



Army and Air Force Mutual Aid Association

120th Annual Report

For the year ended 31 December 1998

Things members should do

- 1.** File certified copies of marriage, former marriages, divorces and birth certificates of your spouse and minor children in the Association vault for future use in processing pension, compensation and other claims for your family. Copies of these records will be provided or the originals returned whenever needed.
- 2.** Keep beneficiary designations updated.
- 3.** Be sure that *all* adult members of the family have a valid will.
- 4.** List all life insurance policies in your Family Information Record (FIR). This provides a record even if policies become lost. Members may send life insurance policies, wills and other important papers for storage in our fireproof vault.
- 5.** Ask our counselors for objective advice in life insurance planning before buying new life insurance to arrange the best possible program.
- 6.** Seek our advice on the Survivor Benefit Plan and things to do before retiring from active service.
- 7.** Update the Family Information Record (FIR) that you receive annually. This ensures that you and your family receive accurate benefit information.
- 8.** Read the reports and other communications from the Association. They are written in the interest of members and their families.
- 9.** Support and protect the interest of your Association. Recommend it to your associates. It is the only *voluntary, nonprofit* mutual benefit association offering membership to U.S. Army and Air Force Officers, Warrant Officers and Non-commissioned Officers maintained for your benefit and that of your families.
- 10.** Be sure that your spouse knows about the Association's services. Advise your family to contact our office immediately in case of emergency.
- 11.** Keep the Association advised of your address so that Annual Reports, newsletters and other mailings will reach you promptly. Your e-mail address, telephone and fax numbers should always be kept current.

"Every Member Get a Member"

1879

OVER 119 YEARS OF SERVICE

1998

Organized 13 January 1879

120th Annual Report

For the year ended 31 December 1998

Army and Air Force Mutual Aid Association

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Fort Myer, Virginia 22211-1110

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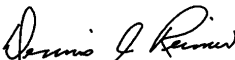
Night depository at both locations

Message to the Army and Air Force Mutual Aid Association

I am honored and delighted to recognize all the members of the Army and Air Force Mutual Aid Association for the outstanding support they provide to our soldiers and families.

Today, our Armed Forces enjoy the undisputed distinction of being the best in the world. That's no accident — we have a military made up of outstanding men and women and we have the support of the American people. Together, we truly are "Team America." For over 120 years the Association has been a vital part of that team, providing quality service and unqualified support for the Army family. Thank you for being such a great part of a great team.

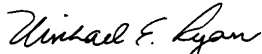
I wish the Association and each of you the very best.


Dennis J. Reiner
General, United States Army

**A MESSAGE TO THE MEMBERSHIP OF THE ARMY AND AIR
FORCE MUTUAL AID ASSOCIATION**

I would like to offer my heartfelt gratitude to the Army and Air Force Mutual Aid Association for its outstanding support to our military members and their families. Our service men and women are frequently deployed overseas and they can rest easy knowing that the association is ready to lend a helping hand whenever needed.

Congratulations on your 120th anniversary and thank you for providing such wonderful support to our Armed Forces.

A handwritten signature in black ink that reads "Michael E. Ryan". The signature is written in a cursive, flowing style.

**MICHAEL E. RYAN
General, United States Air Force**

**REPORT OF THE ONE HUNDRED TWENTIETH ANNUAL MEETING
OF THE
ARMY AND AIR FORCE MUTUAL AID ASSOCIATION
FOR THE YEAR 1998**

*Fort Myer, Virginia 22211-1110
13 April 1999*

[The Annual Meeting of the Army and Air Force Mutual Aid Association convened at 1200 hours, Tuesday, 13 April 1999, at Fort Myer, Virginia. The meeting was called to order by GEN Michael S. Davison, Chairman of the Board of Directors. Nine of the 17 Directors were present.

[Without objection, the reading of the minutes of the Annual Meeting of 14 April 1998 was dispensed with because they had been subsequently published in the Annual Report. GEN Davison then presented the Report of the Board of Directors for the year 1998.]

REPORT OF THE BOARD

The meeting will come to order!

Welcome to our Annual Meeting, the 120th since our beginning in 1879. I am Mike Davison, the Chairman of the Board of Directors.

Once again, I am pleased to have a guest with us from Navy Mutual Aid Association. He is, and would you please stand as you are introduced: RADM Philip J. Coady, USN, Ret, President, Navy Mutual Aid Association.



GEN Michael S. Davison

Admiral Coady, welcome aboard!

Our last Annual Meeting was on 14 April 1998. The minutes were published in the Annual Report that covered our activities for 1997. If there is no objection, we will dispense with the reading of the report. *[No objection, motion approved.]*

One note with respect to our Board of Directors: I have accepted, with regret, the resignation from our Board of LTG Edward D. Baca, USA, whose final active duty assignment was as Chief, National Guard. GEN Baca served on our Board from November 1994 to December 1998. We were honored, indeed, to have had Ed Baca serve in this capacity and we wish him good health and happy times in retirement at his New Mexico location.

My report today will cover membership, services, finance, and an overview of events during 1998.

We begin our 121st year of service to the military community with sustained rates of growth in membership, record services to our members and an impressive expansion of our finances. Our insurance in force grew by 12%, our services reached thousands of members at their locations and our assets increased by 8.75%. As we reported last year, 1997 was a banner year



AAFMAA's 120th Annual Meeting was an opportunity to pass wisdom from one generation to the next.

in member gains, making it a pretty tough act to follow. The 1998 gains in new members support a continued upward trend in our membership. There was a net gain of 984 new members including our FSO (Free Service Only) members. Repeat visits to the non-commissioned officer training activities at Gunter Annex in Montgomery, Alabama and at selected gatherings of NCOs worldwide contributed to a significant increase in growth in the Air Force NCO category.

MEMBERSHIP

We have continued with our firm commitment to attract youthful members for the continued growth of the Association. We focused our attention on the officers and NCO service academies and the Army and Air Force ROTC, OCS and WOCS accession programs. During 1998, 76% of our new members came from these sources.

In response to the many requests from our members, we have increased our life insurance service levels to an initial maximum amount of coverage of \$300,000 for members and for their spouses. Later this spring, we will begin to offer an optional life insurance rider for spouses and children with new policies. Watch for more information on this service by mail, e-mail and newsletter.

Our insurance operations are expanding as evidenced by growth rates of certificates in force and lives insured. I am pleased to report that our certificates in force and our lives insured both increased by 2% during 1998.

In reaching out to the NCO community during 1998, Brad Snyder and I visited the Chiefs of Staff and the senior enlisted advisors of the Army and the Air Force. We received their support and some very thought-provoking suggestions that we have folded into our routine operations.

We finished the year with a total of 61,712 members.

SERVICES

Services constitute the core of our existence. The one constant that has remained since our inception, although it has been rephrased to accommodate changing times, is: to aid the families of the deceased members in a prompt, simple and substantial manner. This mission has grown from providing low-cost insurance to military members who could not purchase protection, to providing today's array of quality life insurance programs tailored to the changing needs of our members.

Our identifying hallmark, providing counseling services on government statutes that affect the benefits of each member and his or her family, is without parallel. We are always developing tools to expand our services with a vision that looks well into the years ahead. The Internet holds promise to open the door for many new services. We are planning for and developing programs to provide our members with direct access to their records. Imagine our ability to provide pre-retirement counseling without your ever leaving your home or office!

As you know, the new information age has arrived. We will be a part of that as we introduce new ways to serve our members. We will continually improve our services and benefits. During 1998, 1,227 families were direct recipients of our family assistance services. Office visits, calls and letters seeking advice and counsel were responded to by our member service staff.

My deepest gratitude goes to our members and to all of the major commanders and their staffs for the excellent support that we received when visiting their commands. Our mission to educate active duty personnel on their government benefits is alive and well. Our staff visited 56 installations or areas where they made many presentations.

Counseling services at our Ft. Myer and Pentagon concourse locations are very active and well appreciated.

FINANCE

In the past year, the Association improved its already excellent financial condition. Financial operations in 1998 set another record. Income from its operations exceeded \$41 million. The market value of assets grew significantly. These continuing outstanding financial results have allowed the Board of Directors to continue, since 1995, the 8.25% crediting rate to cash values of members holding whole life insurance. The crediting rate translates into an excellent policy value with



Ken Hanst (l), AAFMAA President from 1957-1983, greeted members along with current President Brad Snyder.

growth potential. First, the cash value of the account earns a competitive rate of interest. Our 8.25% crediting rate is significantly higher than other organizations offering similar insurance products. Second, the high crediting rate allows the cash value to grow over time. In the long run, this increases the death benefit ultimately paid to your beneficiaries. We can maintain its high crediting rate because we insure a select group of people—you and your families! For the holders of our various term insurance plans, we once again provided either a 20% or a 30% premium refund.



Former President Ken Hanst, current President Brad Snyder, and VP for Services and Secretary Joe Francis together represent a total of 91 years of AAFMAA leadership.

To provide an overall focus to our many activities, we have drafted a five-year strategic plan which provides the Board and our operating staff a road map until the year 2004. As you might expect, we are focusing on new ways to serve our members using the Internet, expanding our life insurance products, and expanding our presence at the service schools for officers and for non-commissioned officers. Each year our budget will be developed within the context of the strategic plan and the plan itself will be extended an additional year to maintain its continuing five-year guidance.

In summary, 1998 was a very good year. Our financial operations led the way and we were able to make some prudent choices that we believe will assure sound operations as we move into our five-year strategic plan. The plan emphasizes continued membership growth, expanded life insurance products and service enhancements—the keys to our future.

I thank you for joining us today and I cannot stress enough how important it is for you and your family to take advantage of the array of services and insurance products available. Please use your Association to the fullest to ensure that your loved ones are secure should the unexpected occur.

We will now receive the reports of the officers of the Association, beginning with our President, Brad Snyder.

(Signed)
Michael S. Davison
General, USA, Retired
Chairman of the Board

[GEN Davison called on the President to have the reports of the officers presented.]

REPORTS OF THE OFFICERS

REPORT OF THE PRESIDENT, CAPTAIN BRADLEY J. SNYDER



Pres. Brad Snyder

Thank you, GEN Davison.

Welcome—and thank you for sharing the day with us.

A special welcome and thank you to GEN Joe Ralston, our guest speaker today, for taking his valuable time to be with us today, especially in light of the current world situation.

GEN Davison reported that 1998 was another great year in our 120-year history. He mentioned our insurance in force, membership, finance and, of course, our unique services to our members and their families. You will hear greater detail in these areas in the reports that follow.

I would like to take just a few moments to speak of our vision as we enter the 21st Century.

We will reevaluate and challenge all facets of our operations while staying focused on our mission.

We will continue to work on more insurance products that will meet the needs of our members and their families. Our efforts will be directed toward more flexible, individually tailored products provided at the lowest possible cost. Amounts will be increased as our assets and other indicators allow us to do so prudently. When you think of life insurance, first think of us!

We will continue to protect our unique tax-exempt status which enables us to return more to you, the members.

We have successfully negotiated a new lease for our office at Ft. Myer for another 30 years. This will continue to be our base of operation.

Our services to members and their families remain our hallmark. We will continue to preserve the personal touch as we continue to review what we do and how we do it. This includes always having a human to answer our phone to properly direct your calls. A continuation and increase in the number of our face-to-face counseling and meetings to provide the very valuable information we have to share. Emphasis will be placed on providing individual attention to our members.

Our greatest challenge will be to expand the availability of our services to more members, thereby attracting more officers and noncommissioned officers of the Army and Air Force to join. We will accomplish this by increasing our outreach

to bases and posts with high concentrations of members. We will also continue to pursue the use of the Internet technology to have members access their files via our Web site. This will bring us into a closer relationship with our members. We will be able to electronically deliver materials on file in an more efficient manner. As we communicate in this manner it will be possible to individually tailor products for the member based on information in their files.

As always, this will be accomplished by preserving what we have now and not by reducing anything else.

The ability to achieve this vision depends on our ability to increase our membership by selling our great insurance products; delivering our unique services in a timely and efficient manner; and by the stewardship of our finances.

I would like to acknowledge the special efforts of your non-compensated Board of Directors and counselors, including the Finance Committee chaired by GEN Bob Sennewald and the Membership Committee chaired by Major Bill Clark. We are indeed fortunate for their generosity and leadership.

I would also like to thank those who make our services and products a reality: the officers, managers, staff members, special consultants and advisors who do the day-to-day work that benefits us all. They bring the essence of the personal touch to our products and services! Also, I'd like to pay a special tribute to five staff members who retired in 1998: Mrs. Margo Ramage, Mrs. Betty Shipp, LTC Bob Kauffman, COL Warren Murray and Mrs. Janet Lewin. We are indebted for their many years of service to our Association.

To once again give you the diversity of our membership, our oldest member is COL Jack Fuller, who is 104 (born March 1895); our youngest member is WO1 Gavin Glasenapp, who is 20 (born November 1978) and our longest being a member is COL Michael Buckley, 73 years, joined in August of 1925. On the surviving spouse side, our oldest spouse is Mrs. Carrie Trunk, who is 105 (born January 1894); our youngest is Mrs. Brandy Heriberto, who is 30 years old (born August 1968); and the longest being a surviving spouse is Mrs. Alice Neagle, 68 years of service received, her husband died September 1930.

Continuing on our successful initiative from last year of having each of you sponsor a new member for one year under our Free Service Only (FSO) program; we have placed at your seat two applications. These are gifts of caring and giving! We would like you to give these to non-members who meet the eligibility requirements and are under age 86. You can give these memberships, paid for by the Association for one full year, so they can experience our unique services and products for a year, while deciding on permanent membership. In the past our best method of attracting new members has always been by other members.

There are many of your friends who missed joining the Association for a number of reasons and now, if eligible, they can still become members through you. Just

have them complete the very basic application and return it to the office. They will be members for one year free! Your name will be linked to their file so that they will always know who cared enough to give them this gift. Make sure you put your name on the “sponsored by” line. If you have any questions, please see one of the staff as you leave today.

Thank you!

[The President then called on the Vice President for Insurance Operations.]

REPORT OF THE VP FOR INSURANCE OPERATIONS, LTC RALPH C. CLARK:

Mr. President, my report will cover two topics: membership and insurance.

First, membership. Our Association had another good year from a membership perspective. We concluded 1998 with 61,712 members on the rolls—a net increase of 984 for the year. This is particularly significant when one considers the environment of shrinking military manpower levels, which is adversely impacting membership for most military associations.



VP for Insurance Ops.
Ralph Clark

Two thousand, four hundred eleven new members joined our Association in 1998. We acquired 76% of those new members through our Career Assistance Program, or CAP. Recall, that’s the membership incentive program that provides a low-interest-rate loan to certain officers and NCOs. The Free Service Only membership program initiated at last year’s Annual Meeting accounted for 232 of our new members. Air Force membership had net growth of over 10%, closing the year at just under 6,900, or 11% of total membership. We had a net gain of 173 non-commissioned officers finishing the year with 554 NCOs on our books. While we did have a good year, we are looking forward to a better year in 1999.

My next topic is insurance. In this area our Association also had a very good year. We provided 3,296 new policies to new and existing members. One thousand, eight hundred forty-one of these policies accompanied those CAP loans I spoke of earlier. One thousand, two hundred thirty-eight existing members took policies on their own lives, their spouses, children, or grandchildren. New, non-CAP members accounted for the rest. Term insurance products are popular with our membership: there were 1,866 term policies on our books at year end—just two years after first offering it.

Our insurance products are very competitive, especially when one considers the crediting rate of 8.25% for our value added insurance and the 20% and 30% refunds of premiums we have provided our non-smoking term policy owners. If you or someone you know needs life insurance and are eligible, please visit our membership team at the table in the lobby. At year end 1998 we had \$1.7 billion

worth of insurance on our books, an increase of over \$185 million for the year. Our actuary reports that the reserves of the Association are necessary and sufficient to provide for this promise of future benefit payments.

In summary, our Association had a very successful 1998 from a membership and insurance standpoint, and we look forward to even greater growth in 1999.

Mr. President, that concludes my report.

[A motion was made to accept the report of the VP for Insurance Operations, seconded and approved.]

REPORT OF THE VP FOR SERVICES AND SECRETARY, MAJ JOSEPH J. FRANCIS:

My report will cover highlights of the services we provided to our members in 1998.

Our AAFMAA services are on call to our extended family of 256,000. We touched the lives of many of them throughout the year. With regret, I report the loss of 786 members to death during 1998. In addition there were 251 widow losses. Finally, our Family Assistance Department assisted with the affairs of an additional 190 immediate family members. We continue to fulfill our pledge made to each of you to provide a lifetime of service to our 9,784 surviving widows. In my last report I mentioned that we were in touch with some of the spouses because we believed that they might qualify for a modest annuity under the provisions of PL 105-85. Our search is completed and today 49 of our surviving spouses are receiving benefits from this program.



VP for Services and Secretary Joe Francis

In 1998 we continued our program of visits to key military installations. Throughout the year we accomplished this task by sending our counselors to make presentations at 56 installations about government benefits and the work of this Association. Our counselors spent 190 days on the road. The use of laptop computers permitted us to provide the same level of service to our members and prospective members at their location that is available here at Ft. Myer. We are grateful for the support given to our Association by the local commanders who have made this service possible.

During 1998, more than 3,500 members made a personal visit to our Ft. Myer office or to the branch office on the Pentagon's concourse. Our visits away from this area afforded us the opportunity to provide direct service to our members at their duty station locations. Your Association's staff responded to thousands of items of correspondence; we received and filed almost 9,000 family documents in our vault storage area and we responded to requests for information with more than 28,000 incoming and outgoing telephone calls as we continued to interact

with our membership. Our Family Assistance Department saw to the needs of over 1,200 families who lost a loved one.

The year 1998 provided us with an ongoing challenge in educating our members who have retired from their military service. For the first time, a retired person enrolled in the Survivor Benefit Plan for more than two years, was permitted to disenroll from this program. We provided the needed analysis to our members on this important question and saved many from making an irreversible mistake.

Mr. President, this concludes my report.

[A motion was made to accept the report of the VP for Services and Secretary, seconded and approved.]

REPORT OF THE VP FOR FINANCE AND TREASURER, MAJ WALTER R. LINCOLN:



VP for Finance and
Treasurer Walt Lincoln

My report covers investments, financial results, and the crediting rate for 1999.

The amount of life insurance in force constitutes the Association's liabilities. Our investments are the assets which enable us to meet those liabilities. Investments grew from \$552 million in 1997 to \$600 million in 1998. This record growth of \$48 million carries the assets to the highest level in Association history. These assets plus our future premium income and future investment earnings are required to meet our future liabilities. The \$600 million of investments are composed of \$383 million in bonds; \$67 million in real estate mortgages; \$18 million in real estate properties; \$74 million in equity mutual funds; \$46 million in member loans; and \$12 million in cash and other assets. On a market value basis, these assets exceed \$662 million.

In 1998 we eliminated directly held, individual stocks. I removed the previous equity manager. The performance had lagged the benchmark over the long term. I shifted the bulk of equities to an S&P 500 index fund. We anticipate this will increase returns and will certainly reduce costs. Always conscious of the need to diversify, I added an international fund and a small cap fund. For perspective, the capital contributed to equities approximates \$21 million while the market value of our three mutual funds exceeds \$74 million.

The operating results for 1998 were the best in the Association's history. Net income from operations totaled \$41 million, an increase of 52% over 1997.

Consolidated Realty, the Association's real estate subsidiary, contributed to the financial results. The four properties within Consolidated Realty had a 95% occupancy rate. Net operating income from real estate increased 18%. In 1998, Consolidated Realty committed to build an additional office building of 60,000

square feet. At the next Annual Meeting we expect to report outstanding results from real estate since the building is already 100% leased. Construction will be completed on May 31.

All these combined results were accomplished at the same time we reduced—*reduced*—the net operating budget. We cut administrative and operating expenses from \$4.9 million in 1997 to less than \$4.8 million in 1998. This reduction of \$181,000 was a 3.6% cut. In 1998 we signed a new lease with the Army to remain in the office at Ft. Myer. The Association will remain at Ft. Myer for the next 30 years! We have begun a program to modernize items which were put on hold pending the outcome of the lease negotiations. These include:

- An expanded reception area for members;
- New carpeting throughout the building;
- New ceiling tile and lighting; and,
- A new telephone system—but remember, you'll always get a human when you call *us* on the phone.

Our net yield on assets for 1998 was 7.2%. The net yield calculation does not include capital gains. The total portfolio return reflects capital gains and time-weighted returns. For 1998 the total portfolio return was 12.6%.

Our asset/liability team, consisting of external investment managers, auditor, liability actuary, general counsel and in-house staff, all contributed to this great success. With us today are: Steve Meltzer and Kevin Holt of Scudder Kemper Investments, Tom Moloney of The Northern Trust Company, Ron Mangas of Centennial Management Corporation, Steve Rogers of Randall Hagner & Co., our auditor Bob Verkouteren of Verkouteren, Auerbach, Olsen & Co., our liability actuary Arthur C. Eddy, and our general counsel John Hagner of Womble Carlyle Sandridge & Rice. Can we promise to deliver these outstanding results forever? No, but we're going to try!

These record financial results enabled the Board of Directors to maintain a crediting rate of 8.25% on whole life policies for 1999. Can we promise an 8.25% crediting rate forever? No, but we will continue to deliver financial results to support outstanding insurance products.



Two active Army officers listen intently to reports of the Association's financial health and membership growth.

In summary, 1998 was the best financial year in the Association's 120-year history!

Mr. President, this concludes my report.

[A motion was made to accept the report of the VP for Finance and Treasurer.]

REPORT OF THE NOMINATING COMMITTEE

19 March 1999

Mr. Chairman:

The Nominating Committee is pleased to present the following nominations for Directors of the Army and Air Force Mutual Aid Association:

To serve until the Annual Meeting in 2003:

(First elected term)

MAJ Joe R. Reeder, USAR

(Second consecutive term)

MAJ William D. Clark, USA, Retired
CSM Jimmie W. Spencer, USA, Retired

(Signed)

BG Willie B. Nance, USA
Chairman

(Signed)

COL John H. Clarke, USA
Member

(Signed)

MAJ Margaret Z. Lawson, USAF
Member

(Signed)

SMS Kenneth R. Martin, USAF
Member

[GEN Davison then called for additional nominations from the floor. There being none, a motion to close the nominations was made, seconded and accepted. The Chairman declared the election of MAJ Joe R. Reeder, USAR, MAJ William D. Clark, USA, Retired and CSM Jimmie W. Spencer, USA, Retired, to serve until the Annual Meeting in 2003.]

[GEN Davison then introduced the guest speaker, GEN Joseph W. Ralston, USAF, Vice Chairman, Joint Chiefs of Staff.]

[Speech as written for General Joseph W. Ralston, USAF, Vice Chairman, Joint Chiefs of Staff, follows.]

“SETTING THE WORLD STAGE”

Thank you, General Davison, for that generous introduction—and let me note what a very special pleasure it is to be introduced by General Davison—a genuine hero in World War II; a legend at West Point; a superb combat commander in Vietnam and Cambodia; and a leader in corporate America. I know you all are fortunate to have him at the helm of the Army and Air Force Mutual Aid Association and I’m honored to follow him to the podium.



Guest speaker GEN Joseph Ralston, USAF, Vice Chairman of the Joint Chiefs of Staff, emphasizes the importance of keeping our all-volunteer armed forces attractive to new recruits.

General Davison, General Sennewald, General Guthrie, my former wing commander and friend, Brad Hosmer, it is my pleasure to be able to join you today for lunch. General Shelton regrets he is not able to be here.

The Army and Air Force Mutual Aid Association is a tremendous organization and it has a richly deserved reputation based on 120 years of great service to the men and women of the Army and Air Force—active, Guard and Reserves.

I’ve been a member for a number of years now, and I must admit that it is a great relief each month to pay my dues, especially when I consider the alternative! And, I want to assure each of you that I appreciate all the help the Association provides.

I want to spend the next few minutes on subjects of profound importance to all of us in this room: the strategic environment in which we find ourselves today and are likely to find ourselves over the next decade; and the “hot-button items” on my plate which affect each of us in this room, the Association you represent, and most importantly, the men and women of in uniform of our Armed Forces.

Let me begin by giving you my perspective on the strategic landscape that stretches out in front of us.

In considering what I might say, my thoughts wandered back to the military and industrial leadership of a century ago. If, in 1899, just 20 years after this Association was founded, military leaders had been asked to look forward to the strategic landscape of the 20th Century, what strategic conclusions would they have drawn as the Victorian Age drew to a close and the 20th Century came into view? Would they have foreseen that in less than a single generation the greatest war in history would break out? Would they have anticipated that in less than a single short career they would see the emergence of the airplane, the tank, the subma-

rine and the wireless radio; systems that would transform forever the field of human conflict? Or would they have used the technology of their day to build a better horse, a better observation balloon, or a better bayonet?

Much of the tragedy of the First World War stemmed from the inability of the military leaders of the day to grasp the implications of change. Their failure doomed an entire generation and led directly to a second, even more destructive global war.

During the Cold War we faced a menacing, but distinct threat in the East. Then an amazing thing happened, the menace from the East collapsed. The Soviet Union and the Warsaw Pact broke up—an accomplishment that many in this room didn't think possible. All of you can take great pride in the role you played in achieving that victory. And I think there are faces of commanders of U.S. Army Europe here at the height of the Cold War who can be particularly proud.

Because of our well-deserved peace dividend—but, even as we cut deep into our force structure, questioned the relevance of our alliances, and considered reducing our forward presence—we did stay engaged. And the world is a better place for that. However, the end of the Cold War has not been the end of peril.

Today's threats are no less menacing, though the sources of danger are nowhere near as clear as the threat that was posed by the former Warsaw Pact.

Indeed, the amorphous nature of today's security environment means the threats, especially asymmetric ones, will be far more difficult to counter. It is the responsibility of each of us who wears the uniform of America's fighting forces, of our nation's leadership, and of those whom we are sworn to protect, to do everything in our country's power to see that we are ready for tomorrow. We must never allow complacency to take hold. We must ensure that future peace dividends don't bankrupt our ability to defend our great nation against emerging dangers on the near horizon.

As we look at the future, we must make the tough calls, prioritizing what is important and discarding what is not. These tough calls must strike a balance between the three enduring priorities for all the Joint Chiefs: readiness, modernization and, most importantly, people. Every decision we make in the Pentagon must be taken with an eye to its effect on these priorities.

First, readiness is really the coin of the realm for us. One thing I've learned in 30-plus years in uniform is that in a crisis we're certainly never asked: "Are you ready?" That's supposed to be a given.

We have a very busy force right now with 120,000-plus "away from home" at any given time in the



All AAFMAA members, active and retired, Army and Air Force alike, are encouraged to give the gift of membership to their colleagues.

Balkans, Sinai, Haiti, the Asia-Pacific region, Southwest Asia and many other places. We have another 100,000 forward deployed in Europe, and another 100,000 in the Western Pacific, and we have another 25,000 or so in the Middle East. These deployments serve as a tangible demonstration of our commitment to peace, stability, and the protection of American interests.



After the official business was conducted, it was time for the business of catching up with fellow members.

In Yugoslavia, for example, our forces, in full concert with our NATO allies, are working to degrade the ability of the Milosevic regime to carry out its repressive and brutal campaign of terror and ethnic cleansing against the people of Kosovo. NATO operations are not aimed at the people of Yugoslavia, but rather at the military and security forces that are being used by Milosevic against his own citizens. With diplomatic efforts exhausted and facing the greatest humanitarian catastrophe in Europe since World War II, NATO had no choice but to take the military action we warned would ensue if Milosevic persisted in his course of violence.

Let me emphasize that while we remain hopeful that Milosevic will reverse his course, until he does NATO forces will continue to reduce his capability to use violence against his own civilian population in Kosovo.

Just last Thursday, I visited the 31st Air Expeditionary Wing at Aviano, Italy, the front line of the air war against Yugoslavia. I was extremely impressed by the enthusiasm, competence, and professionalism displayed by the men and women I saw.

The aircrews are carrying out their missions with great skill—that's a very complex job. When you think about all the pieces that have to come together in that campaign, whether it is the airborne command and control center, the ABCCC, C-130; the compass call, C-130 jamming aircraft; the Navy and the Marine EA6B jamming airplanes; the F-15 air superiority aircraft; or the F-16 defense suppression airplanes. All have to be in place along with AWACS and our fighter bombers as they go into their target in bad weather, fighting their way through a very sophisticated air defense system to find the target, delivering the bomb on that target while the entire world watches on television looking for a mistake; then fighting their way back out through those defenses; and getting back home and getting back on the ground. It is a very complex endeavor and they are working with great professionalism.

At the same time, in Southwest Asia, we are continuing to pressure the Iraqi regime—despite Saddam's best efforts to the contrary and despite our commitments in the Balkans.

Now along with readiness that we are required to demonstrate on a daily basis, we have to move out with our modernization program. It is the key to our future readiness and can't be neglected.

Our best thinking about how we should fight in the 21st Century is found in Joint Vision 2010, our conceptual template for future joint operations. JV2010 truly does point the way ahead and it is designed to take full advantage of America's technological prowess.

The ultimate goal in joint war-fighting in the future is decisive operations, the ability to win quickly and overwhelmingly. Achieving a rapid decision on the battlefield and in operations-other-than-war will be the goal and the hallmark of joint operations in the next century. If we are serious about bringing joint war-fighting into the next century, then we have to go beyond conceptualizing. We have to *operationalize* our vision. We have to translate ideas into steel on target in a way that captures the best of what each service brings to the fight while eliminating the inefficiencies that can sometimes accompany inter-service operations. Operationalizing Joint Vision 2010 is one of the Chairman's key challenges and I can tell you that he is determined to get it right.

When General Shalikashvili spoke to this group almost 5 years ago to the day, he remarked on the time and expense involved in building our outstanding military. Nearly all of you in this room have had a hand in one way or another in the construction and nurturing of the Force we have today. And I know that you feel a genuine sense of proprietary anxiety about where it's going.

Let me assure you that, at the end of the day, we will field a joint force of unmatched capability and versatility.

However, to achieve our vision of American armed forces able to truly dominate the battlefield across the full range of military operations, we will need more than just technology or more efficiencies in the Department of Defense. As history has taught us over and over again, technology alone is never the answer.



The Annual Meeting provides an occasion for all AAFMAA members to discover they have more in common than just their membership.

Rather, it is the vitality of our operational concepts and doctrine, the caliber of our leaders, and the quality of our people that set us apart. They are our decisive factors! The planes, tanks, and ships we have are outstanding. In fact, thanks to our industry partners, they are the best in the world. But without quality men and women to operate ships like the USS Theodore Roosevelt, currently on station in the Adriatic; to fly aircraft like the B-2 bomber, the F-117 stealth fighter, and the

Apache attack helicopter—all engaged in missions over the Balkans; and to drive tanks like the M1A2 Abrams—the best tank in the world, bar none—they aren't worth very much.

To have a first-class military, you need first-rate people. This is the Joint Chiefs' third and most important priority.



The historic Officers Club at Ft. Myer provides an elegant setting for AAFMAA's 120th Annual Meeting.

As the Joint Chiefs told the President and Congress: keeping a quality force means assuring our men and women that they will have an adequate compensation package. That means competitive pay and an attractive retirement plan.

As everyone in this room knows, the people in uniform today do not have to serve. Today we have a recruited force. They are all volunteers, but they don't come knocking our door down to enter; they must be attracted to the opportunities that military service can provide. Serving in the armed forces has never been about money. It has always been about service to our nation. But, our men and women in uniform do want, and clearly deserve, a decent standard of living for their families.

We know that our younger troops are dissatisfied with the retirement plan they have. The REDUX retirement system that started in 1986 was a marked change from what most of us in this room are aware of the past. Instead of 50% of base pay at 20 years, service members under this system get 40% at 20 years—and they get smaller cost of living adjustments after retirement. Our retirement system—as it exists today—is a disincentive.

In James Michener's epic novel of aircraft carriers and the men who fly from them—*The Bridges at Toko-Ri*—the salty, battle-hardened, war-weary admiral asks that most poignant and famous question, "Where do we get such men?"

Now, I wasn't on that fictional bridge when that question was asked, but I'd like to answer the old Admiral anyway. I'd tell him where we get such men—and women—who serve this great country today, who give of themselves not for personal gain but for the nation's gain. They are the sons and daughters of America. To lead them is to be both awed and humbled by them.

However, ladies and gentlemen: if we don't fix our retirement system; if we don't fix our compensation system; if we don't fix our military health-care system, the question will not be where do we get such men and women; but rather, where did they all go?

The power and glory of the U.S. Armed Forces spring not from titanium, steel, cordite, and microchips, but rather from flesh, blood, guts, and gray matter.

We are on the threshold of jeopardizing one of the greatest achievements of the past quarter century, the spectacular success of the all-volunteer force.

The Secretary of Defense and the Joint Chiefs all

share these concerns and are committed to these initiatives. And, I am happy to report that the Congress and the Administration have indicated that they will support the call to improve the compensation package for military personnel.

So, let me close by saying how much I enjoyed speaking with you this afternoon and to thank you, once again, for what you have done for the cause of freedom and for what you continue to do for your Army and Air Force and our country.

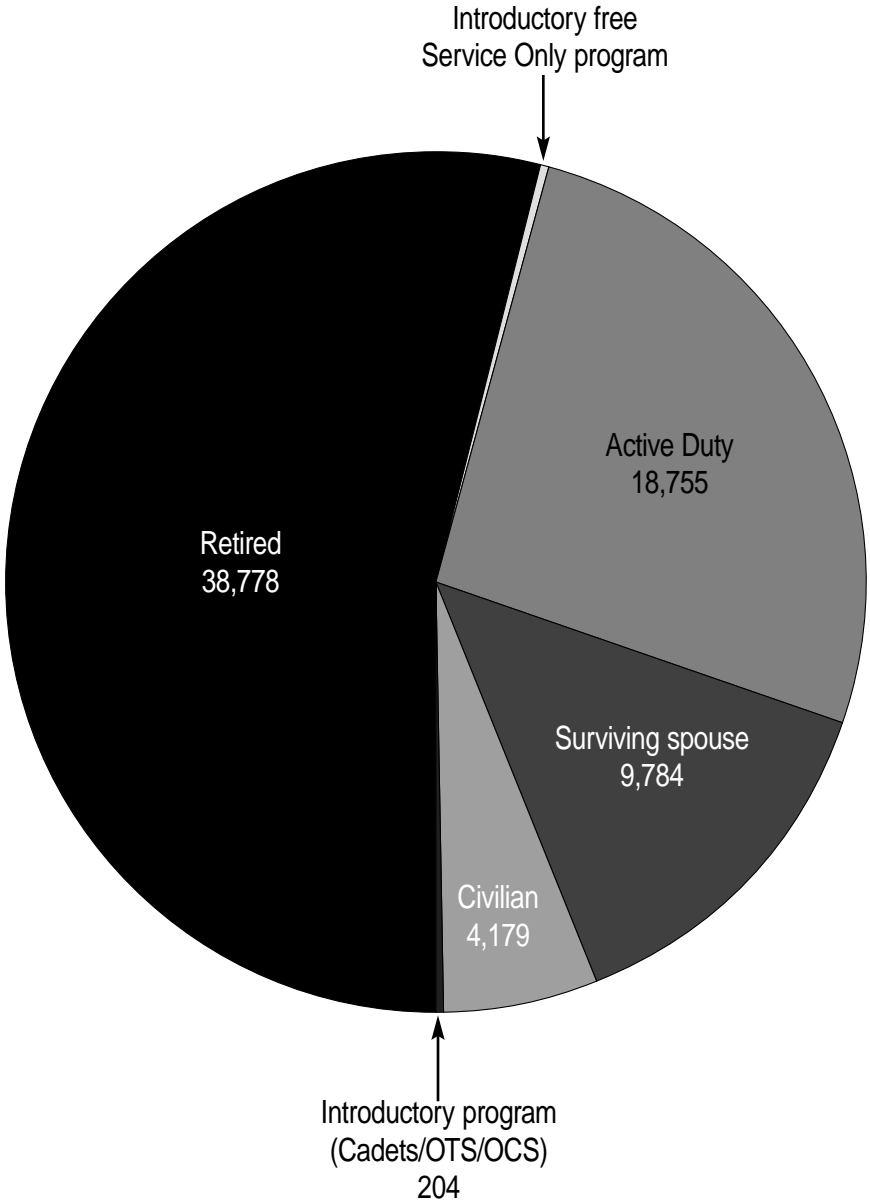
We in the military need your enduring support as we labor in the fields of freedom and democracy. May God bless each of you, and may God bless America. Thank you.

[GEN Davison thanked GEN Ralston for taking time from his busy schedule to share his views with members of our Association. The Chairman then called for new business. There being none, the meeting was adjourned at 1259 hours. A light lunch followed.]



After receiving from GEN Davison (r.) Henry Kissinger's latest book as a token of gratitude for speaking at the Annual Meeting, GEN Ralston promises to put it at the top of his reading list.

AAFMAA FAMILY PROFILE 1998



COMPARATIVE HIGHLIGHTS

	Year ended 31 December	
	1998	1997
Insurance in force <i>(in millions of dollars)</i>	\$1,677.1	\$1,491.8
Reserves <i>(in millions of dollars)</i>	\$597.6	\$550.3
Number of members	61,712	60,728
Number of member deaths	786	771
Death benefits paid <i>(in millions of dollars)</i>	\$17.7	\$17.5
Net yield on assets	7.2%	7.2%
Total portfolio return	12.6%	9.3%
Expenses <i>(as percent of income)</i>	8.9%	10.4%

Statement of the Association Actuary **A.C. Eddy, Inc., Norcross, GA**

In my opinion the reserves of the Association are necessary and sufficient to provide for liabilities to its membership and will achieve the objective of distributing the Association's assets to members and/or their beneficiaries in an equitable manner.

Arthur Crooks Eddy, F.S.A.
President

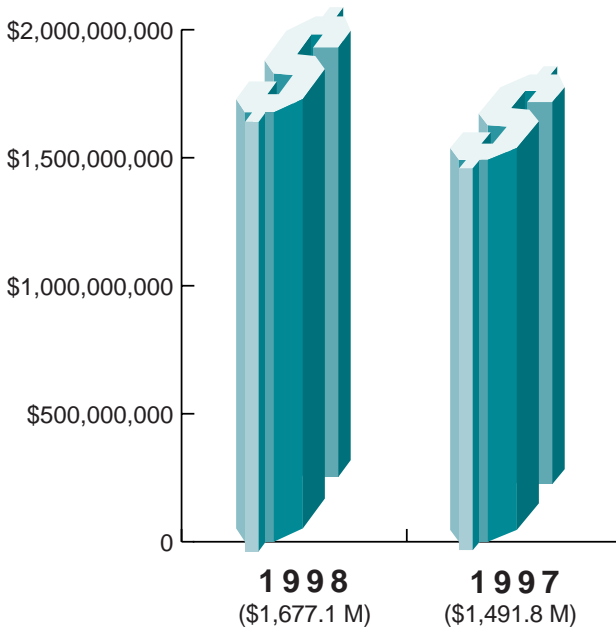
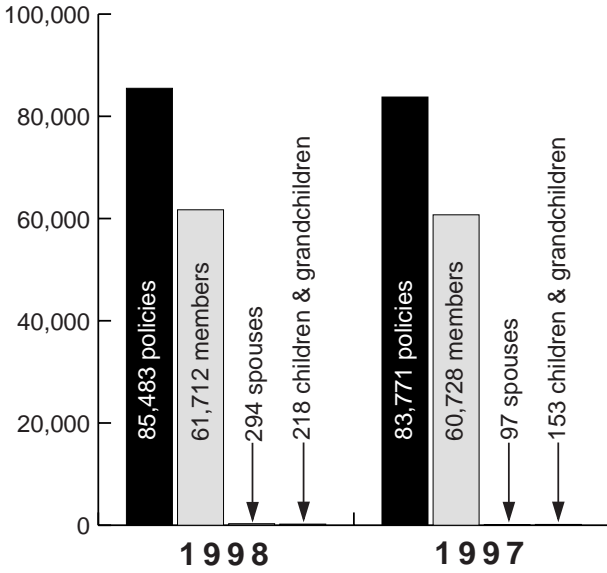
**EXPERIENCE OF THE ASSOCIATION
FROM ORGANIZATION TO 31 DECEMBER 1998**

Year ¹	Number of members	Insurance in force	Average age of insureds		Average age of decedents	Death benefits during the year	Reserves
			New lives	Plans of insurance			
1879	305	\$ 194,895	41.35	42.01			\$ 3,759
1880	593	932,196	34.81	39.09	36.72	\$ 1,478	7,523
1885	927	2,317,500	35.02	42.59	46.25	12,500	44,508
1890	1,047	3,141,000	34.88	45.49	47.74	60,000	106,852
1895	1,157	3,471,000	31.84	47.88	60.96	45,000	112,663
1900	1,346	4,038,000	27.19	47.61	54.58	72,000	147,768
1905	1,422	4,266,000	32.27	48.66	57.21	69,000	229,934
1910	1,424	4,272,000	27.08	48.32	67.55	105,000	325,282
1915	1,675	5,025,000	26.39	46.53	61.51	81,000	422,445
1920	1,558	4,974,000	29.56	47.97	66.48	106,000	438,971
1925	4,216	12,648,000	34.52	40.87	58.83	100,500	855,637
1930	6,283	25,050,000	32.79	41.06	59.43	171,000	2,238,537
1935	6,699	27,804,000	35.76	43.96	55.12	219,034	3,211,814
1940	8,465	35,725,833	29.18	44.56	57.95	327,007	5,405,070
1945	8,072	34,012,972	30.34	48.67	45.33	990,000	7,087,843
1950	14,642	69,136,898	30.96	43.03	49.84	595,940	10,803,136
1955	17,800	88,088,173	34.01	44.38	60.36	603,745	16,868,970
1960	25,411	132,550,801	35.40	44.08	63.77	901,713	27,441,332
1965	33,717	238,693,355	32.50	44.81	58.51	1,782,548	45,979,365
1970	40,601	312,365,372	31.56	43.53	57.55	2,364,964	72,022,430
1975	44,737	461,717,103	35.59	45.12	63.35	3,058,386	110,106,904
1976	45,276	473,506,835	34.02	45.64	62.73	2,866,908	121,401,040
1977	45,782	485,252,594	34.05	46.68	64.18	2,859,010	131,428,965
1978	46,393	499,209,485	35.43	46.68	63.50	2,864,102	146,137,033
1979	47,119	564,464,959	34.77	47.01	65.41	3,559,272	159,634,555
1980	47,674	575,381,813	34.59	47.56	64.72	5,084,567	171,263,311
1981	48,159	585,490,054	32.80	48.05	64.46	5,500,667	183,367,686
1982	48,618	594,077,925	34.99	48.63	63.72	5,229,212	197,140,936
1983	49,054	601,006,320	35.74	49.20	65.50	6,211,821	212,240,170
1984	49,913	611,809,705	38.00	49.75	67.14	7,152,298	234,319,981
1985	50,982	619,571,364	36.46	50.30	68.24	8,300,576	255,370,609
1986	51,874	1,131,804,661	36.78	52.10	67.30	8,997,837	275,221,126
1987	52,812	1,205,284,461	36.31	52.60	67.80	9,486,533	296,242,475
1988	54,264	1,245,697,280	36.93	53.00	70.25	10,522,430	318,188,419
1989	55,460	1,256,865,359	36.51	53.04	70.08	10,918,131	341,862,797
1990	56,887	1,273,025,936	36.00	53.90	72.25	10,619,578	366,647,028
1991	58,235	1,285,509,431	36.00	54.40	72.25	11,805,057	384,391,659
1992	58,835	1,289,521,398	37.00	55.10	72.42	12,715,129	408,656,740
1993	58,858	1,288,765,428	38.00	55.70	73.00	14,292,535	435,125,075
1994	58,988	1,290,064,691	37.00	56.30	73.75	15,316,124	439,522,508
1995	58,765	1,313,573,473	38.00	56.70	74.00	14,691,367	468,150,918
1996	59,334	1,330,951,972	30.00	56.88	74.33	16,450,126	514,631,521
1997	60,728	1,491,836,311	27.00	55.60	74.81	17,491,855	550,338,731
1998	61,712 ²	1,677,139,294 ³	31.00	54.70	75.67	17,655,618	597,610,247

Notes:

1. 1880-1975 shown in five-year increments.
2. Includes 228 free, introductory for one year; Service Only members.
3. Does not include Service Only.

INSURANCE IN FORCE



MEMBERSHIP STATEMENT

Members, 31 December 1997.....	60,728
New members gained in 1998.....	2,411
Losses:	
Members deceased.....	(786)
Non-death losses.....	(641)
Members, 31 December 1998.....	61,712*

INSURANCE STATEMENT

(includes family coverages)

Insurance certificates in force, 31 December 1997.....	83,771
New certificates issued in 1998.....	3,649
Losses:	
Certificates matured by death.....	(1,105)
Non-death certificate losses.....	(832)
Insurance certificates in force, 31 December 1998.....	85,483

INSURANCE CERTIFICATES BY FACE AMOUNT

(includes family coverages)

\$250,000.....	149
\$100,001-249,999.....	1,050
\$100,000.....	644
\$50,001-99,999.....	88
\$50,000.....	441
\$10,001-49,999.....	19,152
\$10,000.....	22,148
under \$10,000.....	41,811
Insurance certificates in force, 31 December 1998.....	85,483

*Includes 228 free, introductory for one year, Service Only members.

Life Insurance Plans

Available to You and Your Family

For **MEMBERS *and* SPOUSES:**

(Limit of \$300,000 total per person.)

★ **Whole Life Value Added** ★

*Issued through age 70;
new members issued through age 65.*

★ **Five-Year Renewable Term** ★

*Issued through age 70
new members issued through age 65.*

★ **Level Term** ★

*Nonsmokers issued through age 49
(Coverage decreases at age 50 and ends at age 60.)
Smokers issued through age 39
(Coverage decreases at age 40 and ends at age 50.)*

For **CHILDREN OF GRANDCHILDREN:**

(Limit of \$100,000 per child/grandchild.)

★ **Whole Life Value Added** ★

Issued through age 23

*For those who are **membership eligible**
and want only our services:*

★ **Service Only Membership** issued through age 85 ★

(Includes \$1,000 Accidental Death Insurance)

INDEPENDENT AUDITOR'S REPORT

VERKOUTEREN, AUERBACH & OLSON, L.L.P.

Certified Public Accountants

850 SLIGO AVENUE, SUITE 400
SILVER SPRING, MARYLAND 20910-4703

(301) 588-8672
FAX (301) 588-5262

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Army and Air Force Mutual Aid Association
Arlington, Virginia

We have audited the accompanying statutory basis statements of assets, liabilities and reserves of Army and Air Force Mutual Aid Association as of December 31, 1998, and the related statutory basis statements of income and reserves and cash flows for the year then ended. These financial statements are the responsibility of the Association's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. 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.

As described more fully in Note 1 to the financial statements, the Association prepared these financial statements using accounting practices prescribed or permitted by the National Association of Insurance Commissioners, which practices differ from generally accepted accounting principles. The effects on the financial statements of the variances between the statutory basis of accounting and generally accepted accounting principles, although not reasonably determinable, are presumed to be material.

In our opinion, because of the effects of the matter discussed in the preceding paragraph, the financial statements referred to above do not present, and are not intended to present, in conformity with generally accepted accounting principles, the financial position of Army and Air Force Mutual Aid Association as of December 31, 1998, or the results of its operations or its cash flows for the year then ended.

In our opinion, the statutory basis financial statements referred to above present fairly, in all material respects, the financial position of Army and Air Force Mutual Aid Association as of December 31, 1998, and the results of its operations and its cash flows for the year then ended, on the basis of accounting described in Note 1.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The list of securities - 31 December 1998 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.



VERKOUTEREN, AUERBACH & OLSON, L.L.P.
SILVER SPRING, MARYLAND

March 5, 1999

STATEMENT OF ASSETS, LIABILITIES AND RESERVES
STATUTORY BASIS
31 DECEMBER 1998

ASSETS

BONDS

US Government obligations	\$161,912,184
Corporate bonds	<u>220,815,721</u>

TOTAL BONDS \$382,727,905

REAL ESTATE MORTGAGES	66,799,808
REAL ESTATE INVESTMENTS	17,998,069
EQUITY SECURITIES	74,130,373
MEMBER LOANS	46,269,990
CASH AND CASH EQUIVALENTS	3,341,572
ACCRUED INVESTMENT INCOME	8,241,956
PROPERTY AND EQUIPMENT, at cost (less accumulated depreciation of \$1,415,958)	<u>556,435</u>

TOTAL ASSETS \$600,066,108

LIABILITIES AND RESERVES

LIABILITIES:

Death benefits payable	\$ 806,973
Accounts payable	530,239
Deferred revenue	1,009,449
Accrued post-retirement benefits	<u>109,200</u>

TOTAL LIABILITIES \$ 2,455,861

RESERVES:

Insurance and other	\$498,746,717
Interest maintenance	26,116,691
Asset valuation	22,972,106
General contingency	<u>49,774,733</u>

TOTAL RESERVES 597,610,247

TOTAL LIABILITIES AND RESERVES \$600,066,108

See Auditor's Report and Accompanying Notes to the statutory basis Financial Statements

STATEMENT OF INCOME AND RESERVES
STATUTORY BASIS
FOR THE YEAR ENDED 31 DECEMBER 1998

INCOME

Premiums	\$ 13,412,725	
Dues	146,474	
Consideration for annuities	8,387	
Net investment income	39,202,120	
Amortization of interest maintenance reserve	856,230	
Other income	<u>1,554</u>	\$ 53,627,490

BENEFITS AND EXPENSES

Death benefits	\$ 17,655,618	
Surrender benefits	2,357,003	
Annuity payments	54,401	
Insurance expense		
increase in aggregate reserves for life policies	12,358,976	
decrease in reserves for annuities	(43,313)	
increase in other reserves	39,778	
General administrative and operating expenses	<u>4,767,766</u>	<u>(37,190,229)</u>

**NET INCOME BEFORE EXCESS INTEREST CREDITS TO MEMBERS
AND INVESTMENT TRANSACTIONS**

16,437,261

Excess interest credited to members' policies

(10,399,249)

NET INCOME AFTER EXCESS INTEREST CREDITING

6,038,012

Net realized gain on investments

(excluding interest maintenance reserve gains)

35,122,373

NET INCOME FROM OPERATIONS

\$ 41,160,385

RESERVE TRANSACTIONS

Beginning reserve balance		\$550,338,731
less INSURANCE RESERVE, beginning:		
Life insurance and other reserves	\$(474,452,372)	
Annuity reserve	<u>(439,655)</u>	(474,892,027)
less CONTINGENCY RESERVE, beginning:		
Interest maintenance reserve	\$ (21,448,151)	
Asset valuation reserve	<u>(18,549,271)</u>	<u>(39,997,422)</u>

TOTAL GENERAL CONTINGENCY RESERVE, BEGINNING OF YEAR ..

35,449,282

Net income

\$ 41,160,385

Change in unrealized appreciation of equity securities ..

(21,312,099)

Change in voluntary insurance reserve

(1,100,000)

Change in asset valuation reserve

(4,422,835)

Net change in reserves for the year

14,325,451

GENERAL CONTINGENCY RESERVE BALANCE, END OF YEAR ...

\$ 49,774,733

See Auditor's Report and Accompanying Notes to the statutory basis Financial Statements

STATEMENT OF CASH FLOWS
STATUTORY BASIS
FOR THE YEAR ENDED 31 DECEMBER 1998

CASH FLOWS FROM OPERATING ACTIVITIES

Net income from operations		\$41,160,385
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of interest maintenance reserve . . \$	(856,230)	
Equity earnings in subsidiaries	(2,516,237)	
Depreciation	<u>212,352</u>	(3,160,115)
Changes in operating assets and liabilities:		
Decrease in accrued investment income	\$484,219	
Increase in death benefits payable	250,455	
Decrease in accounts payable	(42,120)	
Increase in deferred revenue	783,877	
Increase in accrued post-retirement benefits . .	5,239	
Net increase in life, annuities and other reserves . .	<u>22,754,690</u>	<u>24,236,360</u>

NET CASH PROVIDED BY OPERATING ACTIVITIES 62,236,630

CASH FLOWS FROM INVESTING ACTIVITIES

Member loans issued	\$(16,016,181)
Member loan repayments	15,247,386
Securities purchased	(170,505,056)
Securities sold	121,570,195
Property and equipment purchased	<u>(60,084)</u>

NET CASH USED IN INVESTING ACTIVITIES (49,763,740)

CASH FLOWS FROM FINANCING ACTIVITIES

Change in unrealized appreciation of equity securities	\$(21,312,099)
Increase in interest maintenance reserve	<u>5,524,770</u>

NET CASH USED IN FINANCING ACTIVITIES (15,787,329)

Decrease in cash and cash equivalents	(3,314,439)
Cash and cash equivalents at beginning of year	<u>6,656,011</u>

CASH AND CASH EQUIVALENTS AT END OF YEAR \$ 3,341,572

See Auditor's Report and Accompanying Notes to the statutory basis Financial Statements

NOTES TO FINANCIAL STATEMENTS
31 DECEMBER 1998

1. Significant Accounting Policies

The major accounting policies followed by the Association in the preparation of the financial statements are summarized herein. The accompanying financial statements have been prepared in conformity with statutory accounting practices. Although Army and Air Force Mutual Aid Association is not regulated by a state insurance department, these financial statements were prepared in conformity with accounting practices used by insurance companies for regulatory reporting purposes. Such accounting practices, referred to as prescribed or permitted practices, are a comprehensive basis of accounting other than generally accepted accounting principles. Because a major objective of state regulatory authorities is to protect the interests of policyholders, statutory accounting practices are oriented toward demonstrating the solvency of insurance companies and their ability to pay policyholder claims when those claims come due. Generally accepted accounting principles (GAAP) focus on a company's operating performance from period to period on a going-concern basis. Management of the Association believes statutory accounting practices more conservatively measure the Association's financial position and results of operations. The more significant categories of differences between statutory accounting practices and GAAP are summarized below:

- Valuation of investments in bonds
- Accounting for the costs of acquiring new business
- Calculation of certain reserves for policy contract benefits
- Designation of certain assets as "nonadmitted" under statutory accounting practices
- Accounting for investment in subsidiaries
- Recording of an asset valuation reserve (AVR) and an interest maintenance reserve (IMR).

Cash and Cash Equivalents

Cash includes currency on hand and demand deposits with banks or other financial institutions. Cash equivalents are short-term highly liquid investments with original maturities of three months or less.

Investments

Investments are reported according to prescribed valuation procedures. Investments in bonds are reported at amortized value. Equity mutual funds are report-

See Auditor's Report

ed at fair market value. Real estate mortgage, member and Career Assistance Program (CAP) loans are reported at unpaid principal balances, or cost. The carrying values of mortgage and CAP loans are periodically evaluated and adjusted for any perceived impairment in value.

Interest on bonds is recorded as investment income when earned and adjusted for any amortization of premium or accretion of discount. Dividends are recorded as income when earned. Interest income from mortgage and CAP loans is recorded when earned, except on loans in foreclosure or where collection is uncertain. No mortgage loans are in default. Non-performing CAP loans are 0.4% of the total CAP loans outstanding.

Realized gains and losses on sales of investment securities are included in the Statement of Income and Reserves, except as noted in Interest Maintenance Reserve section below. Unrealized gains and losses are included in the Contingency Reserves in the Statement of Assets, Liabilities and Reserves.

The lists of securities show the par, or “face value,” and market value of each security held by the Association. The mortgages held by the Association are private placements for which quoted market values are not available. For such securities, as well as member loans, cost is used as the market value.

The Association has two different types of real estate mortgage loans: those with a fixed interest rate and those with a variable interest rate. The fixed interest rate loans have the same characteristics as conventional single family mortgage loans. The variable interest rate loans have the borrower’s obligation to pay both minimum fixed interest and contingent interest. The contingent interest is a stated percentage of one or more of (i) the net cash flow from the property, (ii) excess net refinancing proceeds from the property, and/or (iii) net appreciation on the disposition of the property.

The Association has one wholly-owned subsidiary corporation, which is the managing partner in a limited partnership for which the Association owns, directly or indirectly, all of the limited partnership interests. The limited partnership (and associated managing corporation) continues to hold real estate properties with a total estimated market value of \$23,300,000. The investments in these wholly-owned subsidiaries are accounted for using the equity method.

Property and Depreciation

Property and equipment are capitalized as purchased and depreciated on a straight line basis over their useful life, ranging from three to fifty years. Under

See Auditor’s Report

statutory accounting practices, the depreciated cost of furniture, equipment and applications software are considered to be “non-admitted assets,” i.e. assets accorded no values because they do not conform to the laws and regulations of the various states. Since the Association is not regulated by any state due to its special exempt status, management has chosen not to reflect these categories of property and equipment as non-admitted assets. The Association holds \$61,101 of net assets categorized in Property and Equipment on the statement of Assets, Liabilities and Reserves which would otherwise be reported as non-admitted.

Use of Estimates

The process of preparing financial statements requires the use of estimates and assumptions regarding certain types of assets, liabilities, revenues and expenses. Such estimates primarily relate to unsettled transactions and events as of the date of the financial statements. Accordingly, upon settlement, actual results may differ from estimated amounts.

Actuarial Reserves

Actuarial reserves for all plans are equal to the sum of the individual benefit plan accumulation values but not less than the minimum cash value for each certificate. The Association holds additional reserves at 31 December 1998 such that the sum of accumulation values and the additional reserves are equal to or greater than minimum reserves for such certificates as prescribed by the National Association of Insurance Commissioners for regulated insurers.

Excess interest credits, as reflected in the statement of income and reserves, equal the amount credited to cash value accounts in excess of statutory minimums.

Income Taxes

The Association is a tax-exempt, non-profit association as described in section 501(c)(23) of the Internal Revenue Code.

2. Nature of Business

The Association, a 120-year-old non-profit service organization with over 61,000 members, is dedicated to aiding its members and the families of deceased members in a prompt, simple and substantial manner. Members consist of active, reserve and retired officers, warrant officers and non-commissioned officers of the United States Army and United States Air Force, as well as cadets serving at the United States Military and United States Air Force Academies, and those with ROTC scholarships and contracts. The spouses, children and grandchildren of members may also be insured by the Association beginning in 1997. Services provided by the Association to its members and the survivors of deceased mem-

See Auditor's Report

bers include: a financial awareness program, income protection counseling, insurance counseling and assistance in applying for entitlement benefits. The Association provides interest-sensitive and term life insurance protection.

3. Retirement Plan

The Association implemented a 401(k) and profit-sharing plan on 1 January 1997, which covers all employees who meet certain minimum eligibility requirements. The Association may contribute as a matching contribution up to 3% of employee elective deferrals. In addition, it may contribute an amount equal to 3% of compensation. The total retirement plan expense for the year ended 31 December 1998 was \$307,900, which includes \$183,532 of employees' elective deferrals.

4. Post-Retirement Benefits

The Association sponsors a post-retirement health care plan and a post-retirement life insurance plan for its retirees. The post-retirement health care plan is contributory, with retiree contributions of 60%; the life insurance plan is non-contributory. The post-retirement expense for the year ended 31 December 1998 was approximately \$34,000.

5. Reinsurance

Reinsurance is provided for catastrophes defined as an accident, including a war risk, arising out of one event or occurrence resulting in the death of three or more insureds. This agreement is subject to a deductible of \$312,500, with a maximum reimbursement of \$250,000 per insured and \$3,750,000 in the aggregate. Such reimbursement does not discharge the primary liability of the Association as direct insurer of the risks insured. The Association evaluates the financial strength of potential reinsurers and continually monitors the financial condition of the reinsurer. The reinsurance agreement became effective 1 July 1997. For the year ended 31 December 1998, the Association incurred premiums of \$46,148 for reinsurance.

6. Commitments

The Association has entered into various non-cancelable contracts for equipment rentals, maintenance, and data processing. The obligations for 1999 under these contracts total \$648,300, some of which are subject to CPI increases. The Association has also committed approximately \$6,200,000 for commercial real estate mortgage loans to be distributed during 1999.

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7. Land and Office Lease

In December 1998, the Association entered into a 30-year lease with the Department of the Army to lease the land upon which the Association's building rests. The annual lease payment is \$11,700, with an evaluation of the fair market rental value to be performed every five years.

The Association is obligated under a lease for office space at the Pentagon. The annual lease obligation is \$27,000, and the lease term runs through 30 September 2002.

8. Concentration of Risk

The Association has its insurance administration database supplied by a national computer services firm. The Association's account is served by a single individual at the computer firm, whose specialization has provided significant benefit. However, there is exposure to a technical void, work delays or backlog should this individual become unavailable to serve the Association's account due to death, retirement or cessation of employment.

9. Year 2000

The Association is in the process of reviewing and modifying its information systems to ensure that its information technology will recognize the year 2000. The cost of the project is not expected to have a significant effect on the Association's results of operations or financial position.

See Auditor's Report

SUPPLEMENTARY INFORMATION
LIST OF SECURITIES—31 DECEMBER 1998

Face Value	U.S. Government Obligations (27.0% of Assets)	Rate of Interest	Maturity	Amortized Value	Market Value
\$ 20,847	Farmers Home Administration	5.75%	2001	\$ 20,847	\$ 20,847
7,253,815	Federal Housing Administration	7.43%	2025	6,469,083	7,471,429
7,320,000	Federal National Mortgage Assn.	7.50%	2010	7,334,223	7,754,588
8,722,775	Federal National Mortgage Assn.	7.50%	2023	8,712,592	9,273,357
9,764,398	Federal National Mortgage Assn.	6.50%	2026	9,110,580	9,827,769
74,000,000	U.S. Treasury Bonds Zero Coupon		2010	32,378,357	41,237,280
88,350,000	U.S. Treasury Bonds Zero Coupon		2018	25,117,957	30,232,799
55,500,000	U.S. Treasury Bonds Zero Coupon		2019	13,712,276	18,020,930
20,900,000	U.S. Treasury Bonds Zero Coupon		2020	5,785,555	6,396,654
68,600,000	U.S. Treasury Bonds Zero Coupon		2021	19,076,834	19,928,300
6,750,000	U.S. Treasury Bonds	7.88%	2021	6,510,046	8,882,528
8,000,000	U.S. Treasury Bonds	8.00%	2021	8,611,281	10,703,280
10,000,000	U.S. Treasury Bonds	7.25%	2022	9,640,597	12,450,900
<u>9,500,000</u>	U.S. Treasury Bonds	6.25%	2023	<u>9,431,956</u>	<u>10,617,675</u>
<u>\$374,681,835</u>	TOTAL			<u>\$161,912,184</u>	<u>\$192,818,336</u>

Face Value	Corporate Bonds (36.8% of Assets)	Rate of Interest	Maturity	Amortized Value	Market Value
\$ 10,000,000	Atlantic Richfield Co.	8.50%	2012	\$ 11,241,144	\$ 12,255,400
10,000,000	Banc 1 Corp.	7.75%	2025	10,146,624	11,515,700
8,000,000	Caterpillar Tractor Co.	9.38%	2021	8,410,585	10,812,240
8,500,000	Coca-Cola Enterprises, Inc.	8.00%	2022	8,746,112	10,159,285
10,000,000	Cox Communications, Inc.	6.88%	2005	10,182,983	10,578,000
6,000,000	Deere & Co.	8.50%	2022	5,976,383	7,390,080
10,000,000	Equistar Chemicals LP	6.50%	2006	9,774,295	9,321,500
8,000,000	Ford Motor Co.	9.98%	2047	8,815,399	11,817,920
8,000,000	General Motors Acceptance Corp.	9.40%	2021	8,546,787	10,678,880
8,000,000	ITT Corp.	6.75%	2005	8,101,768	7,295,712
10,000,000	Lockheed Corp.	9.00%	2022	10,388,334	12,836,800
10,000,000	Mead Corp.	7.35%	2017	10,073,957	10,525,500
905,990	Merrill Lynch Mortgage Investments, Inc.	9.00%	2011	901,540	917,315
10,000,000	Mobil Corp.	7.62%	2033	9,898,091	10,684,600
5,000,000	New England Telephone & Telegraph	7.88%	2029	4,982,638	6,034,450
545,826	Old Stone Home Equity Trust	6.15%	2007	536,488	552,851
281,925	Old Stone Home Equity Trust	6.30%	2007	277,429	285,187
10,000,000	Pacific Bell Telephone & Telegraph	7.12%	2026	10,211,563	11,222,900
10,000,000	Penney, J. C., Inc.	7.62%	2097	9,804,012	10,604,300
5,000,000	Petro-Canada	8.25%	2016	5,010,311	5,692,700
9,000,000	Seagram Limited	6.88%	2023	9,000,000	8,286,750
1,323,374	Security Pacific Acceptance Corp.	8.55%	2011	1,318,692	1,317,168
7,550,000	ShawmutBank, Conn., NA	8.62%	2005	7,835,718	8,594,618
10,000,000	Swiss Bank Corp.	7.75%	2026	9,922,492	11,123,300
10,000,000	TCI Communications, Inc.	8.00%	2005	10,440,395	11,290,600
8,000,000	Texaco Capital, Inc.	8.88%	2021	8,072,693	10,363,280
10,000,000	United Technologies Corp.	8.88%	2019	11,712,570	13,265,800
<u>10,500,000</u>	Worldcom, Inc.	6.95%	2028	<u>10,486,718</u>	<u>11,277,630</u>
<u>\$214,607,115</u>	TOTAL			<u>\$220,815,721</u>	<u>\$246,700,466</u>

See Auditor's Report and Accompanying Notes to the statutory basis Financial Statements

SUPPLEMENTARY INFORMATION
LIST OF SECURITIES—31 DECEMBER 1998

Principal Amount	Real Estate Mortgages (11.1% of Assets)	Rate of Interest	Maturity	Amortized Value	Market Value
\$ 2,896,335	Arlington Forest Shopping Center Arlington, Virginia	7.50%	2013	\$ 2,896,335	\$ 2,896,335
2,284,198	Bethany Investments, L.L.C. Loudoun, Virginia	7.57%	2013	2,284,198	2,284,198
4,400,000	13890 Braddock Road LP Centreville, Virginia	6.95%	2008	4,400,000	4,400,000
2,806,791	Coleman Cadillac Dealership Bethesda, Maryland	10.25%	2009	2,806,791	2,806,791
2,250,000	Colesville Road Office Building Silver Spring, Maryland	10.00%	2000	2,250,000	2,250,000
2,777,234	Dominion Hills Centre L.L.C. Arlington, Virginia	7.50%	2013	2,777,234	2,777,234
3,180,297	Fairfax Professional Center LP Merrifield, Virginia	7.09%	2008	3,180,297	3,180,297
2,630,334	Falls Center Townhouse Offices Potomac, Maryland	7.75%	2000	2,630,334	2,630,334
2,444,759	Firstfield Shopping Center Gaithersburg, Maryland	7.50%	2005	2,444,759	2,444,759
1,600,000	Firstfield Office Building Gaithersburg, Maryland	14.00%	2001	1,600,000	1,600,000
5,476,464	J & A Warehouses Prince Georges County, Maryland	8.16%	2000	5,476,464	5,476,464
5,000,000	Jemal's World* Washington, D.C.	10.00%	2000	5,000,000	5,000,000
1,904,825	PGI Westfields Associates L.L.C. Atlanta, Georgia	6.70%	2001	1,904,825	1,904,825
2,527,595	Prince William Plaza II Woodbridge, Virginia	7.00%	1999	2,527,595	2,527,595
79,840	Randall H. Hagner & Co., Inc. Residential Mortgages	various	various	79,840	79,840
7,067,575	Randolph Buildings Rockville, Maryland	8.75%	2002	7,067,575	7,067,575
4,081,436	Reston Mini Warehouse Reston, Virginia	9.25%	2006	4,081,436	4,081,436
1,789,000	Reston Investments L.L.C. Reston, Virginia	7.57%	2014	1,789,000	1,789,000
1,688,320	Solus L.L.C. Reston, Virginia	7.57%	2013	1,688,320	1,688,320
1,538,534	Sterling Park Shopping Mall Loudoun, Virginia	7.38%	2008	1,538,534	1,538,534
	Westfields 14 L.L.C. Fairfax, Virginia				
1,647,500	Acquisition Loan	10.00%	2003	1,647,500	1,647,500
259,501	Development Loan Westfields 17 L.L.C. Fairfax, Virginia	7.00%	2003	259,501	259,501
5,300,000	Acquisition Loan	6.95%	2003	5,300,000	5,300,000
<u>1,169,270</u>	Development Loan	10.00%	2003	<u>1,169,270</u>	<u>1,169,270</u>
<u>\$66,799,808</u>	TOTAL			<u>\$66,799,808</u>	<u>\$66,799,808</u>

*These real estate mortgage loans also have a contingent interest in addition to the stated interest rate.

See Auditor's Report and Accompanying Notes to the statutory basis Financial Statements

SUPPLEMENTARY INFORMATION
LIST OF SECURITIES—31 DECEMBER 1998

Cost	Real Estate Investments (3.0% of Assets)	Amortized Value	Market Value
\$ 162,136	Consolidated Realty, Inc.	\$ 162,136	\$ 162,136
<u>17,835,933</u>	Consolidated Realty Limited Partnership	<u>17,835,933</u>	<u>23,300,000</u>
<u>\$ 17,998,069</u>	TOTAL	<u>\$17,998,069</u>	<u>\$23,462,136</u>

Number of Shares	Equity securities (12.4% of Assets)	Cost	Market Value
475,429	Banker's Trust International Fund	\$ 6,044,847	\$ 6,589,439
2,727,762	Northern Trust Class A Equity Index Fund	60,736,065	61,343,951
<u>317,957</u>	Scudder Kemper Small Cap Value Fund	<u>6,056,693</u>	<u>6,196,983</u>
<u>3,521,148</u>	TOTAL	<u>\$72,837,605</u>	<u>\$74,130,373</u>

Face Value	Cash and Cash Equivalents (12.4% of Assets)	Rate of Interest	Maturity	Amortized Value	Market Value
\$1,266,884	Cash in Banks			\$ 1,266,884	\$ 1,266,884
2,072,874	Scudder Kemper	5.11%	1998	2,072,874	2,072,874
<u>1,814</u>	The Northern Trust Company	5.11%	1998	<u>1,814</u>	<u>1,814</u>
<u>\$3,341,572</u>	TOTAL			<u>\$ 3,341,572</u>	<u>\$ 3,341,572</u>

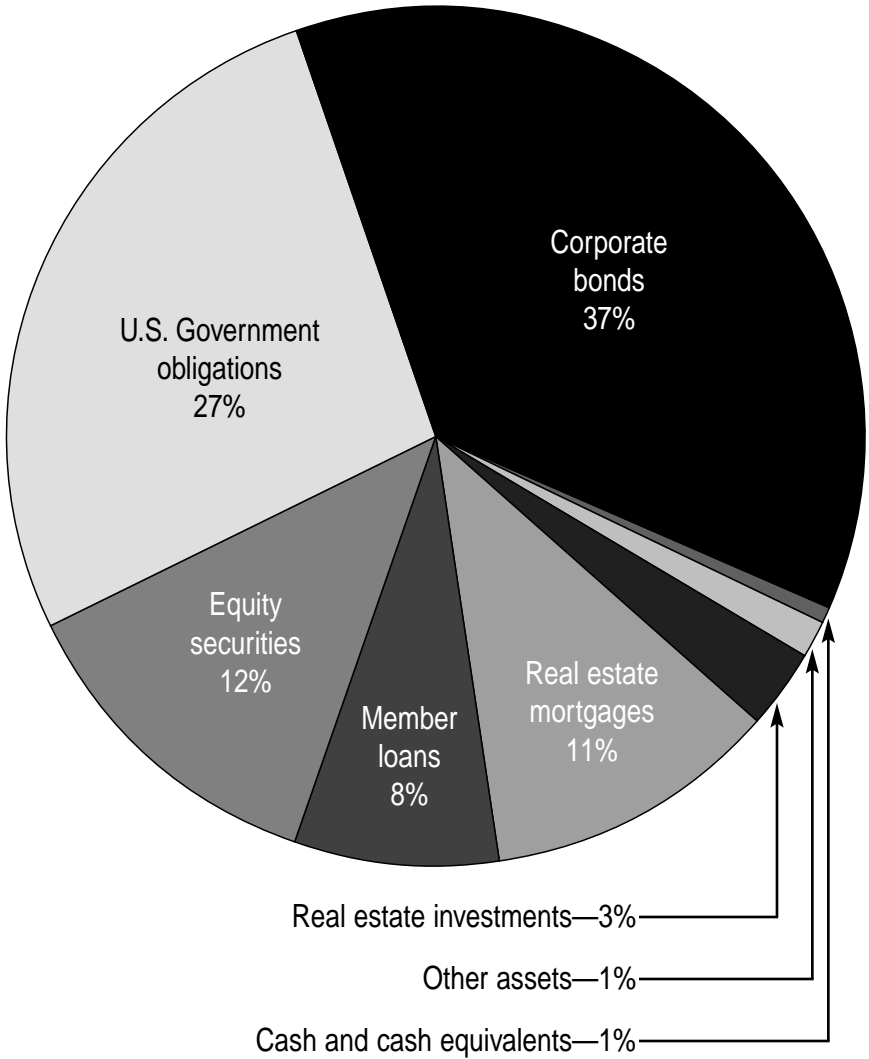
SUMMARY

Securities	Amortized Value	Market Value
U.S. Government Obligations	\$161,912,184	\$192,818,336
Corporate Bonds	220,815,721	246,700,466
Real Estate Mortgages	66,799,808	66,799,808
Real Estate Investments	17,998,069	23,462,136
Equity Securities	74,130,373*	74,130,373
Cash and Cash Equivalents	3,341,572	3,341,572
Accrued Investment Income	<u>8,241,956</u>	<u>8,241,956</u>
TOTAL SECURITIES	553,239,683	615,494,647
Member Loans	46,269,990	46,269,990
Property & Equipment		
Net of Accumulated Depreciation	<u>556,435</u>	<u>556,435</u>
TOTAL ASSETS	<u>\$600,066,108</u>	<u>\$662,321,072</u>

*Equity securities are valued at market.

See Auditor's Report and Accompanying Notes to the statutory basis Financial Statements

1998 Assets



Total assets: **\$600 million**
Net yield on assets: **7.2%**
Total portfolio return: **12.6%**



GUEST SPEAKER

General Joseph W. Ralston, USAF, Vice Chairman, Joint Chiefs of Staff

General Joseph W. Ralston is the Vice Chairman of the Joint Chiefs of Staff, The Pentagon, Washington, DC. In this capacity, he is a member of the Joint Chiefs of Staff and the nation's second-highest-ranking military officer. As the Vice Chairman, General Ralston serves as the Chairman of the Joint Requirements Oversight Council; Vice Chairman of the Defense Acquisition Board; and as a member of the National Security Council Deputies Committee and the Nuclear Weapons Council. In addition, he acts for the Chairman in all aspects of the planning, programming and budgeting system to include participating in meetings of the Defense Resources Board.

General Ralston entered the Air Force in 1965 through the Reserve Officer Training Corps program. His career includes operational command at squadron, wing, numbered Air Force and major command, as well as a variety of influential staff and management positions at every level of the Air Force. He has been closely involved with building the U.S. Air Force of the 21st Century, holding a variety of positions related to the requirements and acquisition process. Prior to assuming his current position, he was commander of Air Combat Command with headquarters at Langley Air Force Base, VA. He is a command pilot with more than 2,500 flying hours, including 147 combat missions over Laos and North Vietnam.

General Ralston and his wife, Dede, have four children: Christopher, Paige, David and Sarah.

History

Before 1879, it was almost impossible for the U.S. Army Officer to provide immediate financial assistance to his family in the event of his death. The suffering of the destitute families of those who lost their lives in the frontier wars emphasized this situation and led to the founding of this nonprofit, mutual benefit life insurance association. Its active supporters and officers have ranged from Generals Philip H. Sheridan, Abner N. Doubleday and John J. Pershing to Generals George C. Marshall, Dwight D. Eisenhower, Henry H. (Hap) Arnold, Carl A. (Tooe) Spaatz, Omar N. Bradley, Maxwell D. Taylor, Lyman L. Lemnitzer, George H. Decker, Harold K. Johnson, William C. Westmoreland, Creighton W. Abrams, Fred C. Weyand, Bernard W. Rogers, Edward C. Meyer, John A. Wickham, Jr., H. Norman Schwarzkopf, and Ronald R. Fogleman.

For more than 120 years, the Association has offered its members permanent life insurance at a minimum cost and has provided immediate cash to the bereaved families of its members. It has withstood the losses of the military campaigns and weathered the financial crises of those years. Today the Association is even more sound and secure and also offers term insurance.

The Association prepares the government and insurance claims for the bereaved parents, spouses and children of its members. This outstanding service, by trained and experienced personnel, assures the members' families that they will be fully informed concerning rights to all government allowances, both now and in the future.

With no paid agents, Army and Air Force Mutual Aid Association must rely on its members for support and assistance in bringing the benefits of membership to the attention of those eligible for membership. Quite properly, its strongest supporters are the survivors it has helped and those members who have had the opportunity to observe the Association's effective assistance on such occasions.

Every eligible U.S. Army and Air Force Officer, Warrant Officer and Noncommissioned Officer should become a member of AAFMAA, the only completely mutual benefit association offering its membership to these services. Every member is urged to utilize the many services the Association offers, to inform their families of the assistance the Association provides in time of emergency, and to recommend membership to others eligible for membership.