, 2012, the appellate court issued a briefing schedule requiring briefing to be complete by the end of October 2012. On August 29, 2012, the trial court dismissed plaintiffs motion for attorneys fees without prejudice to refiling the motion following the resolution of the appeal at the Sixth Circuit Court of Appeals. Briefing on the appeal is complete and oral argument is scheduled for March 6, 2013.

On April 23, 2004, St. Croix Renaissance Group, L.L.L.P. (SCRG), Brownfield Recovery Corp., and Energy Answers Corporation of Puerto Rico (collectively referred to as Plaintiffs) filed a suit against St. Croix Alumina L.L.C. and Alcoa World Alumina, LLC (collectively referred to as Alcoa) in the Territorial Court of the Virgin Islands, Division of St. Croix for claims related to the sale of Alcoa s former St. Croix alumina refinery to Plaintiffs. Alcoa thereafter removed the case to federal court and after a several year period of discovery and motion practice, a jury trial on the matter took place in St. Croix from January 11, 2011 to January 20, 2011. The jury returned a verdict in favor of Plaintiffs and awarded damages as described: on a claim of breaches of warranty, the jury awarded $13; on the same claim, the jury awarded punitive damages in the amount of $6; and on a negligence claim for property damage, the jury awarded $10. Plaintiffs filed a motion seeking pre-judgment interest on the jury award. On February 17, 2011, Alcoa filed post-trial motions seeking judgment notwithstanding the verdict or, in the alternative, a new trial. On May 31, 2011, the court granted Alcoa s motion for judgment regarding Plaintiffs $10 negligence award and denied the remainder of Alcoa s motions. Additionally, the court awarded Plaintiffs pre-judgment interest of $2 on the breach of warranty award. As a result of the court s post-trial decisions, Alcoa recorded a charge of $20 in 2011 (see Note D). On June 14, 2011, Alcoa filed a notice of appeal with the U.S. Court of Appeals for the Third Circuit regarding Alcoa s denied post-trial motions. On June 22, 2011, SCRG filed a notice of cross appeal with the Third Circuit Court related to certain pre-trial decisions of the court and of the court s post-trial ruling on the negligence claim. The Third Circuit Court referred this matter to mediation as is its standard practice in appeals. Following mediation and further, separate settlement discussions, the parties executed an agreement dated September 30, 2011 resolving the matter in its entirety, and subsequently jointly petitioned (i) the District Court to release Alcoa from the jury verdict and (ii) the Third Circuit Court of Appeals to dismiss the matter. On March 13, 2012, the District Court entered an order discharging Alcoa from the jury verdict and, on March 14, 2012, the Third Circuit Court of Appeals dismissed the matter. This matter is now fully resolved.

Before 2002, Alcoa purchased power in Italy in the regulated energy market and received a drawback of a portion of the price of power under a special tariff in an amount calculated in accordance with a published resolution of the Italian Energy Authority, Energy Authority Resolution n. 204/1999 (204/1999). In 2001, the Energy Authority published another resolution, which clarified that the drawback would be calculated in the same manner, and in the same amount, in either the regulated or unregulated market. At the beginning of 2002, Alcoa left the regulated energy market to purchase energy in the unregulated market. Subsequently, in 2004, the Energy Authority introduced regulation no.

148/2004 which set forth a different method for calculating the special tariff that would result in a different drawback for the regulated and unregulated markets. Alcoa challenged the new regulation in the Administrative Court of Milan and received a favorable judgment in 2006. Following this ruling, Alcoa continued to receive the power price drawback in accordance with the original calculation method, through 2009, when the European Commission declared all such special tariffs to be impermissible state aid. In 2010, the Energy Authority appealed the 2006 ruling to the Consiglio di Stato (final court of appeal). On December 2, 2011, the Consiglio di Stato ruled in favor of the Energy Authority and against Alcoa, thus presenting the opportunity for the energy regulators to seek reimbursement from Alcoa of an amount equal to the difference between the actual drawback amounts received over the relevant time period, and the drawback as it would have been calculated in accordance with regulation 148/2004. On February 23, 2012, Alcoa filed its appeal of the decision of the Consiglio di Stato, and that appeal remains pending. On March 26, 2012, Alcoa received a letter from the agency (Cassa Conguaglio per il Settore Eletrico (CCSE)) responsible for making and collecting payments on behalf of the Energy Authority demanding payment in the amount of approximately $110 (85), including interest. By letter dated April 5, 2012, Alcoa informed CCSE that it disputes the payment demand of CCSE since (i) CCSE was not authorized by the Consiglio di Stato decisions to seek payment of any amount, (ii) the decision of the Consiglio di Stato has been appealed and that appeal remains pending, and (iii) in any event, no interest should be payable. On April 29, 2012, Law No. 44 of 2012 (44/2012) came into effect, changing the method to calculate the drawback. Alcoa believes that under 44/2012 its range of reasonably possible loss is from $0 to $50 (39). Following the effectiveness of 44/2012, Alcoa has received no further demands from CCSE. At this time, the company is unable to reasonably predict an outcome for this matter.

European Commission Matters. In July 2006, the European Commission (EC) announced that it had opened an investigation to establish whether an extension of the regulated electricity tariff granted by Italy to some energy-intensive industries complies with European Union (EU) state aid rules. The Italian power tariff extended the tariff that was in force until December 31, 2005 through November 19, 2009 (Alcoa has been incurring higher power costs at its smelters in Italy subsequent to the tariff end date). The extension was originally through 2010, but the date was changed by legislation adopted by the Italian Parliament effective on August 15, 2009. Prior to expiration of the tariff in 2005, Alcoa had been operating in Italy for more than 10 years under a power supply structure approved by the EC in 1996. That measure provided a competitive power supply to the primary aluminum industry and was not considered state aid from the Italian Government. The EC s announcement expressed concerns about whether Italy s extension of the tariff beyond 2005 was compatible with EU legislation and potentially distorted competition in the European market of primary aluminum, where energy is an important part of the production costs.

On November 19, 2009, the EC announced a decision in this matter stating that the extension of the tariff by Italy constituted unlawful state aid, in part, and, therefore, the Italian Government is to recover a portion of the benefit Alcoa received since January 2006 (including interest). The amount of this recovery will be based on a calculation that is being prepared by the Italian Government (see below). In late 2009, after discussions with legal counsel and reviewing the bases on which the EC decided, including the different considerations cited in the EC decision regarding Alcoa s two smelters in Italy, Alcoa recorded a charge of $250 (173), which included $20 (14) to write off a receivable from the Italian Government for amounts due under the now expired tariff structure and $230 (159) to establish a reserve. On April 19, 2010, Alcoa filed an appeal of this decision with the General Court of the EU. Alcoa will pursue all substantive and procedural legal steps available to annul the EC s decision. On May 22, 2010, Alcoa also filed with the General Court a request for injunctive relief to suspend the effectiveness of the decision, but, on July 12, 2010, the General Court denied such request. On September 10, 2010, Alcoa appealed the July 12, 2010 decision to the European Court of Justice (ECJ); this appeal was dismissed on December 16, 2011.

In June 2012, Alcoa received formal notification from the Italian Government with a calculated recovery amount of $375 (303); this amount was reduced by $65 (53) of amounts owed by the Italian Government to Alcoa, resulting in a net payment request of $310 (250). In a notice published in the Official Journal of the European Union on September 22, 2012, the EC announced that it had filed an action against the Italian Government on July 18, 2012 to compel it to collect the recovery amount. On September 27, 2012, Alcoa received a request for payment in full of the $310 (250) by October 31, 2012. Since then, Alcoa has been in discussions with the Italian Government regarding the

timing of such payment. Alcoa commenced payment of the requested amount in five quarterly installments of $66 (50), paying the first installment on October 31, 2012. It is possible that Alcoa may be required to accelerate payment or pay in a lump sum. Notwithstanding the payment request or the timing of such payments, Alcoa s estimate of the most probable loss of the ultimate outcome of this matter and the low end of the range of reasonably possible loss, which is $209 (159) to $375 (303), remains the $209 (159) (the U.S. dollar amount reflects the effects of foreign currency movements since 2009) recorded in November 2009. At December 31, 2012, Alcoa s reserve for this matter stands at $143 (109), reflecting the payment made in October 2012. The full extent of the loss will not be known until the final judicial determination, which could be a period of several years.

Separately, on November 29, 2006, Alcoa filed an appeal before the General Court (formerly the European Court of First Instance) seeking the annulment of the EC s decision to open an investigation alleging that such decision did not follow the applicable procedural rules. On March 25, 2009, the General Court denied Alcoa s appeal. On May 29, 2009, Alcoa appealed the March 25, 2009 ruling before the ECJ. The hearing of the May 29, 2009 appeal was held on June 24, 2010. On July 21, 2011, the ECJ denied Alcoa s appeal.

As a result of the EC s November 19, 2009 decision, management had contemplated ceasing operations at its Italian smelters due to uneconomical power costs. In February 2010, management agreed to continue to operate its smelters in Italy for up to six months while a long-term solution to address increased power costs could be negotiated.

Also in February 2010, the Italian Government issued a decree, which was converted into law by the Italian Parliament in March 2010, to provide interruptibility rights to certain industrial customers who were willing to be subject to temporary interruptions in the supply of power (i.e. compensation for power interruptions when grids are overloaded) over a three-year period. Alcoa applied for and was granted such rights (expired on December 31, 2012) related to its Portovesme smelter. In May 2010, the EC stated that, based on their review of the validity of the decree, the interruptibility rights should not be considered state aid. On July 29, 2010, Alcoa executed a new power agreement effective September 1, 2010 through December 31, 2012 for the Portovesme smelter, replacing the short-term, market-based power contract that was in effect since early 2010.

Additionally in May 2010, Alcoa and the Italian Government agreed to a temporary idling of the Fusina smelter. As of June 30, 2010, the Fusina smelter was fully curtailed (44 kmt-per-year).

At the end of 2011, as part of a restructuring of Alcoa s global smelting system (see Note D), management decided to curtail operations at the Portovesme smelter during the first half of 2012. This action may lead to the permanent closure of the Portovesme smelter, due to the uncertain prospects for viable, long-term power, along with rising raw materials costs and falling global aluminum prices (mid-2011 to late 2011). In March 2012, Alcoa decided to delay the curtailment of the Portovesme smelter until the second half of 2012 based on negotiations with the Italian Government and other stakeholders. In September 2012, Alcoa began the process of curtailing the Portovesme smelter, which was fully curtailed by the end of 2012.

In January 2007, the EC announced that it had opened an investigation to establish whether the regulated electricity tariffs granted by Spain comply with EU state aid rules. At the time the EC opened its investigation, Alcoa had been operating in Spain for more than nine years under a power supply structure approved by the Spanish Government in 1986, an equivalent tariff having been granted in 1983. The investigation is limited to the year 2005 and is focused both on the energy-intensive consumers and the distribution companies. The investigation provided 30 days to any interested party to submit observations and comments to the EC. With respect to the energy-intensive consumers, the EC opened the investigation on the assumption that prices paid under the tariff in 2005 were lower than a pool price mechanism, therefore being, in principle, artificially below market conditions. Alcoa submitted comments in which the company provided evidence that prices paid by energy-intensive consumers were in line with the market, in addition to various legal arguments defending the legality of the Spanish tariff system. It is Alcoa s understanding that the Spanish tariff system for electricity is in conformity with all applicable laws and regulations, and therefore no state aid is present in the tariff system. While Alcoa does not believe that an unfavorable decision is probable, management has estimated that the total potential impact from an unfavorable decision could be approximately $90 (70) pretax. Also,

while Alcoa believes that any additional cost would only be assessed for the year 2005, it is possible that the EC could extend its investigation to later years. If the EC s investigation concludes that the regulated electricity tariffs for industries are unlawful, Alcoa will have an opportunity to challenge the decision in the EU courts.

Environmental Matters. Alcoa continues to participate in environmental assessments and cleanups at a number of locations (more than 100). These include owned or operating facilities and adjoining properties, previously owned or operating facilities and adjoining properties, and waste sites, including Superfund (Comprehensive Environmental Response, Compensation and Liability Act (CERCLA)) sites. A liability is recorded for environmental remediation when a cleanup program becomes probable and the costs or damages can be reasonably estimated.

As assessments and cleanups proceed, the liability is adjusted based on progress made in determining the extent of remedial actions and related costs and damages. The liability can change substantially due to factors such as the nature and extent of contamination, changes in remedial requirements, and technological changes, among others.

Alcoa s remediation reserve balance was $532 and $347 at December 31, 2012 and 2011 (of which $74 and $58 was classified as a current liability), respectively, and reflects the most probable costs to remediate identified environmental conditions for which costs can be reasonably estimated.

In 2012, the remediation reserve was increased by $206 due to charges of $165 related to the Massena West, NY site (see below), charges totaling $45 related to smelter sites in Canada and Norway (see below), a charge of $14 related to the former East St. Louis, IL site (see below), a reversal of $30 related to the former Sherwin, TX site (see below), and a net increase of $12 associated with a number of other sites. In 2011, the remediation reserve was increased by $31 due to charges of $18 related to the decision to permanently shut down and demolish a U.S. smelter (see Note D) and a net increase of $13 associated with a number of other sites. In both periods, the changes to the remediation reserve, except for the aforementioned $18 in 2011, were recorded in Cost of goods sold on the accompanying Statement of Consolidated Operations.

Payments related to remediation expenses applied against the reserve were $22 and $19 in 2012 and 2011, respectively. These amounts include expenditures currently mandated, as well as those not required by any regulatory authority or third party. In 2012 and 2011, the change in the reserve also reflects an increase of $1 and a decrease of $1, respectively, due to the effects of foreign currency translation. Additionally, the change in the 2011 reserve reflects an increase of $3 related to the acquisition of an aerospace fasteners business (see Note F).

Included in annual operating expenses are the recurring costs of managing hazardous substances and environmental programs. These costs are estimated to be approximately 2% of cost of goods sold.

The following discussion provides details regarding the current status of certain significant reserves related to current or former Alcoa sites.

Massena West, NY Alcoa has been conducting investigations and studies of the Grasse River, adjacent to Alcoa s Massena plant site, under a 1989 order from the U.S. Environmental Protection Agency (EPA) issued under CERCLA. Sediments and fish in the river contain varying levels of polychlorinated biphenyls (PCBs).

Alcoa submitted various Analysis of Alternatives Reports to the EPA starting in 1998 through 2002 that reported the results of river and sediment studies, potential alternatives for remedial actions related to the PCB contamination, and additional information requested by the EPA.

In June 2003, the EPA requested that Alcoa gather additional field data to assess the potential for sediment erosion from winter river ice formation and breakup. The results of these additional studies, submitted in a report to the EPA in April 2004, suggest that this phenomenon has the potential to occur approximately every 10 years and may impact sediments in certain portions of the river under all remedial scenarios. The EPA informed Alcoa that a final remedial decision for the river could not be made without substantially more information, including river pilot studies on the effects of ice formation and breakup on each of the remedial techniques. Alcoa submitted to the EPA, and the EPA

approved, a Remedial Options Pilot Study (ROPS) to gather this information. The scope of this study included sediment removal and capping, the installation of an ice control structure, and significant monitoring.

From 2004 through 2008, Alcoa completed the work outlined in the ROPS. In November 2008, Alcoa submitted an update to the EPA incorporating the new information obtained from the ROPS related to the feasibility and costs associated with various capping and dredging alternatives, including options for ice control. As a result, Alcoa increased the reserve associated with the Grasse River by $40 for the estimated costs of a proposed ice control remedy and for partial settlement of potential damages of natural resources.

In late 2009, the EPA requested that Alcoa submit a complete revised Analysis of Alternatives Report in March 2010 to address questions and comments from the EPA and various stakeholders. On March 24, 2010, Alcoa submitted the revised report, which included an expanded list of proposed remedial alternatives, as directed by the EPA. Alcoa increased the reserve associated with the Grasse River by $17 to reflect an increase in the estimated costs of the Company s recommended capping alternative as a result of changes in scope that occurred due to the questions and comments from the EPA and various stakeholders. While the EPA reviewed the revised report, Alcoa continued with its on-going monitoring and field studies activities. In late 2010, Alcoa increased the reserve by $2 based on the then most recent estimate of costs expected to be incurred for on-going monitoring and field studies activities. In late 2011, the EPA and various stakeholders completed their review of the March 2010 revised report and submitted questions and comments to Alcoa. As a result, Alcoa increased the reserve by $1 to reflect a revision in the estimate of costs expected to be incurred for on-going monitoring and field studies activities.

In the first half of 2012, Alcoa received final questions and comments from the EPA and other stakeholders on the revised Analysis of Alternatives Report submitted in March 2010, including a requirement that would increase the scope of the recommended capping alternative. In June 2012, Alcoa submitted a revised Analysis of Alternatives Report, which included four less alternatives than the previous report and addressed the final questions and comments from all stakeholders. These final questions and comments resulted in a change to Alcoa s recommended capping alternative by increasing the area to be remediated. Consequently, Alcoa increased the reserve associated with the Grasse River by $37 to reflect the changes to the recommended alternative.

In October 2012, the EPA selected a proposed remedy from the alternatives included in the June 2012 Analysis of Alternatives Report and released a Proposed Remedial Action Plan (PRAP). The alternative selected by the EPA recommends capping PCB contaminated sediments with concentration in excess of one part per million in the main channel of the river and dredging PCB contaminated sediments in the near-shore areas where total PCBs exceed one part per million. This alternative will result in additional estimated costs above that of the alternative recommended by Alcoa in the June 2012 Analysis of Alternatives Report. As a result, Alcoa increased the reserve associated with the Grasse River by $128 to reflect such additional estimated costs of the EPA s proposed remedy. The PRAP was open for public comment until November 29, 2012 (extended from November 15, 2012 due to the effects of Hurricane Sandy). The EPA is in the process of reviewing the comments received and, at the conclusion of that review, will issue a final Record of Decision (ROD), which may require Alcoa to record a subsequent reserve adjustment. Once a ROD is issued, the planning and design phase is expected to take approximately two to three years, followed by the actual remediation fieldwork that is expected to take approximately four years. The majority of the project funding is expected to be spent between 2016 and 2020.

Sherwin, TX In connection with the sale of the Sherwin alumina refinery, which was required to be divested as part of the Reynolds merger in 2000, Alcoa agreed to retain responsibility for the remediation of the then existing environmental conditions, as well as a pro rata share of the final closure of the active bauxite residue waste disposal areas (known as the Copano facility). Alcoa s share of the closure costs is proportional to the total period of operation of the active waste disposal areas. Alcoa estimated its liability for the active waste disposal areas by making certain assumptions about the period of operation, the amount of material placed in the area prior to closure, and the appropriate technology, engineering, and regulatory status applicable to final closure. The most probable cost for remediation was reserved.

For a number of years, Alcoa has been working with Sherwin Alumina Company to develop a sustainable closure plan for the active waste disposal areas, which is partly conditioned on Sherwin s operating plan for the Copano facility. In 2012, Alcoa received the technical analysis of the closure plan and the operating plan from Sherwin in order to develop a closure cost estimate, including an assessment of Alcoa s potential liability. It was determined that the most probable course of action would result in a smaller liability than originally reserved due to new information related to the amount of storage capacity in the waste disposal areas and revised assumptions regarding Alcoa s share of the obligation based on the operating plan provided by Sherwin. As such, Alcoa reduced the reserve associated with Sherwin by $30.

East St. Louis, IL In response to questions regarding environmental conditions at the former East St. Louis operations, Alcoa and the City of East St. Louis, the owner of the site, entered into an administrative order with the EPA in December 2002 to perform a remedial investigation and feasibility study of an area used for the disposal of bauxite residue from historic alumina refining operations. A draft feasibility study was submitted to the EPA in April 2005. The feasibility study included remedial alternatives that ranged from no further action to significant grading, stabilization, and water management of the bauxite residue disposal areas. As a result, Alcoa increased the environmental reserve for this location by $15 in 2005.

In April 2012, in response to comments from the EPA and other stakeholders, Alcoa submitted a revised feasibility study to the EPA, which soon thereafter issued a PRAP identifying a soil cover as the EPA s recommended alternative. Based on this recommendation, Alcoa submitted a detailed design and cost estimate for implementation of the remedy. A draft consent decree was issued in May 2012 by the EPA and all parties are actively engaged in negotiating a final consent decree and statement of work. As a result, Alcoa increased the reserve associated with East St. Louis by $14 to reflect the necessary costs for this remedy.

On July 30, 2012, the EPA issued a ROD for this matter and Alcoa began the process of bidding and contracting for the construction work. The ultimate outcome of negotiations and the bidding of the construction work could result in additional liability.

Fusina and Portovesme, Italy In 1996, Alcoa acquired the Fusina smelter and rolling operations and the Portovesme smelter, both of which are owned by Alcoa s subsidiary Alcoa Trasformazioni S.r.l. (Trasformazioni), from Alumix, an entity owned by the Italian Government. At the time of the acquisition, Alumix indemnified Alcoa for pre-existing environmental contamination at the sites. In 2004, the Italian Ministry of Environment (MOE) issued orders to Trasformazioni and Alumix for the development of a clean-up plan related to soil contamination in excess of allowable limits under legislative decree and to institute emergency actions and pay natural resource damages. Trasformazioni appealed the orders and filed suit against Alumix, among others, seeking indemnification for these liabilities under the provisions of the acquisition agreement. In 2009, Ligestra S.r.l. (Ligestra), Alumix s successor, and Trasformazioni agreed to a stay on the court proceedings while investigations were conducted and negotiations advanced towards a possible settlement.

In December 2009, Trasformazioni and Ligestra reached an agreement for settlement of the liabilities related to Fusina while negotiations continued related to Portovesme. The agreement outlines an allocation of payments to the MOE for emergency action and natural resource damages and the scope and costs for a proposed soil remediation project, which was formally presented to the MOE in mid-2010. The agreement is contingent upon final acceptance of the remediation project by the MOE. As a result of entering into this agreement, Alcoa increased the reserve by $12 for Fusina. Based on comments received from the MOE and local and regional environmental authorities, Trasformazioni submitted a revised remediation plan in the first half of 2012; however, such revisions did not require any change to the existing reserve.

Additionally, due to new information derived from the site investigations conducted at Portovesme, Alcoa increased the reserve by $3 in 2009. In November 2011, Trasformazioni and Ligestra reached an agreement for settlement of the liabilities related to Portovesme, similar to the one for Fusina. A proposed soil remediation project for Portovesme was formally presented to the MOE in June 2012. Neither the agreement with Ligestra nor the proposal to the MOE resulted in a change to the reserve for Portovesme.

Baie Comeau, Quebec, Canada In August 2012, Alcoa presented an analysis of remediation alternatives to the Quebec Ministry of Sustainable Development, Environment, Wildlife and Parks (MDDEP), in response to a previous request, related to known PCBs and polycyclic aromatic hydrocarbons (PAHs) contained in sediments of the Anse du Moulin bay. As such, Alcoa increased the reserve for Baie Comeau by $25 to reflect the estimated cost of Alcoa s recommended alternative, consisting of both dredging and capping of the contaminated sediments. The ultimate selection of a remedy may result in additional liability at the time the MDDEP issues a final decision.

Mosjøen, Norway In September 2012, Alcoa presented an analysis of remediation alternatives to the Norwegian Climate and Pollution Agency (known as Klif), in response to a previous request, related to known PAHs in the sediments located in the harbor and extending out into the fjord. As such, Alcoa increased the reserve for Mosjøen by $20 to reflect the estimated cost of the baseline alternative for dredging of the contaminated sediments. The ultimate selection of a remedy may result in additional liability at the time the Klif issues a final decision.

Other. In addition to the matters discussed above, various other lawsuits, claims, and proceedings have been or may be instituted or asserted against Alcoa, including those pertaining to environmental, product liability, safety and health, and tax matters. While the amounts claimed in these other matters may be substantial, the ultimate liability cannot now be determined because of the considerable uncertainties that exist. Therefore, it is possible that the Company s liquidity or results of operations in a particular period could be materially affected by one or more of these other matters. However, based on facts currently available, management believes that the disposition of these other matters that are pending or asserted will not have a material adverse effect, individually or in the aggregate, on the financial position of the Company.

Commitments

Investments. Alumínio, a wholly-owned subsidiary of Alcoa, is a participant in four consortiums that each owns a hydroelectric power project in Brazil. The purpose of Alumínio s participation is to increase its energy self-sufficiency and provide a long-term, low-cost source of power for its two smelters and one refinery. These projects are known as Machadinho, Barra Grande, Serra do Facão, and Estreito.

Alumínio committed to taking a share of the output of the Machadinho and Barra Grande projects each for 30 years and the Serra do Facão and Estreito projects each for 26 years at cost (including cost of financing the project). In the event that other participants in any of these projects fail to fulfill their financial responsibilities, Alumínio may be required to fund a portion of the deficiency. In accordance with the respective agreements, if Alumínio funds any such deficiency, its participation and share of the output from the respective project will increase proportionately.

The Barra Grande project reached full capacity in 2006. Alumínio s investment in this project is 42.18% and is accounted for under the equity method. This entitles Alumínio to approximately 160 megawatts of assured power. Alumínio s total investment in this project was $159 (R$326) and $169 (R$314) at December 31, 2012 and 2011, respectively.

The Machadinho project reached full capacity in 2002. Alumínio s investment in this project is 30.99% and is accounted for under the equity method. This entitles Alumínio to approximately 120 megawatts of assured power. Alumínio s total investment in this project was $95 (R$195) and $97 (R$182) at December 31, 2012 and 2011, respectively. Alumínio has also issued a third-party guarantee related to its share of the consortium s debt. Alcoa s maximum exposure to loss on this project is approximately $120 (R$240), which represents Alumínio s investment and guarantee of debt as of December 31, 2012.

The Serra do Facão project reached full capacity in 2010. Alumínio s investment in this project is 34.97% and is accounted for under the equity method. This entitles Alumínio to approximately 65 megawatts of assured power. Alumínio s total investment in this project was $98 (R$200) and $105 (R$196) at December 31, 2012 and 2011, respectively. Alumínio previously issued a third-party guarantee related to its share of the consortium s debt; however, in October 2012, the lender released all of the consortium s investors from their respective guarantees.

Even though the Serra do Facão project has been fully operational since 2010, construction costs continue to be incurred to complete the facility related to environmental compliance in accordance with the installation license. Total estimated project costs are approximately $490 (R$1,000) and Alumínio s share is approximately $170 (R$350). As of December 31, 2012, approximately $170 (R$350) of Alumínio s commitment was expended on the project (includes both funds provided by Alumínio and Alumínio s share of the long-term financing).

The Estreito project is expected to reach full capacity in March 2013. Alumínio s investment in this project is 25.49%, which entitles Alumínio to approximately 150 megawatts of assured power. The Estreito consortium is an unincorporated joint venture, and, therefore, Alumínio s share of the assets and liabilities of the consortium are reflected in the respective lines on the accompanying Consolidated Balance Sheet. Total estimated project costs are approximately $2,520 (R$5,170) and Alumínio s share is approximately $640 (R$1,320). These amounts reflect an approved increase by the consortium in 2012 of approximately $130 (R$270) to complete the Estreito project due to fluctuations in currency, inflation, and the price and scope of construction, among other factors. As of December 31, 2012, approximately $610 (R$1,250) of Alumínio s commitment was expended on the project.

Based on the operational capabilities of all four projects at the end of 2012, Alumínio s current power self-sufficiency satisfies almost 70% of a total energy demand of approximately 690 megawatts from two smelters (São Luís (Alumar) and Poços de Caldas) and one refinery (Poços de Caldas) in Brazil.

In 2004, Alcoa acquired a 20% interest in a consortium, which subsequently purchased the Dampier to Bunbury Natural Gas Pipeline (DBNGP) in Western Australia, in exchange for an initial cash investment of $17 (A$24). The investment in the DBNGP, which is classified as an equity investment, was made in order to secure a competitively priced long-term supply of natural gas to Alcoa s refineries in Western Australia. Alcoa has made additional contributions of $141 (A$176) for its share of the pipeline capacity expansion and other operational purposes of the consortium through September 2011. No further expansion of the pipeline s capacity is planned at this time. In late 2011, the consortium initiated a three-year equity call plan to improve its capitalization structure. This plan requires Alcoa to contribute $40 (A$40), of which $12 (A$11) and $5 (A$6) was made in 2012 and 2011, respectively. In addition to its equity ownership, Alcoa has an agreement to purchase gas transmission services from the DBNGP. At December 31, 2012, Alcoa has an asset of $363 (A$349) representing prepayments made under the agreement for future gas transmission services. Alcoa s maximum exposure to loss on the investment and the related contract is approximately $520 (A$500) as of December 31, 2012.

Purchase Obligations. Alcoa is party to unconditional purchase obligations for energy that expire between 2015 and 2036. Commitments related to these contracts total $176 in 2013, $175 in 2014, $176 in 2015, $165 in 2016, $165 in 2017, and $2,688 thereafter. Expenditures under these contracts totaled $161 in 2012, $227 in 2011, and $129 in 2010. Additionally, Alcoa has entered into other purchase commitments for energy, raw materials, and other goods and services, which total $3,502 in 2013, $2,137 in 2014, $2,085 in 2015, $1,926 in 2016, $2,496 in 2017, and $20,717 thereafter.

Operating Leases. Certain computer equipment, plant equipment, vehicles, and buildings and alumina refinery process control technology are under operating lease agreements. Total expense from continuing operations for all leases was $244 in 2012, $255 in 2011, and $260 in 2010. Under long-term operating leases, minimum annual rentals are $198 in 2013, $155 in 2014, $127 in 2015, $102 in 2016, $77 in 2017, and $597 thereafter.

Guarantees. At December 31, 2012, Alcoa has maximum potential future payments for guarantees issued on behalf of certain third parties of $621. These guarantees expire in 2015 through 2019 and relate to project financing for a hydroelectric power project in Brazil (see Investments section above) and the aluminum complex in Saudi Arabia (see Note I). Alcoa also has outstanding bank guarantees related to tax matters, outstanding debt, workers compensation, environmental obligations, energy contracts, and customs duties, among others. The total amount committed under these guarantees, which expire at various dates between 2013 and 2017, was $494 at December 31, 2012.

Letters of Credit. Alcoa has outstanding letters of credit primarily related to workers compensation, energy contracts, and leasing obligations. The total amount committed under these letters of credit, which automatically renew or expire at various dates, mostly in 2013, was $299 at December 31, 2012.

Surety Bonds. Alcoa has outstanding surety bonds primarily related to tax matters, contract performance, workers compensation, environmental-related matters, and customs duties. The total amount committed under these bonds, which automatically renew or expire at various dates, mostly in 2013 and 2014, was $193 at December 31, 2012.

O. Other (Income) Expenses, Net

	2012	2011	2010
Equity loss (income)	$ 28	$ (15)	$ (14)
Interest income	(31)	(20)	(19)
Foreign currency (gains) losses, net	(5)	16	13
Net gain from asset sales	(321)	(41)	(9)
Net (gain) loss on mark-to-market derivative contracts (X)	(13)	(52)	37
Other, net	1	25	(3)
	$ (341)	$ (87)	$ 5

In 2012, Net gain from asset sales included a $320 gain related to the sale of the Tapoco Hydroelectric Project (see Note F). In 2011, Equity income included higher earnings from an investment in a natural gas pipeline in Australia due to the recognition of a discrete income tax benefit by the consortium (Alcoa World Alumina and Chemicals share of the benefit was $24). Also in 2011, Net gain from asset sales included a $43 gain related to the sale of land in Australia.

P. Cash Flow Information

Cash paid for interest and income taxes was as follows:

	2012	2011	2010
Interest, net of amount capitalized	$ 454	$ 491	$ 452
Income taxes, net of amount refunded	223	382	(67)

The details related to cash paid for acquisitions were as follows:

	2012	2011	2010
Assets acquired	$ -	$ 253	$ 87
Liabilities assumed	-	(12)	(15)
Noncontrolling interests acquired	-	-	4
Redemption of convertible securities of subsidiary	-	-	40
Reduction in Alcoa shareholders equity	-	-	22
Cash paid	-	241	138
Less: cash acquired	-	1	-
Net cash paid	$ -	$ 240	$ 138

Noncash Financing and Investing Activities. In August 2012, Alcoa received a loan of $250 for the purpose of financing all or part of the cost of acquiring, constructing, reconstructing, and renovating certain facilities at Alcoa s rolling mill plant in Davenport, IA (see Note K). Because this loan can only be used for this purpose, the net proceeds of $248 were classified as restricted cash. Since restricted cash is not part of cash and cash equivalents, this transaction was not reflected in the accompanying Statement of Consolidated Cash Flows as it represents a noncash activity. As funds are expended for the project, the release of the cash will be reflected as both an inflow on the Net change in restricted cash line and an outflow on the Capital expenditures line in the Investing Activities section of the Statement of Consolidated Cash Flows. At December 31, 2012, Alcoa had $171 of restricted cash remaining related to this transaction.

In 2011 and 2010, Alcoa issued $600 in common stock to satisfy a portion of its accrued pension benefits liability (see Notes R and W).

Q. Segment and Geographic Area Information

Alcoa is primarily a producer of aluminum products. Aluminum and alumina represent more than 80% of Alcoa s revenues. Nonaluminum products include precision castings and aerospace and industrial fasteners. Alcoa s segments are organized by product on a worldwide basis. Segment performance under Alcoa s management reporting system is evaluated based on a number of factors; however, the primary measure of performance is the after-tax operating income (ATOI) of each segment. Certain items such as the impact of LIFO inventory accounting; interest expense; noncontrolling interests; corporate expense (general administrative and selling expenses of operating the corporate headquarters and other global administrative facilities, along with depreciation and amortization on corporate-owned assets); restructuring and other charges; discontinued operations; and other items, including intersegment profit eliminations and other metal adjustments, differences between tax rates applicable to the segments and the consolidated effective tax rate, the results of the soft alloy extrusions business in Brazil, and other nonoperating items such as foreign currency transaction gains/losses and interest income are excluded from segment ATOI. Segment assets exclude, among others, cash and cash equivalents; deferred income taxes; goodwill not allocated to businesses for segment reporting purposes; corporate fixed assets; LIFO reserves; and other items, including the assets of the soft alloy extrusions business in Brazil and assets classified as held for sale related to discontinued operations.

The accounting policies of the segments are the same as those described in the Summary of Significant Accounting Policies (see Note A). Transactions among segments are established based on negotiation among the parties. Differences between segment totals and Alcoa s consolidated totals for line items not reconciled are in Corporate.

Alcoa s products are used worldwide in transportation (including aerospace, automotive, truck, trailer, rail, and shipping), packaging, building and construction, oil and gas, defense, and industrial applications. Total export sales from the U.S. included in continuing operations were $2,107 in 2012, $1,988 in 2011, and $1,543 in 2010.

Alcoa s operations consist of four worldwide reportable segments as follows:

Alumina. This segment represents a portion of Alcoa s upstream operations and consists of the Company s worldwide refinery system, including the mining of bauxite, which is then refined into alumina. Alumina is mainly sold directly to internal and external smelter customers worldwide or is sold to customers who process it into industrial chemical products. A portion of this segment s third-party sales are completed through the use of agents, alumina traders, and distributors. Slightly more than half of Alcoa s alumina production is sold under supply contracts to third parties worldwide, while the remainder is used internally by the Primary Metals segment.

Primary Metals. This segment represents a portion of Alcoa s upstream operations and consists of the Company s worldwide smelter system. Primary Metals receives alumina, mostly from the Alumina segment, and produces primary aluminum used by Alcoa s fabricating businesses, as well as sold to external customers, aluminum traders, and commodity markets. Results from the sale of aluminum powder, scrap, and excess power are also included in this segment, as well as the results of aluminum derivative contracts and buy/resell activity. Primary aluminum produced by Alcoa and used internally is transferred to other segments at prevailing market prices. The sale of primary aluminum represents more than 90% of this segment s third-party sales. Buy/resell activity refers to when this segment purchases metal from external or internal sources and resells such metal to external customers or the midstream and downstream segments in order to maximize smelting system efficiency and to meet customer requirements.

Global Rolled Products. This segment represents Alcoa s midstream operations, whose principal business is the production and sale of aluminum plate and sheet. A small portion of this segment s operations relate to foil produced at one plant in Brazil. This segment includes rigid container sheet (RCS), which is sold directly to customers in the packaging and consumer market and is used to produce aluminum beverage cans. Seasonal increases in RCS sales are generally experienced in the second and third quarters of the year. This segment also includes sheet and plate used in the aerospace, automotive, commercial transportation, and building and construction markets (mainly used in the

production of machinery and equipment and consumer durables), which is sold directly to customers and through distributors. Approximately one-half of the third-party sales in this segment consist of RCS, while the other one-half of third-party sales are derived from sheet and plate and foil used in industrial markets. While the customer base for flat-rolled products is large, a significant amount of sales of RCS, sheet, and plate is to a relatively small number of customers.

Engineered Products and Solutions. This segment represents Alcoa s downstream operations and includes titanium, aluminum, and super alloy investment castings; forgings and fasteners; aluminum wheels; integrated aluminum structural systems; and architectural extrusions used in the aerospace, automotive, building and construction, commercial transportation, and power generation markets. These products are sold directly to customers and through distributors. Additionally, hard alloy extrusions products, which are also sold directly to customers and through distributors, serve the aerospace, automotive, commercial transportation, and industrial products markets.

The operating results and assets of Alcoa s reportable segments were as follows:

	Alumina	Primary Metals	Global Rolled Products	Engineered Products and Solutions	Total
2012					
Sales:					
Third-party sales	$ 3,092	$ 7,432	$ 7,378	$ 5,525	$ 23,427
Intersegment sales	2,310	2,877	163	-	5,350
Total sales	$ 5,402	$ 10,309	$ 7,541	$ 5,525	$ 28,777
Profit and loss:					
Equity income (loss)	$ 5	$ (27)	$ (6)	$ -	$ (28)
Depreciation, depletion, and amortization	455	532	229	158	1,374
Income taxes	(27)	106	167	297	543
ATOI	90	309	358	612	1,369
2011					
Sales:					
Third-party sales	$ 3,462	$ 8,240	$ 7,642	$ 5,345	$ 24,689
Intersegment sales	2,727	3,192	218	-	6,137
Total sales	$ 6,189	$ 11,432	$ 7,860	$ 5,345	$ 30,826
Profit and loss:					
Equity income (loss)	$ 25	$ (7)	$ (3)	$ 1	$ 16
Depreciation, depletion, and amortization	444	556	237	158	1,395
Income taxes	179	92	104	260	635
ATOI	607	481	266	539	1,893
2010					
Sales:					
Third-party sales	$ 2,815	$ 7,070	$ 6,277	$ 4,584	$ 20,746
Intersegment sales	2,212	2,597	180	-	4,989
Total sales	$ 5,027	$ 9,667	$ 6,457	$ 4,584	$ 25,735
Profit and loss:					
Equity income	$ 10	$ 1	$ -	$ 2	$ 13
Depreciation, depletion, and amortization	406	571	238	154	1,369
Income taxes	60	96	92	195	443
ATOI	301	488	220	415	1,424
2012					
Assets:					
Capital expenditures	$ 374	$ 318	$ 258	$ 200	$ 1,150
Equity investments	658	917	188	-	1,763
Goodwill	10	997	214	2,677	3,898
Total assets	9,709	11,709	4,603	5,891	31,912
2011					
Assets:					
Capital expenditures	$ 371	$ 463	$ 157	$ 173	$ 1,164
Equity investments	450	925	123	-	1,498
Goodwill	11	991	208	2,666	3,876
Total assets	9,782	11,867	4,559	5,831	32,039

The following tables reconcile certain segment information to consolidated totals:

	2012	2011	2010
Sales:			
Total segment sales	$ 28,777	$ 30,826	$ 25,735
Elimination of intersegment sales	(5,350)	(6,137)	(4,989)
Corporate*	273	262	267
Consolidated sales	$ 23,700	$ 24,951	$ 21,013

* For all periods presented, the Corporate amount includes third-party sales of three soft alloy extrusion facilities located in Brazil.

	2012	2011	2010
Net income attributable to Alcoa:			
Total segment ATOI	$ 1,369	$ 1,893	$ 1,424
Unallocated amounts (net of tax):			
Impact of LIFO	20	(38)	(16)
Interest expense	(319)	(340)	(321)
Noncontrolling interests	29	(194)	(138)
Corporate expense	(282)	(290)	(291)
Restructuring and other charges	(75)	(196)	(134)
Discontinued operations	-	(3)	(8)
Other	(551)	(221)	(262)
Consolidated net income attributable to Alcoa	$ 191	$ 611	$ 254

December 31,	2012	2011
Assets:		
Total segment assets	$ 31,912	$ 32,039
Elimination of intersegment receivables	(444)	(483)
Unallocated amounts:		
Cash and cash equivalents	1,861	1,939
Deferred income taxes	4,061	3,738
Corporate goodwill	1,272	1,281
Corporate fixed assets, net	961	935
LIFO reserve	(770)	(801)
Other	1,326	1,472
Consolidated assets	$ 40,179	$ 40,120

Sales by major product grouping were as follows:

	2012	2011	2010
Sales:			
Alumina	$ 2,962	$ 3,350	$ 2,740
Primary aluminum	7,121	7,907	6,842
Flat-rolled aluminum	7,378	7,642	6,277
Investment castings	1,747	1,700	1,521
Fastening systems	1,414	1,313	1,070
Architectural aluminum systems	970	973	884
Aluminum wheels	692	656	475
Other extruded aluminum and forged products	955	1,010	930
Other	461	400	274
	$ 23,700	$ 24,951	$ 21,013

Geographic information for sales was as follows (based upon the country where the point of sale occurred):

	2012	2011	2010
Sales:			
U.S.*	$ 12,361	$ 12,295	$ 10,560
Australia	3,222	3,587	2,842
Brazil	1,244	1,371	1,182
Spain	1,203	1,487	1,234
Netherlands**	949	1,025	940
Norway	820	927	809
France	807	825	662
Russia	713	761	584
Hungary	492	665	505
United Kingdom	438	412	331
Italy	379	537	418
China	326	283	188
Germany	216	229	231
Other	530	547	527
	$ 23,700	$ 24,951	$ 21,013

* Sales that occurred in the U.S. include a portion of alumina from Alcoa s refineries in Suriname, Brazil, Australia, and Jamaica and aluminum from the Company s smelters in Canada.

** Sales that occurred in the Netherlands include aluminum from Alcoa s smelter in Iceland.

Geographic information for long-lived assets was as follows (based upon the physical location of the assets):

December 31,	2012	2011
Long-lived assets:		
U.S.	$ 4,621	$ 4,439
Brazil	4,318	4,844
Australia	3,548	3,390
Iceland	1,571	1,615
Canada	1,399	1,447
Norway	898	894
Russia	494	531
Spain	445	451
Jamaica	414	417
China	395	424
Other	844	830
	$ 18,947	$ 19,282

R. Preferred and Common Stock

Preferred Stock. Alcoa has two classes of preferred stock: Class A Preferred Stock and Class B Serial Preferred Stock. Class A Preferred Stock has 660,000 shares authorized at a par value of $100 per share with an annual $3.75 cumulative dividend preference per share. There were 546,024 of such shares outstanding at December 31, 2012 and 2011. Class B Serial Preferred Stock has 10 million shares authorized (none issued) and a par value of $1 per share.

Common Stock. There are 1.8 billion shares authorized at a par value of $1 per share, and 1,177,906,557 shares were issued at December 31, 2012 and 2011. The current dividend yield as authorized by Alcoa s Board of Directors is $0.12 per annum or $0.03 per quarter.

In January 2011, Alcoa contributed 36,518,563 newly issued shares of its common stock to a master trust that holds the assets of certain U.S. defined benefit pension plans in a private placement transaction. These shares were valued at $16.43 per share (the closing price of Alcoa s common stock on January 24, 2011), or $600 in the aggregate, and were issued to satisfy the estimated minimum required funding and to provide additional funding towards maintaining an approximately 80% funded status of Alcoa s U.S. pension plans. On January 25, 2011, the 36,518,563 shares were registered under Alcoa s then-current shelf registration statement dated March 10, 2008 (replaced by shelf registration statement dated February 18, 2011) for resale by the master trust, as selling stockholder.

In January 2010, Alcoa contributed 44,313,146 newly issued shares of its common stock to a master trust that holds the assets of certain U.S. defined benefit pension plans in a private placement transaction. These shares were valued at $13.54 per share (the closing price of Alcoa s common stock on January 26, 2010), or $600 in the aggregate, and were issued to satisfy a portion of Alcoa s future funding obligations to these plans, including a portion of the estimated minimum required funding for 2011. On January 27, 2010, the 44,313,146 shares were registered under Alcoa s then-current shelf registration statement dated March 10, 2008 for resale by the master trust, as selling stockholder.

As of December 31, 2012, 110 million and 86 million shares of common stock were reserved for issuance upon conversion of convertible notes and under Alcoa s stock-based compensation plans, respectively. Alcoa issues shares from treasury stock to satisfy the exercise of stock options and the conversion of stock awards.

Share Activity (number of shares)

	Common stock	
	Treasury	**Outstanding**
Balance at end of 2009	122,695,718	974,378,820
Private placement	-	44,313,146
Conversion of convertible notes	-	310
Issued for stock-based compensation plans	(3,333,689)	3,333,689
Balance at end of 2010	119,362,029	1,022,025,965
Private placement	-	36,518,563
Issued for stock-based compensation plans	(5,867,538)	5,867,538
Balance at end of 2011	113,494,491	1,064,412,066
Issued for stock-based compensation plans	(2,799,887)	2,799,887
Balance at end of 2012	110,694,604	1,067,211,953

Stock-based Compensation

Stock options under Alcoa s stock-based compensation plans are granted in January each year at market prices on the dates of grant. Prior to 2011, performance stock options were also granted to certain individuals. For performance stock options granted in 2010, the final number of options earned was based on Alcoa s adjusted free cash flow and profitability against pre-established targets. Stock option features based on date of original grant were as follows:

Date of original grant	**Vesting**	**Term**	**Reload feature**
2002 and prior	1 year	10 years	One reload over option term
2003	3 years (1/3 each year)	10 years	One reload in 2004 for 1/3 vesting in 2004
2004 - 2009	3 years (1/3 each year)	6 years	None
2010 and forward	3 years	10 years	None

(1/3 each year)

130

In addition to the stock options described above, Alcoa grants stock awards that vest three years from the date of grant. In 2010, certain of these stock awards were granted with the same performance conditions described above for performance stock options. In 2012 and 2011, the final number of performance stock awards earned will be based on the achievement of sales and profitability targets over a three-year period. One-third of the award will be earned each year based on the performance against pre-established targets for that year. The performance stock awards earned over the three-year period vest at the end of the third year.

Most plan participants can choose whether to receive their award in the form of stock options, stock awards, or a combination of both. This choice is made before the grant is issued and is irrevocable.

The following table summarizes the total compensation expense recognized for all stock options and stock awards (there was no stock-based compensation expense capitalized in 2012, 2011, or 2010):

	2012	2011	2010
Compensation expense recognized:			
Stock option grants	$ 27	$ 34	$ 44
Stock award grants	40	49	40
Total compensation expense before income taxes	67	83	84
Benefit for income taxes	21	27	27
Total compensation expense, net of income taxes	$ 46	$ 56	$ 57

As part of Alcoa s stock-based compensation plan design, individuals who are retirement-eligible have a six-month requisite service period in the year of grant. As a result, a larger portion of expense will be recognized in the first half of each year for these retirement-eligible employees. Of the total compensation expense before income taxes included in the table above, $13, $18, and $19 in 2012, 2011, and 2010, respectively, pertains to the acceleration of expense related to retirement-eligible employees.

The fair value of new options was estimated on the date of grant using a lattice-pricing model with the following assumptions:

	2012	2011	2010
Weighted average fair value per option	$ 3.11	$ 4.96	$ 4.67
Average risk-free interest rate	0.06-1.89%	0.19-3.44%	0.14-3.62%
Dividend yield	0.9%	0.9%	1.1%
Volatility	39-45%	36-43%	47-51%
Annual forfeiture rate	5%	5%	4%
Exercise behavior	45%	45%	35%
Life (years)	5.8	5.8	5.6

The range of average risk-free interest rates was based on a yield curve of interest rates at the time of the grant based on the contractual life of the option. The dividend yield was based on a one-year average. Volatility was based on historical and implied volatilities over the term of the option. Alcoa utilized historical option forfeiture data to estimate annual pre- and post-vesting forfeitures. Exercise behavior was based on a weighted average exercise ratio (exercise patterns for grants issued over the number of years in the contractual option term) of an option s intrinsic value resulting from historical employee exercise behavior. Based upon the other assumptions used in the determination of the fair value, the life of an option was an output of the lattice-pricing model.

The activity for stock options was as follows (options in millions):

	2012	2011	2010
Outstanding, beginning of year:			
Number of options	46.8	56.1	65.5
Weighted average exercise price	$ 17.41	$ 19.29	$ 24.44
Granted:			
Number of options	10.5	4.5	9.0
Weighted average exercise price	$ 10.17	$ 16.24	$ 13.52
Exercised:			
Number of options	(1.5)	(4.3)	(1.6)
Weighted average exercise price	$ 8.28	$ 8.59	$ 8.34
Expired or forfeited:			
Number of options	(10.8)	(9.5)	(16.8)
Weighted average exercise price	$ 31.83	$ 31.90	$ 37.21
Outstanding, end of year:			
Number of options	45.0	46.8	56.1
Weighted average exercise price	$ 12.58	$ 17.41	$ 19.29
Exercisable, end of year:			
Number of options	29.8	28.8	30.2
Weighted average exercise price	$ 13.02	$ 20.90	$ 26.91

The total intrinsic value of options exercised during 2012, 2011, and 2010 was $2, $34, and $8, respectively. In 2012, 2011, and 2010, the cash received from option exercises was $12, $37, and $13 and the total tax benefit realized from these exercises was $1, $11, and $2, respectively.

The following tables summarize certain stock option information at December 31, 2012 (number of options and intrinsic value in millions):

Options Fully Vested and/or Expected to Vest*

Range of exercise price	Number	Weighted average remaining contractual life	Weighted average exercise price	Intrinsic Value
$6.12 - $8.33	17.9	2.06	$ 8.33	$ 7
$8.34 - $11.33	10.3	8.93	10.17	-
$11.34 - $17.40	11.2	7.21	14.47	-
$17.41 - $46.77	5.6	0.26	26.96	-
Total	45.0	4.69	12.58	$ 7

* Expected forfeitures are immaterial to the Company and are not reflected in the table above.

Options Fully Vested and Exercisable

Range of exercise price	Number	Weighted average remaining contractual life	Weighted average exercise price	Intrinsic Value
$6.12 - $8.33	17.9	2.06	$ 8.33	$ 7
$8.34 - $11.33	0.1	6.65	10.72	-
$11.34 - $17.40	6.2	7.07	14.10	-
$17.41 - $46.77	5.6	0.26	26.96	-
Total	29.8	2.77	13.02	$ 7

In addition to stock option awards, the Company grants stock awards and performance share awards, both of which vest three years from the date of grant. Performance share awards are issued at target and the final award amount is determined at the end of the performance period.

The following table summarizes the outstanding stock and performance share awards (awards in millions):

	Stock Awards	Performance Share Awards	Total	Weighted average FMV per award
Outstanding, January 1, 2012	6.4	2.9	9.3	$ 13.63
Granted	3.0	1.9	4.9	10.08
Converted	(1.0)	(0.8)	(1.8)	8.42
Forfeited	(0.5)	(0.2)	(0.7)	13.49
Performance share adjustment	-	0.2	0.2	12.74
Outstanding, December 31, 2012	7.9	4.0	11.9	12.96

At December 31, 2012, there was $22 and $35 of unrecognized compensation expense (pretax) related to non-vested stock option grants and non-vested stock award grants, respectively. This expense is expected to be recognized over a weighted average period of 1.5 years. As of December 31, 2012, the following table summarizes the unrecognized compensation expense expected to be recognized in future periods:

	Stock-based compensation expense (pretax)
2013	$ 38
2014	18
2015	1
Totals	$ 57

S. Earnings Per Share

Basic earnings per share (EPS) amounts are computed by dividing earnings, after the deduction of preferred stock dividends declared and dividends and undistributed earnings allocated to participating securities, by the average number of common shares outstanding. Diluted EPS amounts assume the issuance of common stock for all potentially dilutive share equivalents outstanding not classified as participating securities.

The information used to compute basic and diluted EPS attributable to Alcoa common shareholders was as follows (shares in millions):

	2012	2011	2010
Income from continuing operations attributable to Alcoa common shareholders	$ 191	$ 614	$ 262
Less: preferred stock dividends declared	2	2	2
Income from continuing operations available to common equity	189	612	260
Less: dividends and undistributed earnings allocated to participating securities	-	1	1
Income from continuing operations available to Alcoa common shareholders basic	189	611	259
Add: interest expense related to convertible notes	-	30	-
Income from continuing operations available to Alcoa common shareholders diluted	$ 189	$ 641	$ 259
Average shares outstanding basic	1,067	1,061	1,018
Effect of dilutive securities:			
Stock options	3	7	6
Stock and performance awards	6	4	1
Convertible notes	-	89	-
Average shares outstanding diluted	1,076	1,161	1,025

Participating securities are defined as unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents (whether paid or unpaid) and are included in the computation of earnings per share pursuant to the two-class method. Prior to January 1, 2010, under Alcoa s stock-based compensation programs, certain employees were granted stock and performance awards, which entitle those employees to receive nonforfeitable dividends during the vesting period on a basis equivalent to the dividends paid to holders of Alcoa s common stock. As such, these unvested stock and performance awards met the definition of a participating security. Under the two-class method, all earnings, whether distributed or undistributed, are allocated to each class of common stock and participating securities based on their respective rights to receive dividends. At December 31, 2012, there were no outstanding participating securities, as all such securities have vested and were converted into shares of common stock. At December 31, 2011 and 2010 there were 2 million and 4 million participating securities outstanding, respectively.

Effective January 1, 2010, new grants of stock and performance awards do not contain a nonforfeitable right to dividends during the vesting period. As a result, an employee will forfeit the right to dividends accrued on unvested awards if that person does not fulfill their service requirement during the vesting period. As such, these awards are not treated as participating securities in the EPS calculation as the employees do not have equivalent dividend rights as common shareholders. These awards are included in the EPS calculation utilizing the treasury stock method similar to stock options. At December 31, 2012, 2011, and 2010, there were 12 million, 8 million, and 4 million such awards outstanding, respectively.

In 2012 and 2010, 89 million share equivalents related to convertible notes were not included in the computation of diluted EPS because their effect was anti-dilutive.

Options to purchase 27 million, 27 million, and 23 million shares of common stock at a weighted average exercise price of $15.41, $24.00, and $32.73 per share were outstanding as of December 31, 2012, 2011, and 2010, respectively, but were not included in the computation of diluted EPS because they were anti-dilutive, as the exercise prices of the options were greater than the average market price of Alcoa s common stock.

T. Income Taxes

The components of income from continuing operations before income taxes were as follows:

	2012	2011	2010
U.S.	$ 394	$ (98)	$ (403)
Foreign	(70)	1,161	951
	$ 324	$ 1,063	$ 548

The provision for income taxes on income from continuing operations consisted of the following:

	2012	2011	2010
Current:			
Federal*	$ 85	$ 10	$ 33
Foreign	167	427	409
State and local	9	(1)	(7)
	261	436	435
Deferred:			
Federal*	129	28	37
Foreign	(227)	(211)	(320)
State and local	(1)	2	(4)
	(99)	(181)	(287)
Total	$ 162	$ 255	$ 148

* Includes U.S. taxes related to foreign income

Included in discontinued operations is a tax benefit of $1 in 2011 and $3 in 2010.

The exercise of employee stock options generated a tax charge of $1 in 2012 and a tax benefit of $6 in 2011 and $2 in 2010, representing only the difference between compensation expense recognized for financial reporting and tax purposes. These amounts decreased or increased equity and increased or reduced current taxes payable in their respective periods.

Alcoa has unamortized tax-deductible goodwill of $97 resulting from intercompany stock sales and reorganizations. Alcoa recognizes the tax benefits (generally at a 30% to 34% rate) associated with this tax-deductible goodwill as it is being amortized for local income tax purposes rather than in the period in which the transaction is consummated.

A reconciliation of the U.S. federal statutory rate to Alcoa s effective tax rate for continuing operations was as follows:

	2012	2011	2010
U.S. federal statutory rate	35.0%	35.0%	35.0%
Taxes on foreign operations	(0.1)	(11.0)	(5.4)
Permanent differences on restructuring charges and asset disposals	10.8	-	0.7
Audit and other adjustments to prior years accruals	3.5	(1.1)	1.2
Noncontrolling interests	3.8	0.8	2.6
Statutory tax rate and law changes	(0.4)	0.8	(5.1)
Tax law change related to Medicare Part D	-	-	14.4
Changes in valuation allowances	15.2	2.3	(8.7)
Amortization of goodwill related to intercompany stock sales/reorganizations	(7.7)	(2.8)	(5.2)
Change in legal structure of investment	(4.1)	-	-
Interest income related to income tax positions	(1.3)	(0.2)	-
Company-owned life insurance/split-dollar net premiums	(3.9)	(0.2)	(1.8)
Other	(0.8)	0.4	(0.8)
Effective tax rate	50.0%	24.0%	26.9%

135

On March 23, 2010, the Patient Protection and Affordable Care Act (the PPACA) was signed into law, and, on March 30, 2010, the Health Care and Education Reconciliation Act of 2010 (the HCERA and, together with PPACA, the Acts), which makes various amendments to certain aspects of the PPACA, was signed into law. The Acts effectively change the tax treatment of federal subsidies paid to sponsors of retiree health benefit plans that provide prescription drug benefits that are at least actuarially equivalent to the corresponding benefits provided under Medicare Part D.

Alcoa pays a portion of the prescription drug cost for eligible retirees under certain postretirement benefit plans. These benefits were determined to be actuarially equivalent to the Medicare Part D prescription drug benefit of the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the MPDIMA). Alcoa has been receiving the federal subsidy since the 2006 tax year related to the aforementioned postretirement benefit plans. Under the MPDIMA, the federal subsidy did not reduce an employer s income tax deduction for the costs of providing such prescription drug plans nor was it subject to income tax individually.

Under the Acts, beginning in 2013, an employer s income tax deduction for the costs of providing Medicare Part D-equivalent prescription drug benefits to retirees will be reduced by the amount of the federal subsidy. Under GAAP, any impact from a change in tax law must be recognized in earnings in the period enacted regardless of the effective date. As a result, Alcoa recognized a noncash charge of $79 in 2010 for the elimination of a related deferred tax asset to reflect the change in the tax treatment of the federal subsidy.

The components of net deferred tax assets and liabilities were as follows:

	2012		2011	
December 31,	Deferred tax assets	Deferred tax liabilities	Deferred tax assets	Deferred tax liabilities
Depreciation	$ 104	$ 1,015	$ 74	$ 933
Employee benefits	2,742	46	2,668	51
Loss provisions	368	17	325	9
Deferred income/expense	53	203	45	181
Tax loss carryforwards	2,186	-	2,035	-
Tax credit carryforwards	508	-	477	-
Derivatives and hedging activities	117	16	109	43
Other	324	297	315	288
	6,402	1,594	6,048	1,505
Valuation allowance	(1,400)	-	(1,398)	-
	$ 5,002	$ 1,594	$ 4,650	$ 1,505

The following table details the expiration periods of the deferred tax assets presented above:

December 31, 2012	Expires within 10 years	Expires within 11-20 years	No expiration*	Other*	Total
Tax loss carryforwards	$ 332	$ 886	$ 968	$ -	$ 2,186
Tax credit carryforwards	370	73	65	-	508
Other	-	-	762	2,946	3,708
Valuation allowance	(212)	(659)	(244)	(285)	(1,400)
	$ 490	$ 300	$ 1,551	$ 2,661	$ 5,002

* Deferred tax assets with no expiration may still have annual limitations on utilization. Other represents deferred tax assets whose expiration is dependent upon the reversal of the underlying temporary difference. A substantial amount of Other relates to employee benefits that will become deductible for tax purposes over an extended period of time as contributions are made to employee benefit plans and payments are made to retirees.

The total deferred tax asset (net of valuation allowance) is supported by taxable temporary differences that reverse within the carryforward period (approximately 25%), tax planning strategies (approximately 5%), and projections of future taxable income exclusive of reversing temporary differences (approximately 70%).

Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized. In evaluating the need for a valuation allowance, management considers all potential sources of taxable income, including income available in carryback periods, future reversals of taxable temporary differences, projections of taxable income, and income from tax planning strategies, as well as all available positive and negative evidence. Positive evidence includes factors such as a history of profitable operations, projections of future profitability within the carryforward period, including from tax planning strategies, and the Company s experience with similar operations. Existing favorable contracts and the ability to sell product into established markets are additional positive evidence. Negative evidence includes items such as cumulative losses, projections of future losses, or carryforward periods that are not long enough to allow the utilization of the deferred tax asset based on existing projections of income. In certain jurisdictions, deferred tax assets related to cumulative losses exist without a valuation allowance where in management s judgment the weight of the positive evidence more than offsets the negative evidence of the cumulative losses. Upon changes in facts and circumstances, management may conclude that deferred tax assets for which no valuation allowance is currently recorded may not be realizable in future periods, resulting in a future charge to record a valuation allowance. Existing valuation allowances are re-examined under the same standards of positive and negative evidence. If it is determined that it is more likely than not that a deferred tax asset will be realized, the appropriate amount of the valuation allowance, if any, is released. Deferred tax assets and liabilities are also re-measured to reflect changes in underlying tax rates due to law changes and the granting and lapse of tax holidays.

In December 2011, one of the Company s subsidiaries in Brazil applied for a tax holiday related to its expanded mining and refining operations. If approved, the tax rate for this subsidiary will decrease significantly, resulting in future cash tax savings over the 10-year holiday period (would be effective as of January 1, 2013). Additionally, the net deferred tax asset of the subsidiary would be remeasured at the lower rate in the period the holiday is approved. This remeasurement would result in a decrease to the net deferred tax asset and a noncash charge to earnings of approximately $60 to $120. As of December 31, 2012, Alcoa s subsidiary s application is still pending.

The following table details the changes in the valuation allowance:

December 31,	2012	2011
Balance at beginning of year	$ 1,398	$ 1,268
Increase to allowance	45	157
Release of allowance	(48)	(25)
Foreign currency translation	5	(2)
Balance at end of year	$ 1,400	$ 1,398

The cumulative amount of Alcoa s foreign undistributed net earnings for which no deferred taxes have been provided was approximately $8,000 at December 31, 2012. Alcoa has a number of commitments and obligations related to the Company s growth strategy in foreign jurisdictions. As such, management has no plans to distribute such earnings in the foreseeable future, and, therefore, has determined it is not practicable to determine the related deferred tax liability.

Alcoa and its subsidiaries file income tax returns in the U.S. federal jurisdiction and various states and foreign jurisdictions. With a few minor exceptions, Alcoa is no longer subject to income tax examinations by tax authorities for years prior to 2002. All U.S. tax years prior to 2012 have been audited by the Internal Revenue Service. Various state and foreign jurisdiction tax authorities are in the process of examining Alcoa s income tax returns for various tax years through 2010.

A reconciliation of the beginning and ending amount of unrecognized tax benefits (excluding interest and penalties) was as follows:

December 31,	2012	2011	2010
Balance at beginning of year	$ 51	$ 46	$ 48
Additions for tax positions of the current year	-	-	-
Additions for tax positions of prior years	39	13	30
Reductions for tax positions of prior years	(7)	(3)	(5)
Settlements with tax authorities	(18)	(4)	(22)
Expiration of the statute of limitations	-	-	(5)
Foreign currency translation	1	(1)	-
Balance at end of year	$ 66	$ 51	$ 46

For all periods presented, a portion of the balance at end of year pertains to state tax liabilities, which are presented before any offset for federal tax benefits. The effect of unrecognized tax benefits, if recorded, that would impact the annual effective tax rate for 2012, 2011, and 2010 would be approximately 6%, 2%, and 4%, respectively, of pretax book income. Alcoa does not anticipate that changes in its unrecognized tax benefits will have a material impact on the Statement of Consolidated Operations during 2013.

It is Alcoa s policy to recognize interest and penalties related to income taxes as a component of the Provision for income taxes on the accompanying Statement of Consolidated Operations. In 2012, 2011, and 2010, Alcoa recognized $3, $2, and $1, respectively, in interest and penalties. Due to the expiration of the statute of limitations, settlements with tax authorities, and refunded overpayments, Alcoa also recognized interest income of $7, $2, and $4 in 2012, 2011, and 2010, respectively. As of December 31, 2012 and 2011, the amount accrued for the payment of interest and penalties was $15 and $12, respectively.

U. Receivables

Sale of Receivables Programs

Alcoa has three arrangements, each with a different financial institution, to sell certain customer receivables outright without recourse on a continuous basis. As of December 31, 2012, sold receivables, which were derecognized from the accompanying Consolidated Balance Sheet, in the amount of $37 under the three arrangements combined were uncollected. Alcoa services the customer receivables for the financial institutions at market rates; therefore, no servicing asset or liability was recorded.

On March 30, 2012, Alcoa finalized a one-year arrangement with a financial institution to sell certain customer receivables without recourse on a revolving basis. The sale of such receivables is completed through the use of a bankruptcy remote special purpose entity, which is a consolidated subsidiary of Alcoa. This arrangement provides for minimum funding of $50 up to a maximum of $250 for receivables sold. Alcoa initially sold $304 of customer receivables in exchange for $50 in cash and $254 of deferred purchase price under this arrangement. Alcoa received additional cash funding of $155 throughout 2012. As of December 31, 2012, the deferred purchase price receivable was $18, which was included in Other receivables on the accompanying Consolidated Balance Sheet. The deferred purchase price receivable is reduced as collections of the underlying receivables occur; however, as this is a revolving program, the sale of new receivables will result in an increase in the deferred purchase price receivable. The net change in the deferred purchase price receivable was reflected in the Decrease in receivables line item on the accompanying Statement of Consolidated Cash Flows. This activity is reflected as an operating cash flow because the related customer receivables are the result of an operating activity with an insignificant, short-term interest rate risk. In 2012, the gross cash outflows and inflows associated with the deferred purchase price receivable were $3,339 and $3,321, respectively. The gross amount of receivables sold and total cash collections under this program since its inception was $3,339 and $3,116, respectively. Alcoa services the customer receivables for the financial institution at market rates; therefore, no servicing asset or liability was recorded.

Allowance for Doubtful Accounts

The following table details the changes in the allowance for doubtful accounts related to customer receivables and other receivables:

	Customer receivables		Other receivables	
December 31,	**2012**	**2011**	**2012**	**2011**
Balance at beginning of year	$ 46	$ 46	$ 79	$ 87
Provision for doubtful accounts	2	19	9	7
Write off of uncollectible accounts	(8)	(14)	(3)	(3)
Recoveries of prior write-offs	(1)	(3)	(6)	(5)
Other	-	(2)	(5)	(7)
Balance at end of year	$ 39	$ 46	$ 74	$ 79

V. Interest Cost Components

	2012	2011	2010
Amount charged to expense	$ 490	$ 524	$ 494
Amount capitalized	93	101	96
	$ 583	$ 625	$ 590

W. Pension and Other Postretirement Benefits

Alcoa maintains pension plans covering most U.S. employees and certain employees in foreign locations. Pension benefits generally depend on length of service, job grade, and remuneration. Substantially all benefits are paid through pension trusts that are sufficiently funded to ensure that all plans can pay benefits to retirees as they become due. Most salaried and non-bargaining hourly U.S. employees hired after March 1, 2006 participate in a defined contribution plan instead of a defined benefit plan.

Alcoa also maintains health care and life insurance benefit plans covering eligible U.S. retired employees and certain retirees from foreign locations. Generally, the medical plans pay a percentage of medical expenses, reduced by deductibles and other coverages. These plans are generally unfunded, except for certain benefits funded through a trust. Life benefits are generally provided by insurance contracts. Alcoa retains the right, subject to existing agreements, to change or eliminate these benefits. All salaried and certain non-bargaining hourly U.S. employees hired after January 1, 2002 and certain bargaining hourly U.S. employees hired after July 1, 2010 are not eligible for postretirement health care benefits. All salaried and certain hourly U.S. employees that retire on or after April 1, 2008 are not eligible for postretirement life insurance benefits.

The funded status of all of Alcoa s pension and other postretirement benefit plans are measured as of December 31 each calendar year.

On June 24, 2010, the United Steelworkers ratified a new four-year labor agreement covering approximately 5,400 employees at 11 U.S. locations; the previous labor agreement expired on May 31, 2010. In 2010, as a result of the preparation for and ratification of the new agreement, Alcoa recognized $20 ($13 after-tax) in Cost of goods sold on the accompanying Statement of Consolidated Operations for strike preparation costs, a one-time signing bonus for employees, and an increase to pension net periodic benefit cost (see below). Additionally, as a result of the provisions of the new labor agreement, a significant plan amendment was adopted by one of Alcoa s U.S. pension plans. Accordingly, this plan was required to be remeasured, and through this process, the discount rate was updated from 6.15% at December 31, 2009 to 5.95% at May 31, 2010. The plan remeasurement resulted in an increase to both Alcoa s pension liability of $166 and the plan s unrecognized net actuarial loss (included in other comprehensive loss) of $108 (after-tax). The plan remeasurement also resulted in an increase to 2010 net periodic benefit cost of $9.

Obligations and Funded Status

December 31,	Pension benefits 2012	Pension benefits 2011	Other postretirement benefits 2012	Other postretirement benefits 2011
Change in benefit obligation				
Benefit obligation at beginning of year	$ 13,526	$ 12,343	$ 2,844	$ 2,902
Service cost	203	183	14	17
Interest cost	647	687	132	159
Amendments	6	40	-	(1)
Actuarial losses	1,120	1,163	107	17
Settlements	-	(32)	-	-
Curtailments	-	(7)	-	-
Benefits paid, net of participants contributions	(833)	(813)	(256)	(275)
Medicare Part D subsidy receipts	-	-	21	25
Foreign currency translation impact	82	(38)	1	-
Benefit obligation at end of year*	$ 14,751	$ 13,526	$ 2,863	$ 2,844
Change in plan assets				
Fair value of plan assets at beginning of year	$ 10,311	$ 9,451	$ 8	$ 58
Actual return on plan assets	925	783	-	2
Employer contributions	571	945	-	-
Participants contributions	32	35	-	-
Benefits paid	(822)	(805)	(8)	(52)
Administrative expenses	(42)	(38)	-	-
Settlements	-	(34)	-	-
Foreign currency translation impact	68	(26)	-	-
Fair value of plan assets at end of year*	$ 11,043	$ 10,311	$ -	$ 8
Funded status*	$ (3,708)	$ (3,215)	$ (2,863)	$ (2,836)
Less: Amounts attributed to joint venture partners	(40)	(34)	(4)	(5)
Net funded status	$ (3,668)	$ (3,181)	$ (2,859)	$ (2,831)
Amounts recognized in the Consolidated Balance Sheet consist of:				
Noncurrent assets	$ 86	$ 109	$ -	$ -
Current liabilities	(32)	(29)	(256)	(248)
Noncurrent liabilities	(3,722)	(3,261)	(2,603)	(2,583)
Net amount recognized	$ (3,668)	$ (3,181)	$ (2,859)	$ (2,831)
Amounts recognized in Accumulated Other Comprehensive Loss consist of:				
Net actuarial loss	$ 5,880	$ 5,191	$ 593	$ 511
Prior service cost (benefit)	119	129	(76)	(92)
Total, before tax effect	5,999	5,320	517	419
Less: Amounts attributed to joint venture partners	54	46	(1)	(1)
Net amount recognized, before tax effect	$ 5,945	$ 5,274	$ 518	$ 420
Other Changes in Plan Assets and Benefit Obligations Recognized in Other Comprehensive Loss consist of:				
Net actuarial loss	$ 1,073	$ 1,216	$ 107	$ 17
Amortization of accumulated net actuarial loss	(384)	(246)	(25)	(26)
Prior service cost (benefit)	9	42	-	(1)
Amortization of prior service (cost) benefit	(19)	(19)	16	17
Total, before tax effect	679	993	98	7
Less: Amounts attributed to joint venture partners	8	10	-	(1)
Net amount recognized, before tax effect	$ 671	$ 983	$ 98	$ 8

* At December 31, 2012, the benefit obligation, fair value of plan assets, and funded status for U.S. pension plans were $11,521, $8,437, and $(3,084), respectively. At December 31, 2011, the benefit obligation, fair value of plan assets, and funded status for U.S. pension plans were $10,702, $7,988, and $(2,714), respectively.

Pension Plan Benefit Obligations

	Pension benefits	
	2012	2011
The projected benefit obligation and accumulated benefit obligation for all defined benefit pension plans was as follows:		
Projected benefit obligation	$ 14,751	$ 13,526
Accumulated benefit obligation	14,186	13,025
The aggregate projected benefit obligation and fair value of plan assets for pension plans with projected benefit obligations in excess of plan assets was as follows:		
Projected benefit obligation	13,973	12,828
Fair value of plan assets	10,142	9,470
The aggregate accumulated benefit obligation and fair value of plan assets for pension plans with accumulated benefit obligations in excess of plan assets was as follows:		
Accumulated benefit obligation	13,421	12,184
Fair value of plan assets	10,123	9,281

Components of Net Periodic Benefit Cost

	Pension benefits[1]			Other postretirement benefits[2]		
	2012	2011	2010	2012	2011	2010
Service cost	$ 186	$ 165	$ 148	$ 14	$ 17	$ 20
Interest cost	639	678	682	131	158	174
Expected return on plan assets	(808)	(806)	(787)	-	(2)	(7)
Recognized net actuarial loss	384	247	181	25	26	33
Amortization of prior service cost (benefit)	19	19	17	(16)	(17)	(15)
Settlements[3]	-	2	2	-	-	(3)
Curtailments[4]	-	(9)	(10)	-	-	-
Net periodic benefit cost[5]	$ 420	$ 296	$ 233	$ 154	$ 182	$ 202

(1) In 2012, 2011, and 2010, net periodic benefit cost for U.S pension plans was $288, $190, and $155, respectively.

(2) In 2012, 2011, and 2010, net periodic benefit cost for other postretirement benefits reflects a reduction of $64, $43, and $39, respectively, related to the recognition of the federal subsidy awarded under Medicare Part D.

(3) In all periods presented, settlements were due to the payment of significant lump sum benefits and/or purchases of annuity contracts.

(4) In each period presented, curtailments were due to elimination of benefits or workforce reductions (see Note D).

(5) Amounts attributed to joint venture partners are not included.

Amounts Expected to be Recognized in Net Periodic Benefit Cost

	Pension benefits	Other postretirement benefits
	2013	2013
Net actuarial loss recognition	$ 494	$ 36
Prior service cost (benefit) recognition	19	(18)

Assumptions

Weighted average assumptions used to determine benefit obligations for U.S. pension and other postretirement benefit plans were as follows (assumptions for non-U.S plans did not differ materially):

December 31,	2012	2011
Discount rate	4.15%	4.90%
Rate of compensation increase	3.5	3.5

The discount rate is determined using a Company-specific yield curve model (above-median) developed with the assistance of an external actuary. The cash flows of the plans projected benefit obligations are discounted using a single equivalent rate derived from yields on high quality corporate bonds, which represent a broad diversification of issuers in various sectors, including finance and banking, manufacturing, transportation, insurance, and pharmaceutical, among others. The yield curve model parallels the plans projected cash flows, which have an average duration of 10 years, and the underlying cash flows of the bonds included in the model exceed the cash flows needed to satisfy the Company s plans obligations multiple times.

The rate of compensation increase is based upon actual experience. For 2013, the rate of compensation increase will be 3.5%, which approximates the five-year average.

Weighted average assumptions used to determine net periodic benefit cost for U.S. pension and other postretirement benefit plans were as follows (assumptions for non-U.S plans did not differ materially):

	2012	2011	2010
Discount rate*	4.90%	5.75%	6.15%
Expected long-term rate of return on plan assets	8.50	8.50	8.75
Rate of compensation increase	3.50	3.50	3.50

* In all periods presented, the respective discount rates were used to determine net periodic benefit cost for most U.S. pension plans for the full annual period. However, the discount rates for a limited number of plans were updated during 2011 and 2010 to reflect the remeasurement of these plans due to new union labor agreements, settlements, and (or) curtailments. The updated discount rates used were not significantly different from the discount rates presented.

The expected long-term rate of return on plan assets is generally applied to a five-year market-related value of plan assets (a four-year average or the fair value at the plan measurement date is used for certain non-U.S. plans). The process used by management to develop this assumption has expanded from one that relied primarily on historical asset return information to one that also incorporates forward-looking returns by asset class, as described below.

Prior to developing the expected long-term rate of return for calendar year 2009, management focused on historical actual returns (annual, 10-year moving, and 20-year moving averages) when developing this assumption. Based on that process, management utilized 9% for the expected long-term rate of return for several years through 2008. For calendar year 2009, the expected long-term rate of return was reduced to 8.75% due to lower future expected market returns as a result of the then global economic downturn. This was supported by the fact that, in 2008, the 10-year moving average of actual performance fell below 9% for the first time in 20 years, although the 20-year moving average continued to exceed 9%.

For calendar year 2010, management expanded its process by incorporating expected future returns on current and planned asset allocations using information from various external investment managers and management s own judgment. Management considered this forward-looking analysis as well as the historical return information, and concluded the expected rate of return for calendar 2010 would remain at 8.75%, which was between the 20-year moving average actual return performance and the estimated future return developed by asset class.

For calendar year 2012 and 2011, management again incorporated both actual historical return information and expected future returns into its analysis. Based on strategic asset allocation changes and estimates of future returns by asset class, management used 8.50% as its expected long-term rate of return for both years. This rate again falls within the range of the 20-year moving average of actual performance and the expected future return developed by asset class.

For calendar year 2013, management used the same methodology as it did for 2012 and 2011 and determined that 8.50% will be the expected long-term rate of return.

Assumed health care cost trend rates for U.S. other postretirement benefit plans were as follows (assumptions for non-U.S plans did not differ materially):

	2012	2011	2010
Health care cost trend rate assumed for next year	6.0%	6.5%	6.5%
Rate to which the cost trend rate gradually declines	4.5%	5.0%	5.0%
Year that the rate reaches the rate at which it is assumed to remain	2017	2016	2015

The assumed health care cost trend rate is used to measure the expected cost of gross eligible charges covered by Alcoa s other postretirement benefit plans. For 2013, a 6.0% trend rate will be used, reflecting management s best estimate of the change in future health care costs covered by the plans. The plans actual annual health care cost trend experience over the past three years has ranged from (6.2)% to 3.8%. Management does not believe this three-year range is indicative of expected increases for future health care costs over the long-term.

Assumed health care cost trend rates have an effect on the amounts reported for the health care plan. A one-percentage point change in these assumed rates would have the following effects:

	1% increase	1% decrease
Effect on other postretirement benefit obligations	$ 124	$ (114)
Effect on total of service and interest cost components	5	(5)

Plan Assets

Alcoa s pension and other postretirement plans investment policy and weighted average asset allocations at December 31, 2012 and 2011, by asset class, were as follows:

Asset class	Policy range	Plan assets at December 31, 2012	2011
Equities	20 55%	33%	34%
Fixed income	25 55%	50	50
Other investments	15 35%	17	16
Total		100%	100%

The principal objectives underlying the investment of the pension and other postretirement plans assets are to ensure that Alcoa can properly fund benefit obligations as they become due under a broad range of potential economic and financial scenarios, maximize the long-term investment return with an acceptable level of risk based on such obligations, and broadly diversify investments across and within the capital markets to protect asset values against adverse movements. Specific objectives for long-term investment strategy include reducing the volatility of pension

assets relative to pension liabilities and achieving risk factor diversification across the balance of the asset portfolio. A portion of the assets are matched to the interest rate profile of the benefit obligation through long duration fixed income investments and exposure to broad equity risk has been decreased and diversified through investments in macro hedge funds, equity long and short hedge funds, global and emerging market equities, and gold. Investments are further diversified by strategy, asset class, geography, and sector to enhance returns and mitigate downside risk. A large number of external investment managers are used to gain broad exposure to the financial markets and to mitigate manager-concentration risk.

Investment practices comply with the requirements of the Employee Retirement Income Security Act of 1974 (ERISA) and any other applicable laws and regulations. The use of derivative instruments is permitted where appropriate and necessary for achieving overall investment policy objectives. Currently, the use of derivative instruments is not significant when compared to the overall investment portfolio.

In the course of managing the pension and other postretirement plans assets, trustees of the plans loan securities to brokers/dealers in exchange for a fee. The securities are subsequently returned to the plans in accordance with the brokerage agreement. In support of these transactions, the brokers/dealers provide collateral, which exceeds the value of the securities loaned (102%-105%).

The following section describes the valuation methodologies used by the trustees to measure the fair value of pension and other postretirement benefit plan assets, including an indication of the level in the fair value hierarchy in which each type of asset is generally classified (see Note X for the definition of fair value and a description of the fair value hierarchy).

Equities. These securities consist of direct investments in the stock of publicly traded U.S. and non-U.S. companies and are valued based on the closing price reported in an active market on which the individual securities are traded. As such, the direct investments are generally classified in Level 1. Also, these securities consist of the plans share of commingled funds that are invested in the stock of publicly traded companies and are valued at the net asset value of shares held at December 31. As such, these securities are included in Level 1 if quoted in an active market, otherwise these investments are included in Level 2. Additionally, these securities include direct investments in short and long equity hedge funds and private equity (limited partnerships and venture capital partnerships) and are valued by investment managers based on the most recent financial information available, which typically represents significant unobservable data. As such, these investments are generally classified as Level 3.

Fixed income. These securities consist of U.S. government debt and are generally valued using quoted prices. As such, these securities are included in Level 1. Also, these securities include publicly traded U.S. and non-U.S. fixed interest obligations (principally corporate bonds and debentures) and are valued through consultation and evaluation with brokers in the institutional market using quoted prices and other observable market data. As such, these investments are included in Level 2. Additionally, these securities include cash and cash equivalents, which consist of government securities in commingled funds, and are generally valued using observable market data. As such, these funds are included in Level 2. Furthermore, these securities consist of commercial and residential mortgage-backed securities and are valued by investment managers based on the most recent financial information available, which typically represents significant unobservable data. As such, these investments are generally classified as Level 3.

Other investments. These investments include, among others, exchange traded funds, macro hedge funds, real estate investment trusts, and direct investments of private real estate. Exchange traded funds, such as gold, and real estate investment trusts are valued based on the closing price reported in an active market on which the investments are traded, and, therefore, are included in Level 1. Also, these securities consist of the plans share of commingled funds that are invested in real estate investment trusts and are valued at the net asset value of shares held at December 31. As such, these securities are generally included in Level 2. Direct investments of macro hedge funds and private real estate (includes limited partnerships) are valued by investment managers based on the most recent financial information available, which typically represents significant unobservable data. As such, these investments are generally classified as Level 3. If fair value is able to be determined through the use of quoted market prices of similar assets or other observable market data, then the investments are classified in Level 2.

The fair value methods described above may not be indicative of net realizable value or reflective of future fair values. Additionally, while Alcoa believes the valuation methods used by the plans trustees are appropriate and consistent

with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

The following table presents the fair value of pension and other postretirement plans assets classified under the appropriate level of the fair value hierarchy:

December 31, 2012	Level 1	Level 2	Level 3	Total
Equities:				
Equity securities	$ 1,016	$ 1,196	$ 117	$ 2,329
Short and long equity hedge funds	-	-	756	756
Private equity	-	-	550	550
	$ 1,016	$ 1,196	$ 1,423	$ 3,635
Fixed income:				
Intermediate and long duration government/credit	$ 1,169	$ 3,689	$ 215	$ 5,073
Other	-	507	-	507
	$ 1,169	$ 4,196	$ 215	$ 5,580
Other investments:				
Real estate	$ 113	$ 83	$ 377	$ 573
Macro hedge funds	-	-	796	796
Other	212	-	247	459
	$ 325	$ 83	$ 1,420	$ 1,828
Total	$ 2,510	$ 5,475	$ 3,058	$ 11,043

December 31, 2011	Level 1	Level 2	Level 3	Total
Equities				
Equity securities*	$ 904	$ 1,203	$ 110	$ 2,217
Short and long equity hedge funds	-	-	731	731
Private equity	-	-	542	542
	$ 904	$ 1,203	$ 1,383	$ 3,490
Fixed income:				
Intermediate and long duration government/credit	$ 1,223	$ 3,540	$ 211	$ 4,974
Other	-	340	-	340
	$ 1,223	$ 3,880	$ 211	$ 5,314
Other investments:				
Real estate	$ 97	$ 74	$ 375	$ 546
Macro hedge funds	-	-	668	668
Other	198	-	123	321
	$ 295	$ 74	$ 1,166	$ 1,535
Total**	$ 2,422	$ 5,157	$ 2,760	$ 10,339

* At December 31, 2011, Level 1 equity securities include $36 of Alcoa common stock related to the January 2011 plan contribution (see Funding and Cash Flows section below).

** As of December 31, 2011, the total fair value of pension and other postretirement plans assets excludes a net payable of $20, which represents securities purchased not yet settled less interest and dividends earned on various investments.

Pension and other postretirement benefit plans assets classified as Level 3 in the fair value hierarchy represent investments in which the trustees have used significant unobservable inputs in the valuation model. The following table presents a reconciliation of activity for such investments:

	2012	2011
Balance at beginning of year	$ 2,760	$ 1,499
Realized gains	52	67
Unrealized gains	142	100
Purchases	634	1,221
Sales	(538)	(124)
Issuances	-	-
Settlements	-	-
Foreign currency translation impact	8	(3)
Transfers in and (or) out of Level 3*	-	-
Balance at end of year	$ 3,058	$ 2,760

* In 2012 and 2011, there were no transfers of financial instruments into or out of Level 3

Funding and Cash Flows

It is Alcoa s policy to fund amounts for pension plans sufficient to meet the minimum requirements set forth in applicable country benefits laws and tax laws, including the Pension Protection Act of 2006, the Worker, Retiree, and Employer Recovery Act of 2008, and the Moving Ahead for Progress in the 21st Century Act for U.S. plans. From time to time, Alcoa contributes additional amounts as deemed appropriate. In 2012 and 2011, cash contributions to Alcoa s pension plans were $561 and $336. Also in 2011, Alcoa contributed newly issued shares (see Note R) of its common stock (valued at $600) to a master trust that holds the assets of certain U.S. defined benefit pension plans in a private placement transaction. These shares were issued to satisfy the estimated minimum required funding and to provide additional funding towards maintaining an approximately 80% funded status of Alcoa s U.S. pension plans. The minimum required contribution to pension plans in 2013 is estimated to be $460, of which $140 is for non-U.S. plans.

Benefit payments expected to be paid to pension and other postretirement benefit plans participants and expected Medicare Part D subsidy receipts are as follows:

Year ended December 31,	Pension benefits	Gross Other post-retirement benefits	Medicare Part D subsidy receipts	Net Other post-retirement benefits
2013	$ 880	$ 285	$ 30	$ 255
2014	870	280	30	250
2015	880	280	30	250
2016	890	275	30	245
2017	910	270	35	235
2018 through 2022	4,620	1,200	170	1,030
	$ 9,050	$ 2,590	$ 325	$ 2,265

Defined Contribution Plans

Alcoa sponsors savings and investment plans in several countries, including the U.S. and Australia. Expenses related to these plans were $146 in 2012, $139 in 2011, and $119 in 2010. In the U.S., employees may contribute a portion of their compensation to the plans, and Alcoa matches, mostly in company stock, a portion of these contributions.

X. Derivatives and Other Financial Instruments

Derivatives. Alcoa is exposed to certain risks relating to its ongoing business operations, including financial, market, political, and economic risks. The following discussion provides information regarding Alcoa s exposure to the risks of changing commodity prices, interest rates, and foreign currency exchange rates.

Alcoa s commodity and derivative activities are subject to the management, direction, and control of the Strategic Risk Management Committee (SRMC), which is composed of the chief executive officer, the chief financial officer, and other officers and employees that the chief executive officer selects. The SRMC meets on a periodic basis to review derivative positions and strategy and reports to Alcoa s Board of Directors on the scope of its activities.

The aluminum, energy, interest rate, and foreign exchange contracts are held for purposes other than trading. They are used primarily to mitigate uncertainty and volatility, and to cover underlying exposures. Alcoa is not involved in trading activities for energy, weather derivatives, or other nonexchange commodity trading activities.

The fair values and corresponding classifications under the appropriate level of the fair value hierarchy of outstanding derivative contracts recorded as assets in the accompanying Consolidated Balance Sheet were as follows:

		December 31,	December 31,
Asset Derivatives	**Level**	**2012**	**2011**
Derivatives designated as hedging instruments:			
Prepaid expenses and other current assets:			
Aluminum contracts	1	$ 23	$ 51
Aluminum contracts	3	7	5
Interest rate contracts	2	8	8
Other noncurrent assets:			
Aluminum contracts	1	3	6
Energy contracts	3	3	2
Interest rate contracts	2	37	37
Total derivatives designated as hedging instruments		$ 81	$ 109
Derivatives not designated as hedging instruments*:			
Prepaid expenses and other current assets:			
Aluminum contracts	2	$ -	$ 1
Aluminum contracts	3	211	-
Other noncurrent assets:			
Aluminum contracts	3	329	5
Foreign exchange contracts	1	1	1
Total derivatives not designated as hedging instruments		$ 541	$ 7
Less margin held**:			
Prepaid expenses and other current assets:			
Aluminum contracts	1	$ 9	$ 7
Interest rate contracts	2	8	8
Other noncurrent assets:			
Interest rate contracts	2	9	7
Sub-total		$ 26	$ 22
Total Asset Derivatives		$ 596	$ 94

* See the Other section within Note X for additional information on Alcoa s purpose for entering into derivatives not designated as hedging instruments and its overall risk management strategies.

** All margin held is in the form of cash and is valued under a Level 1 technique. The levels that correspond to the margin held in the table above reference the level of the corresponding asset for which it is held. Alcoa elected to net the margin held against the fair value amounts recognized for derivative instruments executed with the same counterparties under master netting arrangements.

147

The fair values and corresponding classifications under the appropriate level of the fair value hierarchy of outstanding derivative contracts recorded as liabilities in the accompanying Consolidated Balance Sheet were as follows:

Liability Derivatives	Level	December 31, 2012	December 31, 2011
Derivatives designated as hedging instruments:			
Other current liabilities:			
Aluminum contracts	1	$ 13	$ 47
Aluminum contracts	3	35	32
Other noncurrent liabilities and deferred credits:			
Aluminum contracts	1	1	4
Aluminum contracts	3	573	570
Total derivatives designated as hedging instruments		$ 622	$ 653
Derivatives not designated as hedging instruments*:			
Other current liabilities:			
Aluminum contracts	1	$ 1	$ 12
Aluminum contracts	2	21	23
Embedded credit derivative	3	3	-
Other noncurrent liabilities and deferred credits:			
Aluminum contracts	1	-	1
Aluminum contracts	2	5	21
Embedded credit derivative	3	27	28
Total derivatives not designated as hedging instruments		$ 57	$ 85
Less margin posted**:			
Other current liabilities:			
Aluminum contracts	1	$ -	$ 1
Total Liability Derivatives		$ 679	$ 737

* See the Other section within Note X for additional information on Alcoa s purpose for entering into derivatives not designated as hedging instruments and its overall risk management strategies.

** All margin posted is in the form of cash and is valued under a Level 1 technique. The levels that correspond to the margin posted in the table above reference the level of the corresponding liability for which it is posted. Alcoa elected to net the margin posted against the fair value amounts recognized for derivative instruments executed with the same counterparties under master netting arrangements.

The following table shows the net fair values of outstanding derivative contracts at December 31, 2012 and the effect on these amounts of a hypothetical change (increase or decrease of 10%) in the market prices or rates that existed at December 31, 2012:

	Fair value asset/(liability)	Index change of + / - 10%
Aluminum contracts	$ (85)	$ 111
Embedded credit derivative	(30)	3
Energy contracts	3	249
Foreign exchange contracts	1	8
Interest rate contracts	28	1

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value hierarchy distinguishes between (1) market participant assumptions developed based on market data obtained from independent sources (observable inputs) and (2) an entity s own assumptions about market participant assumptions developed based on the best

information available in the circumstances (unobservable inputs). The fair value hierarchy consists of three broad levels, which gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy are described below:

Level 1 Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

Level 2 Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly, including quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; inputs other than quoted prices that are observable for the asset or liability (e.g., interest rates); and inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3 Inputs that are both significant to the fair value measurement and unobservable.

The following section describes the valuation methodologies used by Alcoa to measure derivative contracts at fair value, including an indication of the level in the fair value hierarchy in which each instrument is generally classified. Where appropriate, the description includes details of the valuation models, the key inputs to those models, and any significant assumptions. These valuation models are reviewed and tested at least on an annual basis.

Derivative contracts are valued using quoted market prices and significant other observable and unobservable inputs. Such financial instruments consist of aluminum, energy, interest rate, and foreign exchange contracts. The fair values for the majority of these derivative contracts are based upon current quoted market prices. These financial instruments are typically exchange-traded and are generally classified within Level 1 or Level 2 of the fair value hierarchy depending on whether the exchange is deemed to be an active market or not.

For certain derivative contracts whose fair values are based upon trades in liquid markets, such as interest rate swaps, valuation model inputs can generally be verified through over-the-counter markets and valuation techniques do not involve significant management judgment. The fair values of such financial instruments are generally classified within Level 2 of the fair value hierarchy.

Alcoa has other derivative contracts that do not have observable market quotes. For these financial instruments, management uses significant other observable inputs (e.g., information concerning time premiums and volatilities for certain option type embedded derivatives and regional premiums for aluminum contracts). For periods beyond the term of quoted market prices for aluminum, Alcoa uses a model that estimates the long-term price of aluminum by extrapolating the 10-year London Metal Exchange (LME) forward curve. For periods beyond the term of quoted market prices for energy, management has developed a forward curve based on independent consultant market research. Where appropriate, valuations are adjusted for various factors such as liquidity, bid/offer spreads, and credit considerations. Such adjustments are generally based on available market evidence (Level 2). In the absence of such evidence, management s best estimate is used (Level 3). If a significant input that is unobservable in one period becomes observable in a subsequent period, the related asset or liability would be transferred to the appropriate level classification (1 or 2) in the period of such change.

The following table presents Alcoa s derivative contract assets and liabilities that are measured and recognized at fair value on a recurring basis classified under the appropriate level of the fair value hierarchy (there were no transfers in or out of Levels 1 and 2 during the periods presented):

December 31,	2012	2011
Assets:		
Level 1	$ 27	$ 57
Level 2	45	47
Level 3	550	12
Margin held	(26)	(22)
Total	$ 596	$ 94
Liabilities:		
Level 1	$ 15	$ 64
Level 2	26	44
Level 3	638	630
Margin posted	-	(1)
Total	$ 679	$ 737

Financial instruments classified as Level 3 in the fair value hierarchy represent derivative contracts in which management has used at least one significant unobservable input in the valuation model. The following tables present a reconciliation of activity for such derivative contracts:

	Assets		Liabilities		
2012	Aluminum contracts	Energy contracts	Aluminum contracts	Embedded credit derivative	Energy contracts
Opening balance January 1, 2012	$ 10	$ 2	$ 602	$ 28	$ -
Total gains or losses (realized and unrealized) included in:					
Sales	(8)	-	(33)	-	-
Cost of goods sold	(107)	-	-	(1)	-
Other income, net	16	-	-	3	-
Other comprehensive loss	10	1	39	-	-
Purchases, sales, issuances, and settlements*	596	-	-	-	-
Transfers into and (or) out of Level 3*	-	-	-	-	-
Foreign currency translation	30	-	-	-	-
Closing balance December 31, 2012	$ 547	$ 3	$ 608	$ 30	$ -
Change in unrealized gains or losses included in earnings for derivative contracts held at December 31, 2012:					
Sales	$ -	$ -	$ -	$ -	$ -
Cost of goods sold	-	-	-	-	-
Other income, net	16	-	-	3	-

* In July 2012, two embedded derivatives contained within existing power contracts became subject to derivative accounting under GAAP (see below). The amount reflected in this table represents the initial fair value of these embedded derivatives and was classified as an issuance of Level 3 financial instruments. There were no purchases, sales or settlements of Level 3 financial instruments. Additionally, there were no transfers of financial instruments into or out of Level 3.

	Assets		Liabilities		
2011	**Aluminum contracts**	**Energy contracts**	**Aluminum contracts**	**Embedded credit derivative**	**Energy contracts**
Opening balance January 1, 2011	$ -	$ 9	$ 702	$ 24	$ 62
Total gains or losses (realized and unrealized) included in:					
Sales	-	-	(63)	-	-
Cost of goods sold	-	-	-	(1)	(14)
Other income, net	-	-	-	5	(48)
Other comprehensive loss	5	(7)	(37)	-	-
Purchases, sales, issuances, and settlements**	5	-	-	-	-
Transfers into and (or) out of Level 3**	-	-	-	-	-
Foreign currency translation	-	-	-	-	-
Closing balance December 31, 2011	$ 10	$ 2	$ 602	$ 28	$ -
Change in unrealized gains or losses included in earnings for derivative contracts held at December 31, 2011:					
Sales	$ -	$ -	$ -	$ -	$ -
Cost of goods sold	-	-	-	-	-
Other income, net	-	-	-	5	-

** In 2011, there was an issuance of a Level 3 financial instrument related to a natural gas supply contract (see below). There were no purchases, sales, or settlements of Level 3 financial instruments. Additionally, there were no transfers of financial instruments into or out of Level 3.

As reflected in the table above, the net unrealized loss on derivative contracts using Level 3 valuation techniques was $88 and $618 as of December 31, 2012 and 2011, respectively. These losses were mainly attributed to embedded derivatives in power contracts that index the price of power to the LME price of aluminum. These embedded derivatives are primarily valued using observable market prices; however, due to the length of the contracts, the valuation model also requires management to estimate the long-term price of aluminum based upon an extrapolation of the 10-year LME forward curve. Significant increases or decreases in the actual LME price beyond 10 years would result in a higher or lower fair value measurement. An increase of actual LME price over the inputs used in the valuation model will result in a higher cost of power and a corresponding increase to the liability. The embedded derivatives have been designated as hedges of forward sales of aluminum and related realized gains and losses were included in Sales on the accompanying Statement of Consolidated Operations.

In July 2012, as provided for in the arrangements, management elected to modify the pricing for two existing power contracts, which end in 2014 and 2016 (see directly below), for Alcoa s two smelters in Australia and the Point Henry rolling mill in Australia. These contracts contain an LME-linked embedded derivative, which previously was not recorded as an asset in Alcoa s Consolidated Balance Sheet. Beginning on January 1, 2001, all derivative contracts were required to be measured and recorded at fair value on an entity s balance sheet under GAAP; however, an exception existed for embedded derivatives upon meeting certain criteria. The LME-linked embedded derivative in these two contracts met such criteria at that time. Management s election to modify the pricing of these contracts qualifies as a significant change to the contracts thereby requiring that the contracts now be evaluated under derivative accounting as if they were new contracts. As a result, Alcoa recorded a derivative asset in the amount of $596 (reflects the finalization of the valuation model) with an offsetting liability (deferred credit) recorded in Other current and non-current liabilities. Unrealized gains and losses from the embedded derivative were included in Other (income) expenses, net on the accompanying Statement of Consolidated Operations, while realized gains and losses were included in Cost of goods sold on the accompanying Statement of Consolidated Operations as electricity purchases are made under the contracts. The deferred credit is recognized in Other (income) expenses, net on the accompanying Statement of Consolidated Operations as power is received over the life of the contracts. The embedded derivative is

valued using the probability and interrelationship of future LME prices, Australian dollar to U.S. dollar exchange rates, and the U.S. consumer price index. Significant increases or decreases in the LME price would result in a higher or lower fair value measurement. An increase in actual LME price over the inputs used in the valuation model will result in a higher cost of power and a decrease to the embedded derivative asset.

In 2010, Alcoa entered into derivative contracts that will hedge the anticipated power requirements at Alcoa s two smelters in Australia once the existing contracts expire in 2014 and 2016. These derivatives hedge forecasted power purchases through December 2036. Beyond the term where market information is available, management has developed a forward curve, for valuation purposes, based on independent consultant market research. The effective portion of gains and losses on these contracts were recorded in Other comprehensive (loss) income on the accompanying Consolidated Balance Sheet until the designated hedge periods begin in 2014 and 2016. Once the hedge periods begin, realized gains and losses will be recorded in Cost of goods sold. Significant increases or decreases in the power market may result in a higher or lower fair value measurement. Higher prices in the power market would cause the derivative asset to increase in value.

Also, Alcoa has a six-year natural gas supply contract, which has an LME-linked ceiling. This contract is valued using probabilities of future LME aluminum prices and the price of Brent crude oil (priced on Platts), including the interrelationships between the two commodities subject to the ceiling. Any change in the interrelationship would result in a higher or lower fair value measurement. An LME ceiling was embedded into the contract price to protect against an increase in the price of oil without a corresponding increase in the price of LME. An increase in oil prices with no similar increase in the LME price would limit the increase of the price paid for natural gas. At inception, this contract had a fair value of $5. Unrealized gains and losses from this contract were included in Other (income) expenses, net on the accompanying Statement of Consolidated Operations, while realized gains and losses will be included in Cost of goods sold on the accompanying Statement of Consolidated Operations as gas purchases are made under the contract.

Additionally, an embedded derivative in a power contract that indexes the difference between the long-term debt ratings of Alcoa and the counterparty from any of the three major credit rating agencies is included in Level 3. Management uses market prices, historical relationships, and forecast services to determine fair value. Significant increases or decreases in any of these inputs would result in a lower or higher fair value measurement. A wider credit spread between Alcoa and the counterparty would result in an increase of the future liability and a higher cost of power. Realized gains and losses for this embedded derivative were included in Cost of goods sold on the accompanying Statement of Consolidated Operations and unrealized gains and losses were included in Other (income) expenses, net on the accompanying Statement of Consolidated Operations.

Furthermore, included within Level 3 measurements are derivative financial instruments that hedge the cost of electricity. Transactions involving on-peak power are observable as there is an active market. However, there are certain off-peak times when there is not an actively traded market for electricity. Therefore, management utilizes market prices, historical relationships, and various forecast services to determine the fair value. Management utilized these same valuation techniques for an existing power contract associated with a smelter in the U.S. that no longer qualified for the normal purchase normal sale exception under derivative accounting in late 2009. Unrealized gains and losses for this physical power contract were included in Other (income) expenses, net on the accompanying Statement of Consolidated Operations, while realized gains and losses were included in Cost of goods sold on the accompanying Statement of Consolidated Operations. Additionally, a financial contract related to the same U.S. smelter utilized by management to hedge the price of electricity of the aforementioned power contract no longer qualified for cash flow hedge accounting near the end of 2009. Realized gains and losses of this financial contract were included in Cost of goods sold on the accompanying Statement of Consolidated Operations. In periods prior to January 1, 2010, unrealized gains and losses were included in Other comprehensive (loss) income; in periods subsequent to December 31, 2009, such changes were included in Other (income) expenses, net on the accompanying Statement of Consolidated Operations. Both the physical power contract and the financial contract related to this U.S. smelter expired in September 2011.

The following table presents quantitative information for Level 3 derivative contracts:

	Fair value at December 31, 2012*	Valuation technique	Unobservable input	Range ($ in full amounts)
Assets:				
Aluminum contract	$ 2	Discounted cash flow	Interrelationship of future aluminum and oil prices	Aluminum: $2,037 per metric ton in 2013 to $2,542 per metric ton in 2018 Oil: $90 to $111 per barrel
Aluminum contract	537	Discounted cash flow	Interrelationship of future aluminum prices, foreign currency exchange rates, and the U.S. consumer price index (CPI)	Aluminum: $2,046 per metric ton in 2013 to $2,400 per metric ton in 2016 Foreign currency: A$1 = $1.03 in 2013 to $0.94 in 2016 CPI: 1982 base year of 100 and 232 in 2013 to 254 in 2016
Energy contracts	3	Discounted cash flow	Price of electricity beyond forward curve	$78 per megawatt hour in 2013 to $170 per megawatt hour in 2036
Liabilities:				
Aluminum contracts	600	Discounted cash flow	Price of aluminum beyond forward curve	$2,790 per metric ton in 2023 to $3,002 per metric ton in 2027
Embedded credit derivative	30	Discounted cash flow	Credit spread between Alcoa and counterparty	1.63% to 1.91% (1.77% median)

* The fair value of aluminum contracts reflected as assets and liabilities in this table are both lower by $8 compared to the respective amounts reflected in the Level 3 reconciliation presented above. This is due to the fact that Alcoa has a contract that is in an asset position for the current portion but is in a liability position for the long-term portion, and is reflected as such on the accompanying Consolidated Balance Sheet. However, this contract is reflected as a net liability in this table for purposes of presenting the fair value technique and assumptions utilized to measure the contract as a whole.

Fair Value Hedges

For derivative instruments that are designated and qualify as fair value hedges, the gain or loss on the derivative as well as the loss or gain on the hedged item attributable to the hedged risk are recognized in current earnings. The gain or loss on the hedged items are included in the same line items as the loss or gain on the related derivative contracts as follows (there were no contracts that ceased to qualify as a fair value hedge in any of the periods presented):

		Amount of Gain or (Loss)		
Derivatives in Fair Value Hedging Relationships	**Location of Gain or (Loss) Recognized in Earnings on Derivatives**	**Recognized in Earnings on Derivatives**		
		2012	**2011**	**2010**
Aluminum contracts*	Sales	$ (9)	$ (126)	$ 38
Interest rate contracts	Interest expense	10	64	90
Total		$ 1	$ (62)	$ 128

		Amount of Gain or (Loss)		
Hedged Items in Fair Value Hedging Relationships	**Location of Gain or (Loss) Recognized in Earnings on Hedged Items**	**Recognized in Earnings on Hedged Items**		
		2012	**2011**	**2010**
Aluminum contracts	Sales	$ (9)	$ 133	$ (41)
Interest rate contracts	Interest expense	(10)	(31)	(62)
Total		$ (19)	$ 102	$ (103)

* In 2012, 2011, and 2010, the amount of gain or (loss) recognized in earnings represents $(18), $7, and $(3), respectively, related to the ineffective portion of the hedging relationships.

Aluminum. Alcoa is a leading global producer of primary aluminum and fabricated aluminum products. As a condition of sale, customers often require Alcoa to enter into long-term, fixed-price commitments. These commitments expose Alcoa to the risk of fluctuating aluminum prices between the time the order is committed and the time that the order is shipped. Alcoa s aluminum commodity risk management policy is to manage, principally through the use of futures and contracts, the aluminum price risk associated with a portion of its firm commitments. These contracts cover known exposures, generally within three years. As of December 31, 2012, Alcoa had 386 kmt of aluminum futures designated as fair value hedges. The effects of this hedging activity will be recognized over the designated hedge periods in 2013 to 2016.

Interest Rates. Alcoa uses interest rate swaps to help maintain a strategic balance between fixed- and floating-rate debt and to manage overall financing costs. As of December 31, 2012, the Company had pay floating, receive fixed interest rate swaps that were designated as fair value hedges. These hedges effectively convert the interest rate from fixed to floating on $200 of debt through 2018. In January 2012, interest rate swaps with a notional amount of $315 expired in conjunction with the repayment of 6% Notes, due 2012 (see Note K).

In 2011, Alcoa terminated interest rate swaps with a notional amount of $550 in conjunction with the early retirement of the related debt (see Note K). At the time of termination, the swaps were in-the-money resulting in a gain of $33, which was recorded in Interest expense on the accompanying Statement of Consolidated Operations. In 2010, Alcoa terminated all or a portion of various interest rate swaps with a notional amount of $825 in conjunction with the early retirement of the related debt. At the time of termination, the swaps were in-the-money resulting in a gain of $28, which was recorded in Interest expense on the accompanying Statement of Consolidated Operations.

Cash Flow Hedges

For derivative instruments that are designated and qualify as cash flow hedges, the effective portion of the gain or loss on the derivative is reported as a component of other comprehensive income (OCI) and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings.

Derivatives in Cash Flow Hedging Relationships	Amount of Gain or (Loss) Recognized in OCI on Derivatives (Effective Portion)			Location of Gain or (Loss) Reclassified from Accumulated OCI into Earnings (Effective Portion)	Amount of Gain or (Loss) Reclassified from Accumulated OCI into Earnings (Effective Portion)*			Location of Gain or (Loss) Recognized in Earnings on Derivatives (Ineffective Portion and Amount Excluded from Effectiveness Testing)	Amount of Gain or (Loss) Recognized in Earnings on Derivatives (Ineffective Portion and Amount Excluded from Effectiveness Testing)**		
	2012	2011	2010		2012	2011	2010		2012	2011	2010
Aluminum contracts	$ (10)	$ 72	$ (6)	Sales	$ 36	$ (114)	$ (106)	Other (income) expenses, net	$ (1)	$ 2	$ -
Energy contracts	-	(3)	(10)	Cost of goods sold	-	(8)	(25)	Other (income) expenses, net	-	-	-
Foreign exchange contracts	-	1	(3)	Sales	-	4	(6)	Other (income) expenses, net	-	-	-
Interest rate contracts	-	(2)	(1)	Interest expense	(2)	-	(1)	Other (income) expenses, net	-	-	-
Interest rate contracts	(2)	(5)	(1)	Other (income) expenses, net	-	(3)	-	Other (income) expenses, net	-	-	-
Total	$ (12)	$ 63	$ (21)		$ 34	$ (121)	$ (138)		$ (1)	$ 2	$ -

* Assuming market rates remain constant with the rates at December 31, 2012, a loss of $23 is expected to be recognized in earnings over the next 12 months.

** In 2012 and 2011, the amount of gain or (loss) recognized in earnings represents $(1) and $3, respectively, related to the amount excluded from the assessment of hedge effectiveness. There was also $(1) and less than $1 recognized in earnings related to the ineffective portion of the hedging relationships in 2011 and 2010, respectively.

Aluminum and Energy. Alcoa anticipates the continued requirement to purchase aluminum and other commodities, such as electricity and natural gas, for its operations. Alcoa enters into forwards, futures, and options contracts to reduce volatility in the price of these commodities. Alcoa has also entered into power supply and other contracts that contain pricing provisions related to the LME aluminum price. The LME-linked pricing features are considered embedded derivatives. A majority of these embedded derivatives have been designated as cash flow hedges of future sales of aluminum.

In 2010, Alcoa entered into contracts to hedge the anticipated power requirements at two smelters in Australia. These derivatives hedge forecasted power purchases through December 2036.

Interest Rates. Alcoa had no outstanding cash flow hedges of interest rate exposures as of December 31, 2012, 2011 or 2010. An investment accounted for on the equity method by Alcoa has entered into interest rate contracts, which are designated as cash flow hedges. Alcoa s share of the activity of these cash flow hedges is reflected in the table above.

Foreign Exchange. Alcoa is subject to exposure from fluctuations in foreign currency exchange rates. Contracts may be used from time to time to hedge the variability in cash flows from the forecasted payment or receipt of currencies other than the functional currency. These contracts cover periods consistent with known or expected exposures through 2013.

Alcoa had the following outstanding forward contracts that were entered into to hedge forecasted transactions:

December 31,	2012	2011
Aluminum contracts (kmt)	1,120	1,294
Energy contracts:		
Electricity (megawatt hours)	100,578,295	100,578,295
Natural gas (million British thermal units)	19,160,000	-
Foreign exchange contracts	$ 71	$ -

Other

Alcoa has certain derivative contracts that do not qualify for hedge accounting treatment and, therefore, the fair value gains and losses on these contracts are recorded in earnings as follows:

		Amount of Gain or (Loss) Recognized in Earnings on Derivatives		
Derivatives Not Designated as Hedging Instruments	**Location of Gain or (Loss) Recognized in Earnings on Derivatives**	**2012**	**2011**	**2010**
Aluminum contracts	Sales	$ -	$ (13)	$ 5
Aluminum contracts	Other (income) expenses, net	16	13	(18)
Embedded credit derivative	Other (income) expenses, net	(3)	(5)	(2)
Energy contract	Other (income) expenses, net	-	47	(23)
Foreign exchange contracts	Other (income) expenses, net	-	(3)	6
Total		$ 13	$ 39	$ (32)

The aluminum contracts relate to derivatives (recognized in Sales) and embedded derivatives (recognized in Other (income) expenses, net) entered into to minimize Alcoa s price risk related to other customer sales and certain pricing arrangements.

The embedded credit derivative relates to a power contract that indexes the difference between the long-term debt ratings of Alcoa and the counterparty from any of the three major credit rating agencies. If the counterparty s lowest credit rating is greater than one rating category above Alcoa s credit ratings, an independent investment banker would be consulted to determine a hypothetical interest rate for both parties. The two interest rates would be netted and the resulting difference would be multiplied by Alcoa s equivalent percentage of the outstanding principal of the counterparty s debt obligation as of December 31 of the year preceding the calculation date. This differential would be added to the cost of power in the period following the calculation date.

The energy contract is associated with a smelter in the U.S. for a power contract that no longer qualified for the normal purchase normal sale exception and a financial contract that no longer qualified as a hedge under derivative accounting in late 2009. Alcoa s obligations under the contracts expired in September 2011.

Alcoa has a forward contract to purchase $58 (C$58) to mitigate the foreign currency risk related to a Canadian-denominated loan due in 2014. All other foreign exchange contracts were entered into and settled within each of the periods presented.

Material Limitations

The disclosures with respect to commodity prices, interest rates, and foreign currency exchange risk do not take into account the underlying commitments or anticipated transactions. If the underlying items were included in the analysis, the gains or losses on the futures contracts may be offset. Actual results will be determined by a number of factors that are not under Alcoa s control and could vary significantly from those factors disclosed.

Alcoa is exposed to credit loss in the event of nonperformance by counterparties on the above instruments, as well as credit or performance risk with respect to its hedged customers commitments. Although nonperformance is possible, Alcoa does not anticipate nonperformance by any of these parties. Contracts are with creditworthy counterparties and are further supported by cash, treasury bills, or irrevocable letters of credit issued by carefully chosen banks. In addition, various master netting arrangements are in place with counterparties to facilitate settlement of gains and losses on these contracts.

Other Financial Instruments. The carrying values and fair values of Alcoa s other financial instruments were as follows:

	2012		2011	
December 31,	**Carrying value**	**Fair value**	**Carrying value**	**Fair value**
Cash and cash equivalents	$ 1,861	$ 1,861	$ 1,939	$ 1,939
Restricted cash	189	189	25	25
Noncurrent receivables	20	20	30	30
Available-for-sale securities	67	67	92	92
Short-term borrowings	53	53	62	62
Commercial paper	-	-	224	224
Long-term debt due within one year	465	465	445	445
Long-term debt, less amount due within one year	8,311	9,028	8,640	9,274

The following methods were used to estimate the fair values of other financial instruments:

Cash and cash equivalents, Restricted cash, Short-term borrowings, Commercial paper, and Long-term debt due within one year. The carrying amounts approximate fair value because of the short maturity of the instruments. The fair value amounts for Cash and cash equivalents, Restricted cash, and Commercial paper were classified in Level 1; Short-term borrowings were classified in Level 2; and Long-term debt due within one year was classified in Level 1 of the fair value hierarchy for public debt ($422) and Level 2 of the fair value hierarchy for non-public debt ($43).

Noncurrent receivables. The fair value of noncurrent receivables was based on anticipated cash flows, which approximates carrying value, and was classified in Level 2 of the fair value hierarchy.

Available-for-sale securities. The fair value of such securities was based on quoted market prices. These financial instruments consist of exchange-traded fixed income and equity securities, which are carried at fair value and were classified in Level 1 of the fair value hierarchy.

Long-term debt, less amount due within one year. The fair value was based on quoted market prices for public debt and on interest rates that are currently available to Alcoa for issuance of debt with similar terms and maturities for non-public debt. At December 31, 2012 and 2011, $8,456 and $8,576, respectively, was classified in Level 1 of the fair value hierarchy for public debt and $572 and $698, respectively, was classified in Level 2 of the fair value hierarchy for non-public debt.

Y. Subsequent Events

Management evaluated all activity of Alcoa and concluded that no subsequent events have occurred that would require recognition in the Consolidated Financial Statements or disclosure in the Notes to the Consolidated Financial Statements.

Supplemental Financial Information (unaudited)

Quarterly Data

(in millions, except per-share amounts)

	First	Second	Third	Fourth	Year
2012					
Sales	$ 6,006	$ 5,963	$ 5,833	$ 5,898	$ 23,700
Amounts attributable to Alcoa common shareholders:					
Income (loss) from continuing operations	$ 94	$ (2)	$ (143)	$ 242	$ 191
Loss from discontinued operations	-	-	-	-	-
Net income (loss)	$ 94	$ (2)	$ (143)	$ 242	$ 191
Earnings per share attributable to Alcoa common shareholders*:					
Basic:					
Income (loss) from continuing operations	$ 0.09	$ -	$ (0.13)	$ 0.23	$ 0.18
Loss from discontinued operations	-	-	-	-	-
Net income (loss)	$ 0.09	$ -	$ (0.13)	$ 0.23	$ 0.18
Diluted:					
Income (loss) from continuing operations	$ 0.09	$ -	$ (0.13)	$ 0.21	$ 0.18
Loss from discontinued operations	-	-	-	-	-
Net income (loss)	$ 0.09	$ -	$ (0.13)	$ 0.21	$ 0.18
2011					
Sales	$ 5,958	$ 6,585	$ 6,419	$ 5,989	$ 24,951
Amounts attributable to Alcoa common shareholders:					
Income (loss) from continuing operations	$ 309	$ 326	$ 172	$ (193)	$ 614
(Loss) income from discontinued operations	(1)	(4)	-	2	(3)
Net income (loss)	$ 308	$ 322	$ 172	$ (191)	$ 611
Earnings per share attributable to Alcoa common shareholders*:					
Basic:					
Income (loss) from continuing operations	$ 0.29	$ 0.31	$ 0.16	$ (0.18)	$ 0.58
(Loss) income from discontinued operations	-	(0.01)	-	-	(0.01)
Net income (loss)	$ 0.29	$ 0.30	$ 0.16	$ (0.18)	$ 0.57
Diluted:					
Income (loss) from continuing operations	$ 0.27	$ 0.28	$ 0.15	$ (0.18)	$ 0.55
(Loss) income from discontinued operations	-	-	-	-	-
Net income (loss)	$ 0.27	$ 0.28	$ 0.15	$ (0.18)	$ 0.55

* Per share amounts are calculated independently for each period presented; therefore, the sum of the quarterly per share amounts may not equal the per share amounts for the year.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.

None.

Item 9A. Controls and Procedures.

(a) Evaluation of Disclosure Controls and Procedures

Alcoa s Chief Executive Officer and Chief Financial Officer have evaluated the Company s disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as of the end of the period covered by this report, and they have concluded that these controls and procedures are effective.

(b) Management s Annual Report on Internal Control over Financial Reporting

Management s Report on Internal Control over Financial Reporting is included in Part II, Item 8 of this Form 10-K beginning on page 80.

(c) Attestation Report of the Registered Public Accounting Firm

The effectiveness of Alcoa s internal control over financial reporting as of December 31, 2012 has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report, which is included in Part II, Item 8 of this Form 10-K on page 81.

(d) Changes in Internal Control over Financial Reporting

There have been no changes in internal control over financial reporting during the fourth quarter of 2012, that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

Item 9B. Other Information.

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance.

The information required by Item 401 of Regulation S-K regarding directors is contained under the caption Item 1 Election of Directors of the Proxy Statement and is incorporated by reference. The information required by Item 401 of Regulation S-K regarding executive officers is set forth in Part I, Item 1 of this report under Executive Officers of the Registrant .

The information required by Item 405 of Regulation S-K is contained under the caption Section 16(a) Beneficial Ownership Reporting Compliance of the Proxy Statement and is incorporated by reference.

The Company s Code of Ethics for the CEO, CFO and Other Financial Professionals is publicly available on the Company s Internet website at http://www.alcoa.com under the section About Alcoa Corporate Governance. The remaining information required by Item 406 of Regulation S-K is contained under the captions Corporate Governance and Corporate Governance Business Conduct Policies and Code of Ethics of the Proxy Statement and is incorporated by reference.

The information required by Items 407(c)(3), (d)(4) and (d)(5) of Regulation S-K is included under the captions Item 1 Election of Directors Nominating Board Candidates Procedure and Director Qualifications and Corporate Governance Committees of the Board Audit Committee of the Proxy Statement and is incorporated by reference.

Item 11. Executive Compensation.

The information required by Item 402 of Regulation S-K is contained under the captions Director Compensation , Executive Compensation (excluding the information under the caption Compensation Committee Report), and Corporate Governance Recovery of Incentive Compensation of the Proxy Statement. Such information is incorporated by reference.

The information required by Items 407(e)(4) and (e)(5) of Regulation S-K is contained under the captions Corporate Governance Compensation Committee Interlocks and Insider Participation and Executive Compensation Compensation Committee Report of the Proxy Statement. Such information (other than the Compensation Committee Report, which shall not be deemed to be filed) is incorporated by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

The information required by Item 201(d) of Regulation S-K relating to securities authorized for issuance under equity compensation plans is contained under the caption Equity Compensation Plan Information of the Proxy Statement and is incorporated by reference.

The information required by Item 403 of Regulation S-K is contained under the captions Alcoa Stock Ownership Stock Ownership of Certain Beneficial Owners and Stock Ownership of Directors and Executive Officers of the Proxy Statement and is incorporated by reference.

Item 13. Certain Relationships and Related Transactions, and Director Independence.

The information required by Item 404 of Regulation S-K is contained under the captions Executive Compensation (excluding the information under the caption Compensation Committee Report), Corporate Governance Director Independence and Related Person Transactions of the Proxy Statement and is incorporated by reference.

The information required by Item 407(a) of Regulation S-K regarding director independence is contained under the captions Item 1 Election of Directors and Corporate Governance of the Proxy Statement and is incorporated by reference.

Item 14. Principal Accounting Fees and Services.

The information required by Item 9(e) of Schedule 14A is contained under the captions Item 2 Ratification of the Appointment of the Independent Registered Public Accounting Firm Report of the Audit Committee and Audit and Non-Audit Fees of the Proxy Statement and in Attachment A (Pre-Approval Policies and Procedures for Audit and Non-Audit Services) thereto and is incorporated by reference.

PART IV

Item 15. Exhibits, Financial Statement Schedules.

(a) The consolidated financial statements and exhibits listed below are filed as part of this report.

(1) The Company s consolidated financial statements, the notes thereto and the report of the Independent Registered Public Accounting Firm are on pages 81 through 158 of this report.

(2) Financial statement schedules have been omitted because they are not applicable, not required, or the required information is included in the consolidated financial statements or notes thereto.

(3) Exhibits.

Exhibit

Number	**Description***
3(a).	Articles of the Registrant as amended May 7, 2012, incorporated by reference to exhibit 3(a) to the Company s Current Report on Form 8-K dated May 10, 2012.
3(b).	By-Laws of the Registrant, as amended effective September 27, 2012, incorporated by reference to exhibit 3 to the Company s Current Report on Form 8-K dated October 3, 2012.
4(a).	Articles. See Exhibit 3(a) above.
4(b).	By-Laws. See Exhibit 3(b) above.
4(c).	Form of Indenture, dated as of September 30, 1993, between Alcoa Inc. and The Bank of New York Trust Company, N.A., as successor to J. P. Morgan Trust Company, National Association (formerly Chase Manhattan Trust Company, National Association), as successor Trustee to PNC Bank, National Association, as Trustee (undated form of Indenture incorporated by reference to exhibit 4(a) to Registration Statement No. 33-49997 on Form S-3).
4(c)(1).	First Supplemental Indenture, dated as of January 25, 2007, between Alcoa Inc. and The Bank of New York Trust Company, N.A., as successor to J.P. Morgan Trust Company, National Association (formerly Chase Manhattan Trust Company, National Association), as successor Trustee to PNC Bank, National Association, as Trustee, incorporated by reference to exhibit 99.4 to the Company s Current Report on Form 8-K (Commission file number 1-3610) dated January 25, 2007.
4(c)(2).	Second Supplemental Indenture, dated as of July 15, 2008, between Alcoa Inc. and The Bank of New York Mellon Trust Company, N.A., as successor in interest to J. P. Morgan Trust Company, National Association (formerly Chase Manhattan Trust Company, National Association, as successor to PNC Bank, National Association), as Trustee, incorporated by reference to exhibit 4(c) to the Company s Current Report on Form 8-K dated July 15, 2008.
4(c)(3).	Third Supplemental Indenture, dated as of March 24, 2009, between Alcoa Inc. and The Bank of New York Mellon Trust Company, N.A., as successor in interest to J.P. Morgan Trust Company, National Association (formerly Chase Manhattan Trust Company, National Association, as successor to PNC Bank, National Association), as Trustee, incorporated by reference to exhibit 4.2 to the Company s Current Report on Form 8-K dated March 24, 2009.
4(d).	Form of 5.55% Notes Due 2017, incorporated by reference to exhibit 4(d) to the Company s Annual Report on Form 10-K for the year ended December 31, 2008.
4(e).	Form of 5.90% Notes Due 2027, incorporated by reference to exhibit 4(d) to the Company s Annual Report on Form 10-K for the year ended December 31, 2008.

4(f).	Form of 5.95% Notes Due 2037, incorporated by reference to exhibit 4(d) to the Company s Annual Report on Form 10-K for the year ended December 31, 2008.
4(g).	Form of 6.00% Notes Due 2013, incorporated by reference to exhibit 4(a) to the Company s Current Report on Form 8-K dated July 15, 2008.
4(h).	Form of 6.75% Notes Due 2018, incorporated by reference to exhibit 4(b) to the Company s Current Report on Form 8-K dated July 15, 2008.
4(i).	Form of 5.25% Convertible Notes due 2014, incorporated by reference to exhibit 4.1 to the Company s Current Report on Form 8-K dated March 24, 2009.
4(j).	Form of 6.150% Notes due 2020, incorporated by reference to exhibit 4 to the Company s Current Report on Form 8-K dated August 3, 2010.
4(k).	Form of 5.40% Notes due 2021, incorporated by reference to Exhibit 4 to the Company s Current Report on Form 8-K, dated April 21, 2011.
4(l).	Alcoa Retirement Savings Plan for Fastener Systems Employees, incorporated by reference to exhibit 4(e) to the Company s Form S-8 Registration Statement dated July 27, 2012.
4(m).	Alcoa Retirement Savings Plan for Bargaining Employees, incorporated by reference to exhibit 4(d) to the Company s Form S-8 Registration Statement dated July 27, 2012.
4(n).	Alcoa Retirement Savings Plan for Salaried Employees, incorporated by reference to exhibit 4(c) to the Company s Form S-8 Registration Statement dated July 27, 2012.
4(o).	Alcoa Retirement Savings Plan for Hourly Non-Bargaining Employees, incorporated by reference to exhibit 4(c) to the Company s Post-Effective Amendment No. 6 to Form S-8 Registration Statement dated November 30, 2010.
10(a).	Alcoa s Summary of the Key Terms of the AWAC Agreements, incorporated by reference to exhibit 99.2 to the Company s Current Report on Form 8-K (Commission file number 1-3610) dated November 28, 2001.
10(b).	Charter of the Strategic Council executed December 21, 1994, incorporated by reference to exhibit 99.3 to the Company s Current Report on Form 8-K (Commission file number 1-3610) dated November 28, 2001.
10(c).	Amended and Restated Limited Liability Company Agreement of Alcoa Alumina & Chemicals, L.L.C. dated as of December 31, 1994, incorporated by reference to exhibit 99.4 to the Company s Current Report on Form 8-K (Commission file number 1-3610) dated November 28, 2001.
10(d).	Shareholders Agreement dated May 10, 1996 between Alcoa International Holdings Company and WMC Limited, incorporated by reference to exhibit 99.5 to the Company s Current Report on Form 8-K (Commission file number 1-3610) dated November 28, 2001.
10(e).	Side Letter of May 16, 1995 clarifying transfer restrictions, incorporated by reference to exhibit 99.6 to the Company s Current Report on Form 8-K (Commission file number 1-3610) dated November 28, 2001.
10(f).	Enterprise Funding Agreement, dated September 18, 2006, between Alcoa Inc., certain of its affiliates and Alumina Limited, incorporated by reference to exhibit 10(f) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2006.

10(f)(1).	Amendments to Enterprise Funding Agreement, effective January 25, 2008, between Alcoa Inc., certain of its affiliates and Alumina Limited, incorporated by reference to exhibit 10(f)(1) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2007.
10(g).	Five-Year Revolving Credit Agreement, dated as of July 25, 2011, among Alcoa Inc., the Lenders and Issuers named therein, Citibank, N.A., as Administrative Agent for the Lenders and Issuers, and JPMorgan Chase Bank, N.A., as Syndication Agent, incorporated by reference to exhibit 10 to the Company s Current Report on Form 8-K dated July 28, 2011.
10(g)(1).	Extension Request, dated as of November 28, 2012, to Five-Year Revolving Credit Agreement by Alcoa Inc. to Citibank, N.A., as Administrative Agent, and Consents to Extension Request executed by the Lenders listed therein.
10(h).	Aluminum Project Framework Shareholders Agreement, dated December 20, 2009, between Alcoa Inc. and Saudi Arabian Mining Company (Ma aden), incorporated by reference to exhibit 10(i) to the Company s Annual Report on Form 10-K for the year ended December 31, 2009.
10(h)(1).	First Supplemental Agreement, dated March 30, 2010, to the Aluminium Project Framework Shareholders Agreement, dated December 20, 2009, between Saudi Arabian Mining Company (Ma aden) and Alcoa Inc., incorporated by reference to exhibit 10(c) to Company s Quarterly Report on Form 10-Q for the quarter ended March 31, 2010.
10(i).	Closing Memorandum, dated December 20, 2009, between Alcoa Inc. and Aluminum Financing Limited, incorporated by reference to exhibit 10(j) to the Company s Annual Report on Form 10-K for the year ended December 31, 2009.
10(i)(1).	Parent Guarantee, dated December 20, 2009, between Abdullah Abunayyan Trading Corp. and Alcoa Inc., incorporated by reference to exhibit 10(j)(1) to the Company s Annual Report on Form 10-K for the year ended December 31, 2009.
10(i)(2).	Parent Guarantee, dated December 20, 2009, between Alcoa Inc. and Aluminum Financing Limited, incorporated by reference to exhibit 10(j)(2) to the Company s Annual Report on Form 10-K for the year ended December 31, 2009.
10(j).	Purchase Agreement, dated March 30, 2010, between Alcoa Inc., Aluminum Financing Limited, and Abdullah Abunayyan Trading Corp., incorporated by reference to exhibit 10(d) to Company s Quarterly Report on Form 10-Q for the quarter ended March 31, 2010.
10(k).	Settlement Agreement, dated as of October 9, 2012, by and between Aluminium Bahrain B.S.C., Alcoa Inc., Alcoa World Alumina LLC, and William Rice, incorporated by reference to exhibit 10(a) to the company s Quarterly Report on Form 10-Q for the quarter ended September 30, 2012.
10(l).	Employees Excess Benefits Plan, Plan A, incorporated by reference to exhibit 10(b) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 1980.
10(l)(1).	Amendments to Employees Excess Benefits Plan, Plan A, effective January 1, 2000, incorporated by reference to exhibit 10(b)(1) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2000.
10(l)(2).	Amendments to Employees Excess Benefits Plan, Plan A, effective January 1, 2002, incorporated by reference to exhibit 10(j)(2) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2002.

10(l)(3).	Amendments to Employees Excess Benefits Plan, Plan A, effective December 31, 2007, incorporated by reference to exhibit 10(j)(3) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2007.
10(l)(4).	Amendments to Employees Excess Benefits Plan, Plan A, effective December 29, 2008, incorporated by reference to exhibit 10(j)(4) to Company s Annual Report on Form 10-K for the year ended December 31, 2008.
10(l)(5).	Amendment to Employees Excess Benefits Plan A, effective December 18, 2009, incorporated by reference to exhibit 10(m)(5) to the Company s Annual Report on Form 10-K for the year ended December 31, 2009.
10(l)(6).	Amendment to Employees Excess Benefits Plan A, effective January 1, 2011, incorporated by reference to exhibit 10(n)(6) to the Company s Annual Report on Form 10-K for the year ended December 31, 2010.
10(l)(7).	Amendments to Employees Excess Benefits Plan A, effective January 1, 2012, incorporated by reference to exhibit 10(l)(7) to the Company s Annual Report on Form 10-K for the year ended December 31, 2011.
10(m).	Alcoa Internal Revenue Code Section 162(m) Compliant Annual Cash Incentive Compensation Plan, incorporated by reference to Attachment D to the Company s Definitive Proxy Statement on Form DEF 14A, filed March 7, 2011.
10(n).	2004 Summary Description of the Alcoa Incentive Compensation Plan, incorporated by reference to exhibit 10(g) to the Company s Quarterly Report on Form 10-Q (Commission file number 1-3610) for the quarter ended September 30, 2004.
10(n)(1).	Incentive Compensation Plan of Alcoa Inc., as revised and restated effective November 8, 2007, incorporated by reference to exhibit 10(k)(1) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2007.
10(n)(2).	Amendment to Incentive Compensation Plan of Alcoa Inc., effective December 18, 2009, incorporated by reference to exhibit 10(n)(2) to the Company s Annual Report on Form 10-K for the year ended December 31, 2009.
10(o).	Employees Excess Benefits Plan, Plan C, as amended and restated effective December 31, 2007, incorporated by reference to exhibit 10(l) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2007.
10(o)(1).	Amendments to Employees Excess Benefits Plan, Plan C, effective December 29, 2008, incorporated by reference to exhibit 10(l)(1) to Company s Annual Report on Form 10-K for the year ended December 31, 2008.
10(o)(2).	Amendment to Employees Excess Benefits Plan C, effective December 18, 2009, incorporated by reference to exhibit 10(o)(2) to the Company s Annual Report on Form 10-K for the year ended December 31, 2009.
10(o)(3).	Amendment to Employees Excess Benefits Plan C, effective January 1, 2011, incorporated by reference to exhibit 10(p)(3) to the Company s Annual Report on Form 10-K for the year ended December 31, 2010.
10(o)(4).	Amendments to Employees Excess Benefits Plan C, effective January 1, 2012, incorporated by reference to exhibit 10(o)(4) to the Company s Annual Report on Form 10-K for the year ended December 31, 2011.

10(p).	Deferred Fee Plan for Directors, as amended effective July 9, 1999, incorporated by reference to exhibit 10(g)(1) to the Company s Quarterly Report on Form 10-Q (Commission file number 1-3610) for the quarter ended June 30, 1999.
10(q).	Restricted Stock Plan for Non-Employee Directors, as amended effective March 10, 1995, incorporated by reference to exhibit 10(h) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 1994.
10(q)(1).	Amendment to Restricted Stock Plan for Non-Employee Directors, effective November 10, 1995, incorporated by reference to exhibit 10(h)(1) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 1995.
10(r).	Description of Changes to Non-Employee Director Compensation and Stock Ownership Guidelines, effective January 1, 2011, incorporated by reference to exhibit 10(b) to Company s Quarterly Report on Form 10-Q for the quarter ended September 30, 2010.
10(s).	Fee Continuation Plan for Non-Employee Directors, incorporated by reference to exhibit 10(k) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 1989.
10(s)(1).	Amendment to Fee Continuation Plan for Non-Employee Directors, effective November 10, 1995, incorporated by reference to exhibit 10(i)(1) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 1995.
10(s)(2).	Second Amendment to the Fee Continuation Plan for Non-Employee Directors, effective September 15, 2006, incorporated by reference to exhibit 10.2 to the Company s Current Report on Form 8-K (Commission file number 1-3610) dated September 20, 2006.
10(t).	Deferred Compensation Plan, as amended effective October 30, 1992, incorporated by reference to exhibit 10(k) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 1992.
10(t)(1).	Amendments to Deferred Compensation Plan, effective January 1, 1993, February 1, 1994 and January 1, 1995, incorporated by reference to exhibit 10(j)(1) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 1994.
10(t)(2).	Amendment to Deferred Compensation Plan, effective June 1, 1995, incorporated by reference to exhibit 10(j)(2) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 1995.
10(t)(3).	Amendment to Deferred Compensation Plan, effective November 1, 1998, incorporated by reference to exhibit 10(j)(3) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 1999.
10(t)(4).	Amendments to Deferred Compensation Plan, effective January 1, 1999, incorporated by reference to exhibit 10(j)(4) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 1999.
10(t)(5).	Amendments to Deferred Compensation Plan, effective January 1, 2000, incorporated by reference to exhibit 10(j)(5) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2000.
10(t)(6).	Amendments to Deferred Compensation Plan, effective January 1, 2005, incorporated by reference to exhibit 10(q)(6) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2005.

10(t)(7).	Amendments to Deferred Compensation Plan, effective November 1, 2007 incorporated by reference to exhibit 10(p)(7) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2007.
10(t)(8).	Amendments to Deferred Compensation Plan, effective December 29, 2008, incorporated by reference to exhibit 10(p)(8) to the Company s Annual Report on Form 10-K for the year ended December 31, 2008.
10(t)(9).	Amendment to Deferred Compensation Plan, effective April 1, 2009, incorporated by reference to exhibit 10(s)(9) to the Company s Annual Report on Form 10-K for the year ended December 31, 2009.
10(t)(10).	Amendment to Deferred Compensation Plan, effective December 18, 2009, incorporated by reference to exhibit 10(s)(10) to the Company s Annual Report on Form 10-K for the year ended December 31, 2009.
10(t)(11).	Amendment to Deferred Compensation Plan, effective January 1, 2011, incorporated by reference to exhibit 10(u)(11) to the Company s Annual Report on Form 10-K for the year ended December 31, 2010.
10(t)(12).	Amendment to Amendment to Deferred Compensation Plan, effective January 1, 2011, incorporated by reference to exhibit 10(u)(11) to the Company s Annual Report on Form 10-K for the year ended December 31, 2010, effective January 1, 2011.
10(t)(13).	Amendment to Deferred Compensation Plan, effective January 1, 2013.
10(u).	Summary of the Executive Split Dollar Life Insurance Plan, dated November 1990, incorporated by reference to exhibit 10(m) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 1990.
10(v).	Amended and Restated Dividend Equivalent Compensation Plan, effective January 1, 1997, incorporated by reference to exhibit 10(h) to the Company s Quarterly Report on Form 10-Q (Commission file number 1-3610) for the quarter ended September 30, 2004.
10(w).	Form of Indemnity Agreement between the Company and individual directors or officers, incorporated by reference to exhibit 10(j) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 1987.
10(x).	2004 Alcoa Stock Incentive Plan, as amended through November 11, 2005, incorporated by reference to exhibit 10.1 to the Company s Current Report on Form 8-K (Commission file number 1-3610) dated November 16, 2005.
10(y).	2009 Alcoa Stock Incentive Plan, incorporated by reference to Attachment C to the Company s Definitive Proxy Statement on Form DEF 14A filed March 16, 2009.
10(y)(1).	Amended and Restated 2009 Alcoa Stock Incentive Plan, dated February 15, 2011, incorporated by reference to exhibit 10(z)(1) to the Company s Annual Report on Form 10-K for the year ended December 31, 2010.
10(z).	Terms and Conditions for Special Retention Awards under the 2009 Alcoa Stock Incentive Plan, effective January 1, 2010, incorporated by reference to exhibit 10(e) to Company s Quarterly Report on Form 10-Q for the quarter ended March 31, 2010.
10(aa).	Alcoa Supplemental Pension Plan for Senior Executives, as amended and restated effective December 31, 2007, incorporated by reference to exhibit 10(u) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2007.

10(aa)(1).	Amendment to Alcoa Supplemental Pension Plan for Senior Executives, effective December 29, 2008, incorporated by reference to exhibit 10(u)(1) to Company s Annual Report on Form 10-K for the year ended December 31, 2008.
10(aa)(2).	Amendment to Alcoa Supplemental Pension Plan for Senior Executives, effective December 16, 2009, incorporated by reference to exhibit 10(y)(2) to the Company s Annual Report on Form 10-K for the year ended December 31, 2009.
10(aa)(3).	Amendment to Alcoa Supplemental Pension Plan for Senior Executives, effective December 18, 2009, incorporated by reference to exhibit 10(y)(3) to the Company s Annual Report on Form 10-K for the year ended December 31, 2009.
10(aa)(4).	Amendment to Alcoa Supplemental Pension Plan for Senior Executives, effective January 1, 2011, incorporated by reference to exhibit 10(bb)(4) to the Company s Annual Report on Form 10-K for the year ended December 31, 2010.
10(aa)(5).	Amendments to Alcoa Supplemental Pension Plan for Senior Executives, effective January 1, 2012, incorporated by reference to exhibit 10(aa)(5) to the Company s Annual Report on Form 10-K for the year ended December 31, 2011.
10(bb).	Deferred Fee Estate Enhancement Plan for Directors, effective July 10, 1998, incorporated by reference to exhibit 10(r) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 1998.
10(cc).	Alcoa Inc. Change in Control Severance Plan, as amended and restated effective November 8, 2007, incorporated by reference to exhibit 10(x) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2007.
10(cc)(1).	Amendment to Alcoa Inc. Change in Control Severance Plan, effective December 16, 2009, incorporated by reference to exhibit 10(bb)(1) to the Company s Annual Report on Form 10-K for the year ended December 31, 2009.
10(dd).	Form of Agreement for Stock Option Awards, effective January 1, 2004, incorporated by reference to exhibit 10(a) to the Company s Quarterly Report on Form 10-Q (Commission file number 1-3610) for the quarter ended September 30, 2004.
10(ee).	Form of Agreement for Stock Awards, effective January 1, 2004, incorporated by reference to exhibit 10(b) to the Company s Quarterly Report on Form 10-Q (Commission file number 1-3610) for the quarter ended September 30, 2004.
10(ff).	Form of Agreement for Performance Share Awards, effective January 1, 2004, incorporated by reference to exhibit 10(c) to the Company s Quarterly Report on Form 10-Q (Commission file number 1-3610) for the quarter ended September 30, 2004.
10(gg).	Stock Option Award Rules, revised January 1, 2004, incorporated by reference to exhibit 10(d) to the Company s Quarterly Report on Form 10-Q (Commission file number 1-3610) for the quarter ended September 30, 2004.
10(hh).	Stock Awards Rules, effective January 1, 2004, incorporated by reference to exhibit 10(e) to the Company s Quarterly Report on Form 10-Q (Commission file number 1-3610) for the quarter ended September 30, 2004.
10(ii).	Performance Share Awards Rules, effective January 1, 2004, incorporated by reference to exhibit 10(f) to the Company s Quarterly Report on Form 10-Q (Commission file number 1-3610) for the quarter ended September 30, 2004.

10(jj).	2005 Deferred Fee Plan for Directors, as amended, effective January 17, 2013.
10(kk).	Global Pension Plan, effective January 1, 1998, incorporated by reference to exhibit 10(jj) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2004.
10(kk)(1).	Amendments to Global Pension Plan, incorporated by reference to exhibit 10(jj)(1) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2004.
10(kk)(2).	Amendments to Global Pension Plan, effective January 1, 2005, incorporated by reference to exhibit 10(gg)(2) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2005.
10(kk)(3).	Amendments to Global Pension Plan, effective December 1, 2005, incorporated by reference to exhibit 10(gg)(3) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2005.
10(kk)(4).	Amendments to Global Pension Plan, effective December 29, 2008, incorporated by reference to exhibit 10(ff)(4) to the Company s Annual Report on Form 10-K for the year ended December 31, 2008.
10(kk)(5).	Amendments to Global Pension Plan, effective July 1, 2009, incorporated by reference to exhibit 10(jj)(5) to the Company s Annual Report on Form 10-K for the year ended December 31, 2009.
10(kk)(6).	Amendments to Global Pension Plan, effective December 18, 2009, incorporated by reference to exhibit 10(jj)(6) to the Company s Annual Report on Form 10-K for the year ended December 31, 2009.
10(kk)(7).	Amendment to Global Pension Plan, effective January 1, 2011, incorporated by reference to exhibit 10(mm)(7) to the Company s Annual Report on Form 10-K for the year ended December 31, 2010.
10(kk)(8).	Amendment to Global Pension Plan, effective January 1, 2011.
10(ll).	Executive Severance Agreement, as amended and restated effective December 8, 2008, between Alcoa Inc. and Klaus Kleinfeld, incorporated by reference to exhibit 10(gg) to the Company s Annual Report on Form 10-K for the year ended December 31, 2008.
10(ll)(1).	Executive Severance Agreement, as amended and restated effective December 8, 2008, between Alcoa Inc. and Charles D. McLane, Jr., incorporated by reference to exhibit 10(gg)(2) to the Company s Annual Report on Form 10-K for the year ended December 31, 2008.
10(ll)(2).	Form of Executive Severance Agreement between the Company and new officers entered into after July 22, 2010, incorporated by reference to exhibit 10(a) to Company s Quarterly Report on Form 10-Q for the quarter ended September 30, 2010.
10(mm).	Summary of 2013 Non-Employee Director Compensation and Stock Ownership Guidelines.
10(nn).	Form of Award Agreement for Stock Options, effective January 1, 2006, incorporated by reference to exhibit 10.2 to the Company s Current Report on Form 8-K (Commission file number 1-3610) dated November 16, 2005.
10(oo).	Form of Award Agreement for Stock Awards, effective January 1, 2006, incorporated by reference to exhibit 10.3 to the Company s Current Report on Form 8-K (Commission file number 1-3610) dated November 16, 2005.

10(pp).	Form of Award Agreement for Performance Share Awards, effective January 1, 2006, incorporated by reference to exhibit 10.4 to the Company s Current Report on Form 8-K (Commission file number 1-3610) dated November 16, 2005.
10(qq).	Form of Award Agreement for Performance Stock Options, effective January 1, 2006, incorporated by reference to exhibit 10.5 to the Company s Current Report on Form 8-K (Commission file number 1-3610) dated November 16, 2005.
10(rr).	Form of Award Agreement for Stock Options, effective May 8, 2009, incorporated by reference to exhibit 10.2 to the Company s Current Report on Form 8-K dated May 13, 2009.
10(ss).	Terms and Conditions for Stock Options, effective January 1, 2011, incorporated by reference to exhibit 10(c) to the Company s Quarterly Report on Form 10-Q for the quarter ended June 30, 2011.
10(tt).	Form of Award Agreement for Restricted Share Units, effective May 8, 2009, incorporated by reference to exhibit 10.3 to the Company s Current Report on Form 8-K dated May 13, 2009.
10(uu).	Terms and Conditions for Restricted Share Units, effective January 1, 2011, incorporated by reference to exhibit 10(b) to the Company s Quarterly Report on Form 10-Q for the quarter ended June 30, 2011.
10(vv).	Summary Description of Equity Choice Program for Performance Equity Award Participants, dated November 2005, incorporated by reference to exhibit 10.6 to the Company s Current Report on Form 8-K (Commission file number 1-3610) dated November 16, 2005.
10(ww).	Reynolds Metals Company Benefit Restoration Plan for New Retirement Program, as amended through December 31, 2005, incorporated by reference to exhibit 10(rr) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2005.
10(ww)(1).	Amendments to the Reynolds Metals Company Benefit Restoration Plan for New Retirement Program, effective December 18, 2009, incorporated by reference to exhibit 10(tt)(1) to the Company s Annual Report on Form 10-K for the year ended December 31, 2009.
10(ww)(2).	Amendments to the Reynolds Metals Company Benefit Restoration Plan for New Retirement Program, effective January 1, 2012, incorporated by reference to exhibit 10(xx)(2) to the Company s Annual Report on Form 10-K for the year ended December 31, 2011.
10(xx).	Global Expatriate Employee Policy (pre-January 1, 2003), incorporated by reference to exhibit 10(uu) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2005.
10(yy).	Form of Special Retention Stock Award Agreement, effective July 14, 2006, incorporated by reference to exhibit 10.3 to the Company s Current Report on Form 8-K (Commission file number 1-3610) dated September 20, 2006.
10(zz).	Omnibus Amendment to Rules and Terms and Conditions of all Awards under the 2004 Alcoa Stock Incentive Plan, effective January 1, 2007, incorporated by reference to exhibit 10(tt) to the Company s Annual Report on Form 10-K (Commission file number 1-3610) for the year ended December 31, 2007.
10(aaa).	Letter Agreement, dated August 14, 2007, between Alcoa Inc. and Klaus Kleinfeld, incorporated by reference to exhibit 10(b) to the Company s Quarterly Report on Form 10-Q (Commission file number 1-3610) for the quarter ended September 30, 2007.
10(bbb).	Employment Offer Letter, dated April 2, 2012, between Alcoa Inc. and Audrey Strauss, incorporated by reference to exhibit 10(b) to the Company s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012.

10(ccc).	Director Plan: You Make a Difference Award, incorporated by reference to exhibit 10(uu) to the Company s Annual Report on Form 10-K for the year ended December 31, 2008.
10(ddd).	Form of Award Agreement for Stock Options, effective January 1, 2010, incorporated by reference to exhibit 10(ddd) to the Company s Annual Report on Form 10-K for the year ended December 31, 2009.
12.	Computation of Ratio of Earnings to Fixed Charges.
21.	Subsidiaries of the Registrant.
23.	Consent of Independent Registered Public Accounting Firm.
24.	Power of Attorney for certain directors.
31.	Certifications pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
95.	Mine Safety Disclosure.
101. INS	XBRL Instance Document.
101. SCH	XBRL Taxonomy Extension Schema Document.
101. CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
101. DEF	XBRL Taxonomy Extension Definition Linkbase Document.
101. LAB	XBRL Taxonomy Extension Label Linkbase Document.
101. PRE	XBRL Taxonomy Extension Presentation Linkbase Document.

* Exhibit Nos. 10(l) through 10(ddd) are management contracts or compensatory plans required to be filed as Exhibits to this Form 10-K. Amendments and modifications to other Exhibits previously filed have been omitted when in the opinion of the registrant such Exhibits as amended or modified are no longer material or, in certain instances, are no longer required to be filed as Exhibits.

No other instruments defining the rights of holders of long-term debt of the registrant or its subsidiaries have been filed as Exhibits because no such instruments met the threshold materiality requirements under Regulation S-K. The registrant agrees, however, to furnish a copy of any such instruments to the Commission upon request.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ALCOA INC.

February 19, 2013 By /s/ Graeme W. Bottger
Graeme W. Bottger
Vice President and Controller

(Also signing as Principal Accounting Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ Klaus Kleinfeld	Chairman and Chief Executive Officer	February 19, 2013
Klaus Kleinfeld	(Principal Executive Officer and Director)	
/s/ Charles D. McLane, Jr.	Executive Vice President and Chief	February 19, 2013
Charles D. McLane, Jr.	Financial Officer (Principal Financial Officer)	

Arthur D. Collins, Jr., Kathryn S. Fuller, Judith M. Gueron, Michael G. Morris, E. Stanley O Neal, James W. Owens, Patricia F. Russo, Sir Martin Sorrell, Ratan N. Tata and Ernesto Zedillo, each as a Director, on February 19, 2013, by Graeme W. Bottger, their Attorney-in-Fact.*

*By /s/ Graeme W. Bottger
Graeme W. Bottger

Attorney-in-Fact