



# Army and Air Force Mutual Aid Association

## 122<sup>nd</sup> Annual Report

(for the year ended 31 December 2000)



*Insurance from a name you can trust... AAFMAA*

STABILITY • REPUTATION • LOW COST • SINCE 1879

# 2000

# AAFMAA Mission

To be the premier provider of insurance  
and survivor services to the Army and  
Air Force communities.

## Board of Directors

(as of 31 December 2000)

GEN Robert W. Sennewald, USA, Ret.

*Chairman*

LTG Donald M. Babers, USA, Ret

*Vice Chairman*

MAJ William D. Clark, USA, Ret.

LTG John A. Dubia, USA, Ret.

COL Wayne T. Fujito, USA, Ret.

SMA Robert E. Hall, USA, Ret.

COL Richard S. Hassan, USAF\*

LGen Bradley C. Hosmer, USAF, Ret.\*\*\*

MAJ Walter R. Lincoln, USA, Ret.

GEN Jack N. Merritt, USA, Ret.

BG L. Donne Olvey, USA, Ret.

MGen Susan L. Pamerleau, USAF, Ret.\*\*

CMSAF Sam E. Parish, USAF, Ret.

MAJ Joe R. Reeder, USAR

### Chairmen Emeriti

GEN Walter T. Kerwin, USA, Ret.

GEN Michael S. Davison, USA, Ret.

### Directors Emeriti

GEN John R. Guthrie, USA, Ret.

BG Elizabeth P. Hoisington, USA, Ret.

## Association Officers

MAJ Walter R. Lincoln, USA, Ret., CFP

*President and Treasurer*

LTC Tom E. Hargis, USA, Ret.

*Secretary*

Capt Cristiano A. Marchiori, USAFR, CFP

*Assistant Treasurer*

*\*On active duty as of 31 December 2000. All others are retired or separated from active service. All directors serve without compensation.*

*\*\* Resigned effective 15 January 2001.*

*\*\*\*Resigned effective 1 March 2001.*

## From the Chairman

I am honored to serve as your Chairman of the Board. Taking over from General Mike Davison proved an easy transition. His leadership and development of a Strategic Plan provided a road map to the future. Last year's "future" is now history; I'm happy to report that the year 2000 was a great success. AAFMAA set records in all indicators: Number of Members, Number of Policies, Insurance in Force, and Assets.

Let me cover four broad aspects of your Association which will help us continue to set even more records as we fulfill the needs of our members.

Our focus is always directed towards providing low-cost insurance and exceptional services. For over 122 years, the Association has assisted survivors of deceased members when they have needed it the most. All our efforts are focused on delivering great insurance and great services.

AAFMAA will continue to expand insurance products as demanded by the members and warranted by economics. If AAFMAA can do it better than anyone else, we'll do it. If we can't, we'll direct members to those who can do it best. Our goal is to get the best deal for the men, women, and families of the Army and Air Force Communities. Part of meeting our mission of being the premier provider of insurance to the Army and Air Force communities requires us to control costs and maintain stringent underwriting standards. This allows us to offer low premiums on term insurance and high crediting rates on whole life insurance. We anticipate continuing to reduce our administrative costs per member, thereby continuing to deliver the best value on life insurance for all members.

In our continuing effort to represent the members with an absolutely first rate Board of Directors, in 2000 the Executive Committee appointed COL Richard S. Hassan, USAF, SMA Robert E. Hall, USA, Ret., and GEN Jack N. Merritt, USA, Ret. to the Board. These directors, plus those nominated by the Nominating Committee, are on this year's enclosed ballot. The directors serve the Association on a *pro bono* basis. We



expect a lot of your directors, and they deliver to ensure that every Board decision is made with the members' best interests in mind.

Effective 1 July 2000, member services previously provided by AAFMAA are accomplished by the Armed Forces Services Corporation (AFSC) under contract to AAFMAA. AFSC was formed by employees of AAFMAA's Member Services Department. The transition from in-house operations to AFSC has proceeded incredibly well. AFSC continues to deliver the same outstanding services AAFMAA members and their survivors have always enjoyed.

The members of this Association have served or are now serving our country at great personal risk. Every member can rely upon AAFMAA to serve them in *their* time of need. On behalf of the entire Board of Directors, I thank you for the opportunity to lead the Association as the first Chairman of the 21<sup>st</sup> Century.

Yours very truly,

A handwritten signature in dark ink, reading "Robert W. Sennewald". The signature is fluid and cursive, with the first name and last name clearly legible.

**Robert W. Sennewald**  
*General, USA, Retired*

**Message to the Army and Air Force  
Mutual Aid Association**

**April 6, 2001**

Congratulations on 122 years of dedicated service to our soldiers and airmen. On behalf of The Army's soldiers and their family members "On point for our Nation around the world," I would like to extend my heartfelt congratulations and sincere appreciation to a great organization and its members on this noteworthy occasion.

Thank you for the important role and services that your organization provides in the lives of our soldiers and their families. Your exemplary record of public service and determination to improving the lives of those less fortunate, shines like a beacon beckoning others to follow suit. Your organization clearly represents the best that our great Nation has to offer.

Best wishes for continued success.

Sincerely,



**Eric K. Shinseki**  
General, United States Army

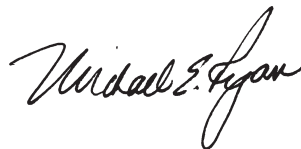
## Message to the Army and Air Force Mutual Aid Association

April 4, 2001

For 122 years, the Army and Air Force Mutual Aid Association has stood with our airmen and soldiers in their times of personal need. Today, more than ever, our military families need the support your organization provides.

Our operations take military members to every corner of the globe to participate in combat, exercises, humanitarian relief operations and more. Your services provide our men and women and their families an important sense of security and peace of mind during difficult times. The positive impact of your work is retold one life and one family at a time—the Association does make a difference!

Thank you for all your support to our Armed Forces and best wishes for your continued success.



**MICHAEL E. RYAN**  
General, USAF

# Report of the President and Treasurer



As General Sennewald illustrated, we are focused on doing our very best for the AAFMAA members. The year 2000 has been a challenging year to achieve record results, but it was done. My report covers membership, insurance in force, insurance policies, lives insured, investments, financial results, and the crediting rate.

**Membership.** The number of Association members grew by 2.3%, a substantial increase over previous trends. This indicates that your Association is continuing to evolve and become increasingly important to the soldiers and airmen of the Army and Air Force.

**Insurance in Force.** Our insurance in force grew from \$1.91B in 1999 to \$2.45B in 2000. This is a net increase of \$540M, the best result in Association history and over twice the growth of 1999. Two significant factors contributed to this growth. The Association asset base allowed the maximum initial insurance limits to be raised to \$500,000 per insured life. Also, the introduction of our Level Term II policy has received a positive response. The limit for children and grandchildren remains unchanged.

**Insurance Policies.** Insurance policies, on a net basis, grew from 85,349 to 87,257, or 2.2%. More members are using AAFMAA to insure their entire family. The opportunity to insure spouses, children and grandchildren has contributed to the growth in the number of policies.

**Lives Insured.** The membership grew by 1,410. In addition, spouses, children and grandchildren grew by 334. The growth in membership and the growth in other family members resulted in a total of 63,777 lives insured. This healthy expansion of 2.8% indicates that our competitive products address the needs of a broader market.

**Investments.** The \$2.45B insurance in force constitutes our liabilities. Our investments are the assets that enable us to meet those liabilities. Investments grew from \$643M in 1999 to \$662M in 2000. This \$19M growth was achieved in a year when the stock markets were not particularly kind. These assets plus our future premium income and future investment earnings will meet our \$2.45B of future liabilities. The \$662M of investments are allocated as reflected in the Summary of Assets.

**Financial Results.** As mentioned above, year 2000 included substantial market turbulence. In spite of that, results for 2000 were very positive. The Contingency Reserve increased 5.5%. An increase in the Contingency Reserve further protects against future unexpected events and allows the

Association to grow with greater safety for current members.

Net Income rose to \$21.0M from \$10.5M. While net income doubled, along with the growth in insurance in force, policies, and members, General Administrative and Operating Expenses declined as a percentage of revenue from 10.0% to 8.8%. This illustrates the care with which we treat your money. Continuing to control costs is imperative in achieving our goal of being the absolutely lowest cost provider of insurance.

Our Net Yield on Assets for 2000 was 6.6%. The Net Yield calculation does not include capital appreciation, on a market value basis. Including capital appreciation, the Total Return for 2000 was 10.6% versus 9.2% for 1999.

Consolidated Realty, LLC, the Association's real estate equity investment arm, contributed to this outstanding financial result. The Net Rental Income totaled \$1,483,429. The properties within Consolidated Realty had an 85% occupancy rate. Additional information on Consolidated Realty, LLC is included later in the Annual Report.

**Crediting Rate.** These very favorable financial results have enabled the Board of Directors to maintain our crediting rate of 8.25% on whole life policies for the year 2000. The crediting rate determines the amount of interest that is added to policy cash values each month. As these cash values grow to sufficient levels, the insurance coverage grows. This 8.25% crediting rate continues to be very competitive. Crediting rates will vary and the 8.25% current crediting rate is NOT guaranteed for the future.

**In summary,** our Association had a record year and is more financially sound than ever before. The Board of Directors have provided a road map for success; the officers of the Association have led the day to day operations with efficiency and focus; but, most importantly, the staff of your Association has provided every member great service and great results. As President and Treasurer, I am honored to report to the membership on their successful efforts.



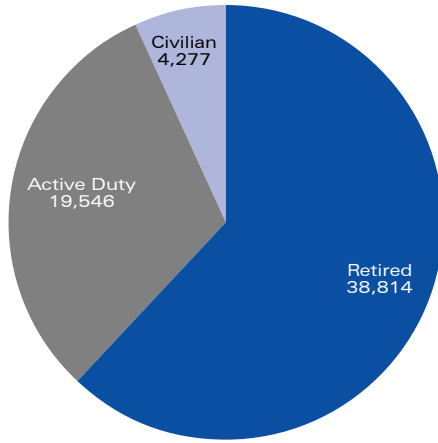
*Walter R. Lincoln*

Walter R. Lincoln, CFP

President and Treasurer

# AAFMAA Overview 2000

## Member Profile



Surviving Spouses: 10,057

## Comparative Highlights

	Year ended 31 December	
	2000	1999
Insurance in Force (\$ millions)	\$2,450.1	\$1,909.3
Total Reserves (\$ millions)	\$658.1	\$639.5
Number of members	62,637	61,227
Number of member deaths	772	782
Death benefits paid (\$ millions)	\$18.4	\$17.7
Net Yield on Assets	6.6%	6.6%
Total Portfolio Return	10.6%	9.2%
Expenses (% of gross revenue)	8.8%	10.0%

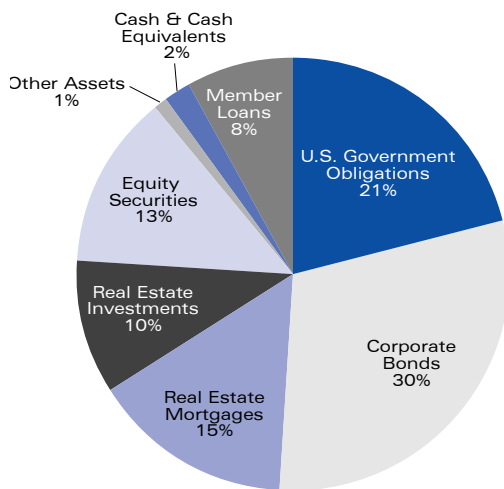
(This and all other presentations exclude Free Service Only (FSO) Memberships.)

## 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

## 2000 Assets



Total Assets: \$662 Million

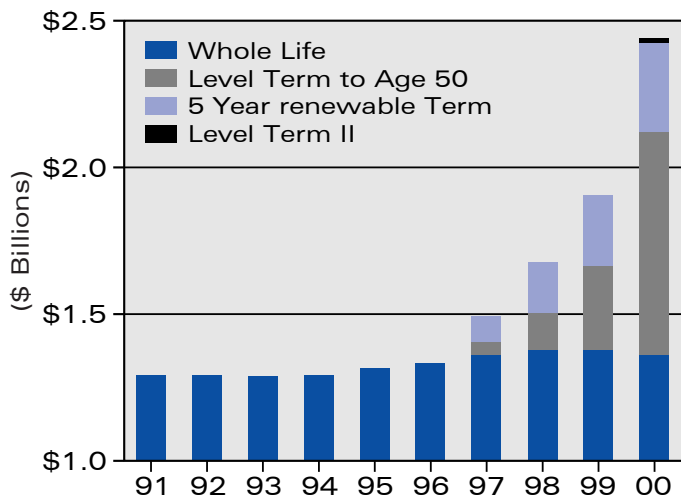
## Summary of Assets

Securities	Amortized Value	Market Value
U.S. Government Obligations	\$137,956,707	\$160,200,104
Corporate Bonds	200,323,725	192,064,297
Real Estate Mortgages	99,903,995	99,903,995
Real Estate Investments	63,993,458	73,775,000
Equity Securities	83,321,433*	83,321,433
Cash and Cash Equivalents	15,131,993	15,131,993
Accrued Investment Income	7,629,527	7,629,527
<b>Total Securities</b>	<b>608,260,838</b>	<b>632,026,349</b>
Member Loans	52,729,781	52,729,781
Related Party Receivable	94,035	94,035
Property & Equipment		
Net of Accumulated Depreciation	950,046	950,046
<b>Total Assets</b>	<b>\$662,034,700</b>	<b>\$685,800,211</b>

\*Equity Securities are valued at market.

## Insurance in Force Statement

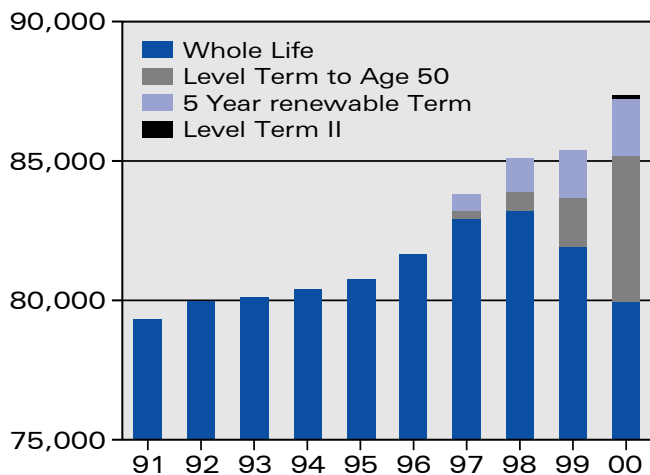
(includes family coverages)



Insurance in force, beginning of year . . . . .	\$1,909,284,032
New insurance sold in 2000 . . . . .	\$ 595,410,545
Cash value growth . . . . .	\$ .23,738,891
Death benefits paid . . . . .	\$ (18,417,309)
Other terminations . . . . .	\$ (59,873,285)
Insurance in force, end of year . . . . .	\$2,450,142,874

## Insurance Policy Statement

(includes family coverages)

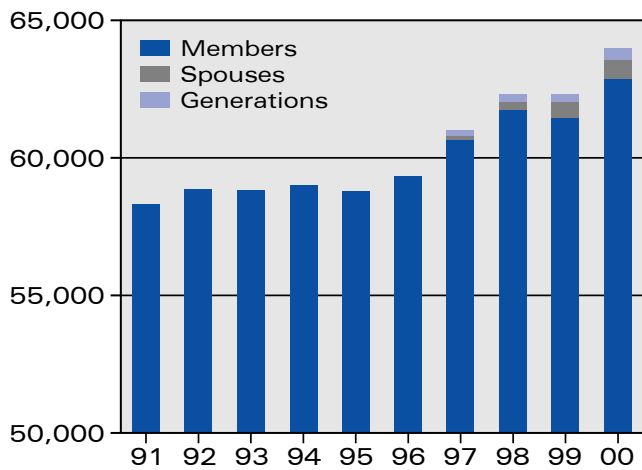


Insurance policies in force,	
beginning of year . . . . .	85,349
New policies issued . . . . .	5,247
Policies matured by death . . . . .	(1,083)
Other policy terminations . . . . .	(2,256)
Insurance policies in force,	
end of year . . . . .	87,257



# Members and Lives Statement

(includes family coverages)



Members, beginning of year	.61,227
Gains	.4,065
Losses	.(2,655)
Members, end of year	.62,637
Spouses and Generations, beginning of year	.806
Gains	.349
Losses	.(15)
Spouses and Generations, end of year	.1,140
Total Lives	.63,777

## Experience of the Association from Organization to 31 December 2000

Year*	Number of members	(\$) Insurance in force	New members	Average age of Insured at date of issue	Decedents	(\$) Death Benefits Paid	(\$) Reserves
1879	305	194,895	41.35	42.01			3,759
1880	593	932,196	34.81	39.09	36.72	1,478	7,523
1890	1,047	3,141,000	34.88	45.49	47.74	60,000	106,852
1900	1,346	4,038,000	27.19	47.61	54.58	72,000	147,768
1910	1,424	4,272,000	27.08	48.32	67.55	105,000	325,282
1920	1,558	4,974,000	29.56	47.97	66.48	106,000	438,971
1930	6,283	25,050,000	32.79	41.06	59.43	171,000	2,238,537
1940	8,465	35,725,833	29.18	44.56	57.95	327,007	5,405,070
1950	14,642	69,136,898	30.96	43.03	49.84	595,940	10,803,136
1960	25,411	132,550,801	35.40	44.08	63.77	901,713	27,441,332
1970	40,601	312,365,372	31.56	43.53	57.55	2,364,964	72,022,430
1980	47,674	575,381,813	34.59	47.56	64.72	5,084,567	171,263,311
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	1,677,139,294	32.60	54.70	75.67	17,655,618	597,610,247
1999	61,227	1,909,284,032	32.60	53.10	76.83	17,716,553	639,501,125
2000	62,637	2,450,142,874	32.80	49.10	78.00	18,417,309	658,065,901

\*1880-1990 shown in ten-year increments.

(For privacy purposes, listings of Member Deaths and New Members are no longer included in the Annual Report.)

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

*Certified Public Accountants*

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

**(301) 588-5572**

**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, 2000, 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 (GAAP). The effects on the financial statements of the variances between the statutory basis of accounting and GAAP, 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 GAAP, the financial position of Army and Air Force Mutual Aid Association as of December 31, 2000, 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 do present fairly, in all material respects, the financial position of Army and Air Force Mutual Aid Association as of December 31, 2000, 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 supplementary information (Summary of Assets - 31 December 2000) 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

April 2, 2001

# Statement of Assets, Liabilities and Reserves

Statutory Basis  
31 December 2000

## Assets

### Bonds

U.S. Government Obligations .....	\$ 137,956,707
Corporate Bonds .....	<u>200,323,725</u>

Total Bond .....\$ 338,280,432

Real Estate Mortgages .....	99,903,995
Real Estate Investments .....	63,993,458
Equity Securities .....	83,321,433
Member Loans, net of allowance .....	52,729,781
Cash and Cash Equivalents .....	15,131,993
Accrued Investment Income .....	7,629,527
Related Party Receivable .....	94,035
Property and Equipment, at cost (less accumulated depreciation of \$923,558) .....	<u>950,046</u>

Total Assets .....\$ 662,034,700

## Liabilities and Reserves

### Liabilities

Death Benefits Payable .....	\$ 1,083,775
Accounts Payable .....	659,332
Deferred Revenue .....	1,973,855
Accrued Post-retirement Benefits .....	<u>251,837</u>

Total Liabilities .....\$ 3,968,799

### Reserves

Insurance and Other .....	\$545,339,951
Interest Maintenance .....	25,845,975
Asset Valuation .....	29,693,722
General Contingency .....	<u>57,186,253</u>

Total Reserves ..... 658,065,901

Total Liabilities and Reserves .....\$ 662,034,700

*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 2000

### Income

Premiums	\$ 13,422,193	
Net investment income	40,877,303	
Amortization of interest maintenance reserve	<u>1,065,295</u>	\$ 55,364,791

### Benefits and Expenses

Death benefits	\$ 18,417,309	
Surrender benefits	2,152,124	
Services benefits	1,219,856	
Premium refunds, term insurance	255,133	
Annuity payments	49,688	
Insurance expense		
Increase in aggregate reserves for life policies	7,259,646	
Decrease in reserves for annuities	(51,473)	
Increase in other reserves	46,984	
General administrative and operating expenses	<u>4,880,517</u>	<u>(34,229,784)</u>

### Net Income Before Excess Interest Credits

and Investment Transactions	21,135,007
Excess interest credited to members' policies	<u>(11,644,487)</u>

### Net Income After Excess Interest Crediting

Net realized gain on investments	
(excluding interest maintenance reserve gains)	<u>11,955,608</u>

### Net Income from Continuing Operations

	21,446,128
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### Discontinued Operations

Loss on disposal of division	<u>(478,883)</u>
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### Net Income

	<u><u>\$ 20,967,245</u></u>
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### Reserve Transactions

#### Insurance and Other Reserves, Beginning of Year

Increase in reserves for life policies	\$ 7,259,646	
Decrease in reserves for annuities	(51,473)	
Increase in other reserves	46,984	
Excess interest credited	<u>11,644,487</u>	
Net change in reserves for the year		<u>18,899,644</u>

#### Insurance and Other Reserves, End of Year

	<u><u>\$ 545,339,951</u></u>
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#### General Contingency Reserve, Beginning of Year

Net Income	\$ 20,967,245	
Change in unrealized appreciation of equity securities	(20,152,788)	
Change in asset valuation reserve	<u>2,183,185</u>	
Net change in reserves for the year		<u>2,997,642</u>

#### General Contingency Reserve, End of Year

	<u><u>\$ 57,186,253</u></u>
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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 2000

### Cash Flows from Operating Activities

Net income		\$ 20,967,245
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of interest maintenance reserve	(1,065,295)	
Equity earnings in subsidiaries	(2,300,028)	
Depreciation	152,222	
Bad debt expense	156,213	(3,056,888)
Changes in operating assets and liabilities:		
Decrease in accrued investment income	525,744	
Increase in related party receivable	(94,035)	
Decrease in death benefits payable	(265,181)	
Decrease in accounts payable	(138,831)	
Increase in deferred revenue	974,176	
Increase in accrued post-retirement benefits	137,137	
Net increase in life, annuities and other reserves	18,899,644	20,038,654

Net Cash Provided by Operating Activities 37,949,011

### Cash Flows from Investing Activities

Members Loans issued	\$ (24,762,640)
Member Loan Repayments	17,449,941
Securities Purchased	(40,655,609)
Securities Sold	55,659,252
Capital Contributions to Subsidiaries	(33,866,656)
Property and Equipment Purchased	(34,298)

Net Cash Used in Investing Activities (26,210,010)

### Cash Flows from Financing Activities

Decrease in Interest Maintenance Reserve	(84,030)
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Net Cash Used in Financing Activities (84,030)

Increase in Cash and Cash Equivalents 11,654,971  
Cash and Cash Equivalents at Beginning of Year 3,477,022

Cash and Cash Equivalents at End of Year \$ 15,131,993

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

# Notes to Financial Statements

31 December 2000

## 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 "non-admitted" 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 reported 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 1% 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 summary of assets shows the amortized value and market value of each category of securities 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, except that certain loans also require the borrower to pay a fixed amount of additional interest at prepayment or maturity of the loan. 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, (iii) net appreciation

*See Auditor's Report*

on the disposition of the property, and/or (iv) gross proceeds from the sale of the property above a threshold amount.

The Association has one wholly owned subsidiary Limited Liability Company, (LLC). The LLC holds real estate properties with a total estimated market value of \$73,775,000. The investment in this wholly owned LLC is 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 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 \$653,302 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 certain additional reserves at 31 December 2000 such that the sum of accumulation values and these 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.

### **Concentration of Credit Risk**

The Association has a concentration of credit risk in that a majority of its Real Estate Mortgages is held for properties or construction in the Washington, DC metropolitan area. Likewise, the Real Estate Investments consist of real estate located in the Northern Virginia area.

### **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 122-year-old non-profit service organization with over 62,000 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 and soldiers and airmen 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. The Association provides interest-sensitive and term life insurance protection.

## **3. Related-Party Transactions**

Armed Forces Services Corporation (AFSC) is a for-profit, Virginia non-stock corporation created July 1, 2000. This organization resulted from the spin-off of the services department of the Association. As part of the Association, this department provided the various services to the Association's members, i.e., financial awareness and income protection counseling, assistance in applying for entitlement benefits, storage of documents, etc. There are two Association Directors, one serving as the Chairman of AAFMAA, who are also Directors on the Board of AFSC, one serving as the Chairman of AFSC. However, these two members do not constitute a majority vote on the AFSC Board. [Subsequent to this report, the Chairman of AFSC has resigned from the AAFMAA Board and the Chairman of AAFMAA has resigned from the AFSC Board.]

For all Association members who were such before July 1, 2000, and maintain their grandfathered status, these serv-



ices will continue to always be provided. The Association signed a ten-year contract with AFSC to provide these continuing services. For the six-months ended December 31, 2000, the Association incurred servicing expenses of \$1,219,856.

To facilitate a smooth transition for the services department into their own corporate entity, the Association provided office space, supplies and other necessary services to the new entity, AFSC. The costs incurred by AFSC were to be repaid. At December 31, 2000, AFSC owed to AAFMAA \$94,035, which represents the costs incurred through then, including interest at 9.2% per annum.

The Association has guaranteed two bank loans for AFSC, one a six-year term loan for long-term start-up expenses of \$1,700,000, and the other a one-year revolving line of credit to provide working capital funds for \$500,000. AFSC has signed a promissory note to AAFMAA for the amount of both guaranteed loans. If AFSC uses these loan facilities, AFSC pays interest to the lender and pays AAFMAA a fee for the guarantees in the amount of 7% of the amount borrowed.

The property, credit enhancement and intangible benefits provided by AAFMAA to AFSC were carefully valued to assure AAFMAA members and the Internal Revenue Service that no "private inurement" was given by non-profit AAFMAA to for-profit AFSC and to assure the AFSC Board that it was being asked to pay a fair price for the benefits it received. PriceWaterhouseCoopers provided a third party valuation of the intangible benefits ("going concern" value) to assure that intangible benefits were neither under-valued nor over-valued. The valuation amount of \$644,000, owed by AFSC to the Association, is not reflected in the Statement of Assets, Liabilities and Reserves. It will be reflected in the financial statements at such time when payment is received. The valuation amount incurs interest at 9.2% per annum.

#### 4. Retirement Plan

The Association has a 401(k) and profit-sharing plan that covers all employees who meet certain minimum eligibility requirements. The Association may contribute as a matching contribution up to 5% 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 2000 was \$401,927, which includes \$225,329 of employees' elective deferrals.

#### 5. Post-Retirement Benefits

The Association previously sponsored 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%, and has been eliminated except for retirees already covered by the plan. The life insurance plan was noncontributory, and has been eliminated except for retirees already covered by the plan. The post-retirement expense for the year ended 31 December 2000 was approximately \$25,000.

#### 6. 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 \$375,000, with a maximum reimbursement of \$300,000 per insured and \$5,000,000 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. For the year ended 31 December 2000, the Association incurred premiums of \$46,878 for reinsurance.

#### 7. Commitments

The Association has entered into various non-cancelable contracts for equipment rentals, maintenance, and data processing. The obligations for 2001 under these contracts total \$700,200, some of which are subject to CPI increases. In addition to this, the Association has committed \$2,400,000 to the Armed Forces Services Corporation for the performance of services to our members for 2001.

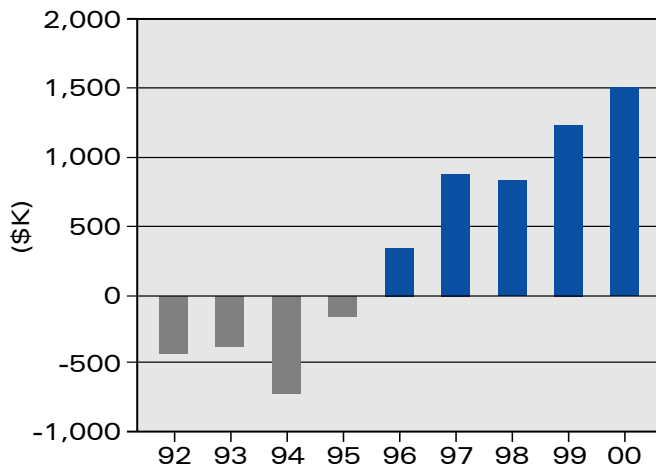
#### 8. Land Lease

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.



# Consolidated Realty

**Annual Net Income**



Consolidated Realty, LLC is wholly owned by AAFMAA and serves as AAFMAA's real estate equity investment arm. Consolidated Realty helps to diversify AAFMAA's investment portfolio and strives to generate a rate of return equal to or exceeding the historical rate of return on real estate equity, adjusted for inflation. This is accomplished by offering exceptional value to tenants through a focus on providing class A office space and superior services. Consolidated Realty seeks to expand its office real estate holdings when it makes sound financial sense.

Before forming Consolidated Realty, properties were held in multiple separate entities. Consolidated Realty was formed in 1994 to eliminate losses and introduce efficiencies. Three factors are responsible for the improved performance: (1) greater attention by management, (2) recent improvement in the real estate market, and (3) additional capital contributions.

The following photos show 4 of the 6 buildings owned by Consolidated Realty. These are examples of the type of superior properties Consolidated Realty has in its portfolio.



# History



In 1876 Lieutenant Colonel George Armstrong Custer (former brevet Major General) led his ill-fated expedition against the Cheyenne and Sioux in Dakota Territory. The ensuing massacre of the 7th Cavalry at the Battle of the Little Big Horn starkly emphasized the desperate circumstances of bereaved Army families of that era.

When a death occurred on the frontier, the family was usually in need, and the Army's method of resolving those needs was a literal "passing of the hat" to raise money to transport dependents "back East" to the care of relatives and friends. In the case of the 7th Cavalry, the old system collapsed. There were no survivors; there was no hat to pass-and no one to pass it to! Thence came the impetus to establish an in-house benefit society. As a result, on 13 January 1879 the Army Mutual Aid Association was created and adopted its Constitution. Those documents were prepared by a Committee chaired by Lieutenant Colonel Roger Jones, Assistant Inspector General of the Army. They expressed the purpose of the Association as "to aid the families of the deceased members in a prompt, simple and substantial manner". The first Certificate of Membership and Insurance was issued to the first President of the Association, the same Lieutenant Colonel Roger Jones on 3 February 1879.

Since then, 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., Walter T. "Dutch" Kerwin, Michael S. Davison, H. Norman Schwarzkopf, and Ronald R. Fogleman.

In 1984, the Association's members voted to make Air Force officers eligible to join. In 1987, the name was officially changed to the Army and Air Force Mutual Aid Association (AAFMAA). In 1995, the Association's members voted to

expand membership to include noncommissioned officers and raise the age limit for admitting new members from 60 to 66 years. In 2000, the Association's members voted to include all enlisted ranks of the Army and Air Force within the eligible categories of membership. Also, in 2000, a corporation comprised of former AAFMAA employees was created and member services was contracted out to the Armed Forces Services Corporation (AFSC), based upon approval at the Annual Meeting.

For more than 122 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. Spouses, children, and grandchildren are also eligible to purchase these life insurance plans.

The Association assists with the preparation of 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, Noncommissioned Officer and soldier and airman should become a member of AAFMAA. Every member is urged to utilize the many services the Association offers, inform their families of the assistance the Association provides at the time of death, and recommend membership to others eligible for membership.

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## Army and Air Force Mutual Aid Association

102 Sheridan Avenue • Fort Myer, VA 22211-1110

Branch office located in Pentagon Concourse

Toll Free: 1-800-336-4538 • Local: 703-522-3060 (*recorded message after hours*) • FAX: 703-522-1336

E-mail: [info@aafmaa.com](mailto:info@aafmaa.com) • Web Site: [www.aafmaa.com](http://www.aafmaa.com)

Office Hours: 8:30 a.m. - 4:30 p.m. • Monday - Friday

*Night depository at Fort Myer*

# AAFMAA Survivor Assistance Services—added protection at no extra cost.

For more than 122 years, AAFMAA has protected the families of Army and Air Force personnel with critical Survivor Assistance Services. In the event of your death, AAFMAA will be there for your family with:

- Expeditious payment. Death benefit is usually initiated on the day we receive the death notification. Other settlement options are available upon request.
- Claims initiation. For government and life insurance claims, upon notification of death, AAFMAA sends appropriate forms for prompt receipt of benefits.
- Claims representation. We make initial inquiries and provide points of contact for resolution of all claims.
- Lifetime generic benefit notification. We provide an annual notice of changes in laws affecting benefits.

## Are you eligible to become an AAFMAA member?

Eligibility extends to those who are:

- Active duty or retired Army or Air Force personnel below age 66.
- Active Army or Air Force Guard or Reserve personnel below age 66.
- USMA and USAFA cadets.
- Army or Air Force ROTC contract or scholarship cadets.

## Is a member's family eligible?

Yes, if:

- Your spouse is below age 71.
- Your children or grandchildren are below age 24 (for Value-Added Whole Life insurance).

## Shop around. There's just no comparison.

AAFMAA is always great coverage for a low price. Here are just some of the reasons:

- AAFMAA's insurance continues after you leave the military. SGLI stops 120 days after you separate or retire.
- Your spouse is eligible for AAFMAA's low-cost coverage. SGLI and VGLI don't cover spouses.
- Survivor Assistance Services are provided at no additional cost.
- Your children and grandchildren are eligible for low-cost AAFMAA coverage, too.
- AAFMAA's representatives are ready to assist you with your best interests in mind.

They'll answer your questions and provide quotes over the phone, without obligation.



*Insurance from a name you can trust... AAFMAA*  
STABILITY • REPUTATION • LOW COST • SINCE 1879

## AAFMAA Direct (toll free) 877-398-2263

Five minutes on the phone NOW could save you thousands of dollars for the life of your policy.

## **AAFMAA. The one place for life insurance, wherever you are in life.**

### **Early in your military career:**

Term life that beats SGLI in price and coverage.

Career Assistance Program (CAP)  
\$5,000 loan and \$250,000 term life

### **As your responsibilities grow:**

Level Term to Age 50

Value-Added Whole Life for you and your spouse

Level Term II College Protection Policy

Career Assistance Program (CAP)  
\$5,000 loan and \$250,000 term life

### **Planning for separation from service/retirement and beyond:**

5-year Renewable Term—cheaper than VGLI  
Value-Added Whole Life Generations Coverage for children and grandchildren

### **AAFMAA protects your family with low-cost coverage.**

You may insure your spouse up to \$500,000 in term, Value-Added Whole Life, or a combination. You may also insure each child/grandchild up to \$100,000 in Value-Added Whole Life.