



INSURANCE FOR EVERY STAGE OF LIFE

Our Mission is to be the **premier provider**
of insurance and survivor services to the
 Army and Air Force communities.

AAFMAA

BOARD OF DIRECTORS

(as of 31 December 2004)

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 Chairman of the Board



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 LTG, USA, Retired
 Vice Chairman of the Board
 Chairman, Finance Committee



JACK N. MERRITT
 GEN, USA, Retired
 Chairman, Membership
 Committee



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 MAJ, USA, Retired
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 GEN Michael S. Davison, USA, Retired

DIRECTORS EMERITI

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 BG Elizabeth P. Hoisington, USA, Retired

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CMSgt Brady M. Gruler, USAF, Retired
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ROBERT L. SMOLEN
 Maj Gen, USAF



JAMES P. GERSTENLAUER
 COL, USA



MACK C. HILL
 BG, USA, Retired

*(Board members are listed in order of
 longevity on the Board.)*

MESSAGE FROM THE CHAIRMAN

In 1879, the Association was founded with the express purpose, "to aid the families of the deceased members in a prompt, simple, and substantial manner". Over 126 years later, that purpose is still AAFMAA's focus. Families. They are why we exist. With this important mission in mind, I am pleased to again report that we are continuing to improve our products and services for the membership and importantly for their survivors. One of the services we added in 2004 is the ability for AAFMAA, through the Defense Finance and Accounting Service (DFAS), to reduce or stop active duty allotments with the member's authorization, which is a convenience for the member and a cost savings for AAFMAA. For our older members, we developed the **ANNUITY**Life product, which is a modified life insurance policy that requires minimal medical underwriting and allows owners to annuitize the policy cash value, either immediately or at a future date. Please see President Lincoln's comments for more details about our products and financial success for 2004.

In order to "aid the families of the deceased members..." AAFMAA's Survivor Assistance Services (SAS) are included with each member's policy, and remain for the lifetime of the surviving family members. We are pleased to have our long-time partner, the Armed Forces Services Corporation (AFSC), under contract to AAFMAA, administer these services, which include:

- Expeditionary payment of the death benefit
- Claims initiation, plus continuous follow-up
- Claims representation, plus follow-up in disputes
- Lifetime individualized notification of changes in laws impacting survivor benefits
- Social Security notification of possible age related income changes for spouses and children
- Annual statement of spouse entitlements



Survivor Assistance Services are included with each member's policy.

For Grandfathered AAFMAA members, AFSC also administers your Living Services. For non-grandfathered members, AFSC's living services can be purchased directly from AFSC.

In 2004, we implemented the Beneficiary Assistance Team, whose sole responsibility is to assist beneficiaries with settling AAFMAA policies. They assist with selection of one of AAFMAA's four settlement options; Life Annuity, Life Annuity with 10 Years Certain, Interest Only, and Lump Sum. With maximum insurance coverage now available up to \$800,000, it is increasingly important for beneficiaries to realize that settlement options, other than lump sum, are available.

All of our products and services are provided so that you, the member, know that AAFMAA will take care of your family when you are gone. You have trusted us to do that for 126 years. That is our mission. That is our focus. That is our promise.

Yours very truly,

A handwritten signature in dark ink, reading "Robert W. Sennewald". The signature is written in a cursive, flowing style.

ROBERT W. SENNEWALD
General, USA, Retired

Since 1879, the Army and Air Force Mutual Aid Association **has played an important role** in making its services available in times of need.

MESSAGE TO THE ARMY AND AIR FORCE MUTUAL AID ASSOCIATION

UNITED STATES AIR FORCE

15 February 2005

Since 1879, the Army and Air Force Mutual Aid Association has been an invaluable resource for our military in times of personal need. Congratulations on 126 years of excellence.

A central concern of the Air Force leadership is the financial and emotional welfare of our military members and their families. The Army and Air Force Mutual Aid Association's legacy of support, commitment, deeds and service has brought peace of mind and security during these difficult and uncertain times to the members of our Armed Forces and their families.

Your Association has earned our deepest respect and gratitude for its important work and for its countless efforts on behalf of our men and women in uniform. Thank you for the work that you perform and best wishes for continued success.



JOHN P. JUMPER
General, USAF

UNITED STATES ARMY


15 February 2005

I would like to express my most sincere appreciation to the Army and Air Force Mutual Aid Association for 126 years of dedicated assistance and support provided to the Soldiers of America's Army and their families.

Today, our Armed Forces enjoy the undisputed distinction of being the best in the world. The readiness of our young men and women is inextricably linked to their well-being. Since 1879, the Army and Air Force Mutual Aid Association has played an important role in making its services available in times of need. Our Soldiers can face the hazards of duty and separation from loved ones knowing that, if needed, their family members will receive competent and compassionate assistance and support from your organization.

Thank you and best wishes for continued success. God bless you and your families, our Soldiers and our Nation.

Sincerely,



PETER J. SCHOOMAKER
General, United States Army

REPORT OF THE PRESIDENT AND TREASURER



As General Sennewald illustrated in his comments, AAFMAA was founded for the specific purpose of aiding the families of deceased members. Today that is still our focus. Achieving three key objectives enables us to fulfill that mission: (1) sell more, (2) control costs and (3) invest wisely.

The following results for 2004 demonstrate AAFMAA's achievements in the "sell more" category.

- **Insurance in force.** Record growth of \$3.2 billion gross insurance sold (a 38% increase from 2003) with a net increase of \$2.5 billion.
- **Policies in force.** Net increase of 2,833 policies for a new record total of 97,799 policies.
- **Membership and Lives Insured.** Net membership growth of 3,029 to an all-time high of 70,167. The number of spouses, children and grandchildren insured increased by a net of 772. Total lives insured at year end was 73,883, a net growth of 5% over 2003.

AAFMAA constantly strives to reduce costs and operate more efficiently. Our new ability to stop or decrease active duty pay allotments with the member's authorization is a convenience for members and has greatly reduced the administrative costs associated with allotment premium payments. Similarly, the Trade-Up Program allows insurable members to obtain higher insurance coverages for the same premium, typically by consolidating several small policies into a single larger policy. This helps the member with higher benefits but also helps all members by controlling operating expenses such as postage, labor, printing, and insurance maintenance costs to administer fewer, larger policies. Cost cutting initiatives allow us to continue offering low-cost insurance premiums. Our Level Term I

**We take the confidence
you place in us seriously and
work constantly to achieve the
best results possible...**

policy can save a family up to 50% over comparable coverage from SGLI. Our Level Term II policy is a great alternative to VGLI with savings up to 75%!

Equally important is our investment performance. AAFMAA adheres to strict investment guidelines, which have proven to be very successful. In 2004 the Net Yield on Assets was 6.3% and our Total Return was 8.2%, enabling us to maintain an attractive 7.0% crediting rate. Our total assets for year end 2004 equaled \$800 million, an increase of \$40 million from 2003. We understand that it's your money; we are responsible for investing it wisely. We take the confidence you place in us seriously and work constantly to achieve the best results possible, within acceptable limits of risk.

The result of selling more, controlling costs and investing wisely is to be able to continue to provide our members and their families a variety of low-cost products, an attractive crediting rate, and excellent services. You trust us to take care of your survivors when you are gone. We value that trust.

Walter R. Lincoln

WALTER R. LINCOLN, CFP®
MAJ, USA, Retired
President and Treasurer

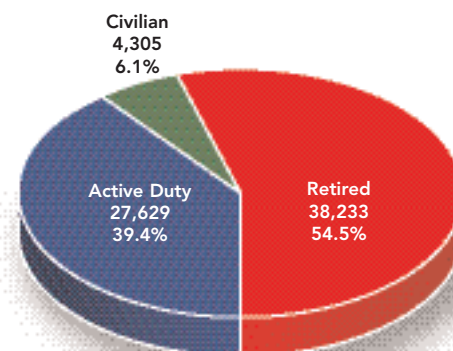
COMPARATIVE HIGHLIGHTS

	Year ended 31 December	
	2004	2003
Insurance in Force (\$ millions)	\$9,605	\$7,130
Total Reserves (\$ millions)	\$785.6	\$754.0
Number of members	70,167	67,138
Number of member deaths	878	842
Death benefits paid (\$ millions)	\$33.6	\$24.5
Net Yield on Assets	6.3%	6.9%
Total Portfolio Return	8.2%	12.2%

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.

MEMBER PROFILE



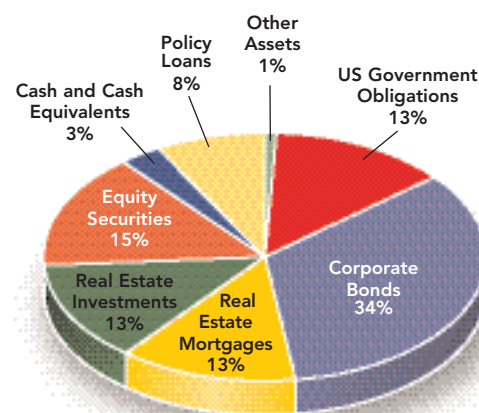
Surviving Spouses: 11,915

2004 ASSETS

SUMMARY OF ASSETS

	Year ended 31 December	
Securities	Amortized Value	Market Value
U.S. Government Obligations	\$ 107,993,697	\$ 108,560,277
Corporate Bonds	264,064,482	297,320,947
Real Estate Mortgages	102,964,585	102,964,585
Real Estate Investments	107,894,566	138,949,285
Equity Securities	116,193,384*	116,193,384
Cash and Cash Equivalents	26,667,201	26,668,532
Accrued Investment Income	8,086,074	8,086,074
Total Securities	733,863,989	798,743,084
Policy Loans	65,591,259	65,591,259
Property & Equipment Net of Accumulated Depreciation	505,584	505,584
Other Assets	450,267	450,267
Total Assets	\$ 800,411,099	\$ 865,290,194

*Equity Securities are valued at market.

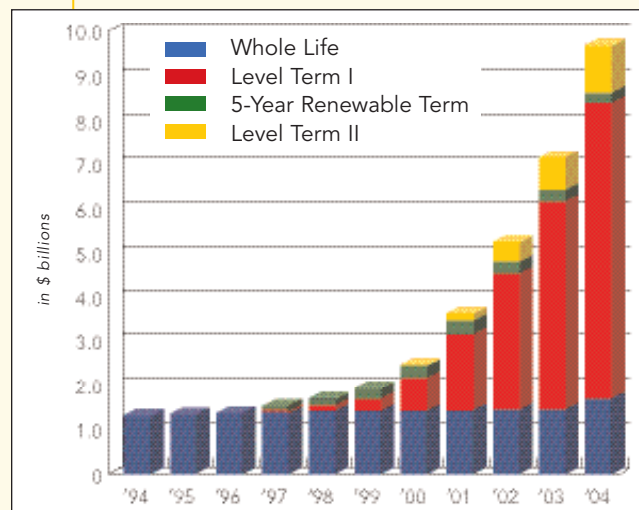


Total Assets: \$800 Million

INSURANCE IN FORCE

Insurance in force, beginning of year\$7,129,672,995
 Insurance sold\$3,220,311,545
 Death benefit growth13,319,189
 Death benefits incurred(33,550,549)
 Other terminations(724,872,836)

Insurance in force, end of year\$9,604,880,344

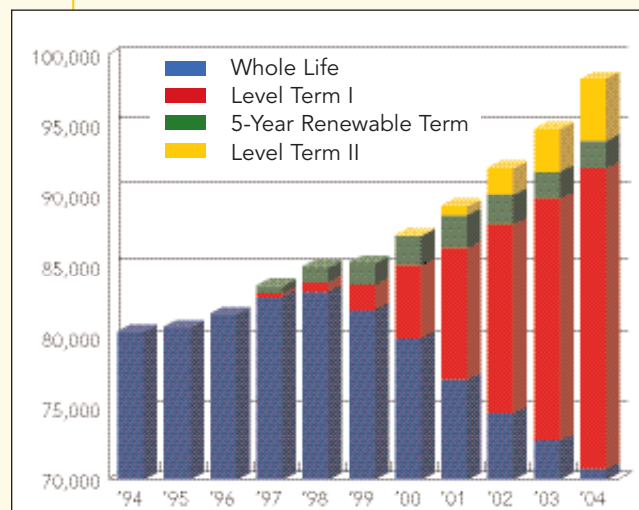


POLICIES IN FORCE

Policies in force,
 beginning of year94,966
 New policies issued9,553
 Policies matured by death(1,308)
 Other policy net terminations(5,412)

Policies in force, end of year97,799

Note: Beginning balance includes 243 Service Only (SO) policies and ending balance includes 232 SO policies.

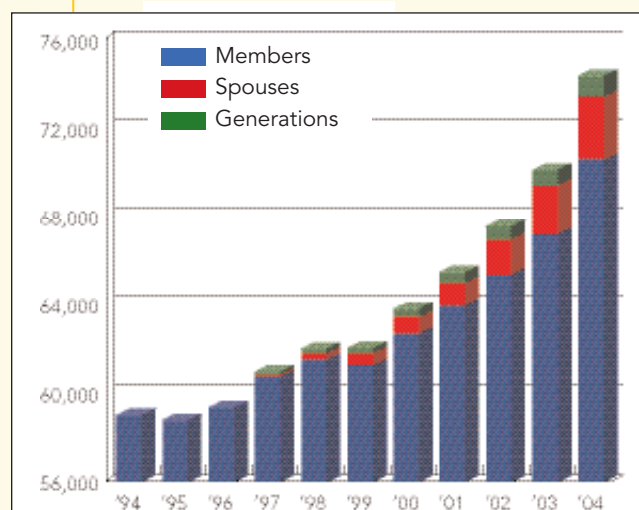


MEMBERS AND LIVES

Members, beginning of year67,138
 Gains5,924
 Losses(2,895)
 Members, end of year70,167
 Spouses and Generations, beginning of year2,944
 Gains862
 Losses(90)

Spouses and Generations, end of year3,716

Total Lives73,883



STATEMENT OF ASSETS, LIABILITIES AND RESERVES

STATUTORY BASIS

For the year ended 31 December 2004

ASSETS

Bonds		
U.S. Government Obligations	\$ 107,993,697	
Corporate Bonds	<u>264,064,482</u>	
Total Bonds		\$ 372,058,179
Real Estate Mortgages		102,964,585
Real Estate Investments		107,894,566
Equity Securities		116,193,384
Policy Loans		65,591,259
Cash and Cash Equivalents		26,667,201
Accrued Investment Income		8,086,074
Property and Equipment, at cost		
(less accumulated depreciation of \$972,398)		505,584
Other		<u>450,267</u>
Total Assets		<u><u>\$ 800,411,099</u></u>

LIABILITIES AND RESERVES

Liabilities		
Death Benefits Payable	\$ 9,063,440	
Accounts Payable	1,781,249	
Deferred Revenue	1,339,593	
Settlement Options Payable	2,214,513	
Accrued Post-Retirement Benefits	<u>441,460</u>	
Total Liabilities		\$ 14,840,255
Reserves		
Insurance and Other	\$ 589,876,176	
Interest Maintenance	48,363,379	
Asset Valuation	32,218,551	
War Risk	41,623,581	
General Contingency	<u>73,489,157</u>	
Total Reserves		<u>785,570,844</u>
Total Liabilities and Reserves		<u><u>\$ 800,411,099</u></u>

See Notes to Financial Statements

STATEMENT OF INCOME AND RESERVES

STATUTORY BASIS

For the year ended 31 December 2004

INCOME

Premiums	\$	45,899,124	
Dues		90,943	
Net investment income		41,527,505	
Amortization of Interest Maintenance Reserve		<u>3,362,002</u>	\$ 90,879,574
Benefits and Expenses			
Death benefits	\$	33,550,549	
less war claims		<u>(5,610,000)</u>	
Net death benefit claims	\$	27,940,549	
Surrender benefits		25,988,735	
Services benefits		2,355,778	
Premium refunds, term insurance		775,905	
Annuity payments		158,327	
Insurance expense			
Increase in aggregate reserves for life policies		16,024,186	
Increase in reserves for annuities		73,292	
Increase in reserves for dues		39,405	
General administrative and operating expenses		<u>6,959,278</u>	<u>(80,315,455)</u>
Net Income Before Excess Interest Credits and Investment Transactions			
Excess interest credited to policies			10,564,119
			<u>(6,883,395)</u>
Net Income After Excess Interest Crediting			
Net realized gain on investments			3,680,724
(excluding Interest Maintenance Reserve gains of \$911,940)			<u>4,722,230</u>
Net Income			<u><u>\$ 8,402,954</u></u>

RESERVE TRANSACTIONS

Insurance and Other Reserves, Beginning of Year	\$	568,355,898
Increase in reserves for life policies	\$	16,024,186
less portion attributable to War Reserve		<u>(1,500,000)</u>
Net increase in reserves for life policies		14,524,186
Increase in reserves for annuities		73,292
Increase in reserves for dues		39,405
Excess interest credited		<u>6,883,395</u>
Net change in reserves for the year		<u>21,520,278</u>
Insurance and Other Reserves, End of Year		<u><u>\$ 589,876,176</u></u>

GENERAL CONTINGENCY RESERVE

General Contingency Reserve, Beginning of Year	\$	64,925,992
Net Income	\$	8,402,954
Decrease in unrealized depreciation of equity securities		8,193,747
Increase in Asset Valuation Reserve		(2,423,536)
Increase in War Reserve		(7,110,000)
Life insurance reserve increase attributable to War Reserve		<u>1,500,000</u>
Net change in reserves for the year		<u>8,563,165</u>
General Contingency Reserve, End of Year		<u><u>\$ 73,489,157</u></u>

See Notes to Financial Statements

STATEMENT OF CASH FLOWS

STATUTORY BASIS

For the year ended 31 December 2004

CASH FLOWS FROM OPERATING ACTIVITIES

Net income	\$	8,402,954
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of Interest Maintenance Reserve	\$	(3,362,002)
Equity earnings in subsidiaries		(7,071,582)
Realized net gains from investments		(5,634,170)
Amortization/accretion of bond discounts/premiums		1,317,290
Net increase in life, annuities & other reserves		21,520,278
Depreciation		35,570
Bad debt expense		385,569
		7,190,953
Changes in operating assets and liabilities:		
Decrease in accrued investment income	\$	163,278
Decrease in other assets		132,793
Increase in death benefits payable		6,896,216
Increase in accounts payable		724,115
Decrease in deferred revenue		(305,391)
Increase in accrued post-retirement benefits		6,552
Increase in settlement options payable		1,072,572
		8,690,135
Net Cash Provided by Operating Activities		24,284,042

CASH FLOWS FROM INVESTING ACTIVITIES

Policy loans issued	\$	(22,361,238)
Policy loan repayments		20,983,764
Securities purchased		(155,994,373)
Securities sold/redeemed		142,064,374
Capital Contributions to subsidiaries		(6,215,758)
Distribution from subsidiaries		8,619,262
Net Cash Used by Investing Activities		(12,903,969)
Increase in cash and cash equivalents		11,380,073
Cash and Cash equivalents at Beginning of Year		15,287,128
Cash and Cash Equivalents at End of Year	\$	26,667,201

See Notes to Financial Statements

1. SIGNIFICANT ACCOUNTING POLICIES

These notes summarize major accounting policies followed by AAFMAA to prepare our financial statements. The accompanying financial statements conform to statutory accounting practices. Although AAFMAA is not subject to insurance regulation, these financial statements conform to 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 (GAAP). Because a major objective of 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. Management believes statutory accounting practices more conservatively measure AAFMAA'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 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. Equities are reported at fair market value. Investments in bonds are reported at amortized cost in accordance with the National Association of Insurance Commissioners (NAIC).

Real estate mortgages, policy loans and Career Assistance Program (CAP) loans are reported at unpaid principal balances, or cost. The carrying values of 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 loans is recorded when earned, except on loans in foreclosure or where collection is uncertain. CAP loans are non-collateralized. CAP loans of approximately \$379,600 were written off due to non-performance during the year. This number represents about 1.4% of total CAP loans outstanding as of year-end.

Realized gains and losses on sales of investment securities are included in the Statement of Income and Reserves, except as noted in the 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 AAFMAA. Mortgages are private placements for which quoted market values are not available. For mortgages and policy loans, cost is used as the market value. Equity securities are reported at cost of \$126,653,043 less unrealized losses of \$10,459,659.

AAFMAA has two types of real estate mortgage loans: fixed interest rate and variable interest rate. The fixed interest rate loans have characteristics similar to conventional single-family home 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 obligate the borrower to pay both minimum fixed interest and contingent interest. The contingent

interest is either a stated amount within the terms of the loan or 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 on the disposition of the property, (iv) gross proceeds from the sale of the property above a threshold amount, and/or (v) initial principal.

AAFMAA has two wholly owned real estate investment subsidiaries: Starco Properties Holding LLC and Riverside Property LLC. Starco Properties Holding LLC was formed on 1 January 2004 as a single member limited liability company (LLC), for the purpose of holding individual LLCs, formed to own and operate real estate investment properties. This form of ownership limits risks and liabilities from one commercial real property affecting other commercial real properties owned by AAFMAA. Starco Properties Holding LLC has a total estimated market value of \$104,525,000 and was 100% leased at 31 December 2004. Riverside Property LLC was formed in September 2003 as a single purpose entity owning one office property in Washington, DC. As of 31 December 2004, the property was 100% leased to a single tenant. On 21 January 2005, the tenant exercised its option to purchase the property. AAFMAA intends to terminate Riverside Property LLC after the completion of its audit and the payment of 2004 and 2005 D.C. Unincorporated Business Franchise Taxes.

Property and Depreciation

Certain office equipment, furniture and applications software are expensed in the year of purchase. Under statutory accounting practices, the book values (cost less accumulated depreciation) of these assets are considered "non-admitted assets," i.e. assets accorded no value. The building, land improvements and certain other equipment are being depreciated on a monthly basis. Total depreciation for the year was \$35,570.

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 of insurance are equal to the sum of the individual benefit plan accumulation values but not less than the minimum cash value for each certificate. AAFMAA held certain additional reserves at 31 December 2004 such that the sum of accumulation values and these additional reserves were equal to or greater than minimum reserves for such certificates as prescribed by the NAIC for regulated insurers. Excess interest credits, as reflected in the Statement of Income and Reserves, equaled the amount credited to cash value accounts in excess of statutory minimums.

Interest Maintenance Reserve/Asset Valuation Reserve

An IMR is maintained based upon a formula prescribed by the NAIC for the purpose of capturing the realized gains and losses resulting from changes in the overall level of interest rates. These realized gains and losses are amortized into income over the approximate remaining life of the investments had they not been sold. An AVR is maintained based upon a formula prescribed by the NAIC for the purpose of providing for default and equity risks related to AAFMAA's invested assets.

Concentration of Credit Risk

AAFMAA has a concentration of credit risk. 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 assets 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.

31 December 2004

2. NATURE OF BUSINESS

AAFMAA was formed in 1879. It provides life insurance benefits and survivor services. Members consist of active, retired, reserve, and guard, officers, warrant officers, non-commissioned officers and soldiers and airmen of the US Army and US Air Force, cadets serving at the US Military Academy and US Air Force Academy, and cadets with ROTC scholarships and contracts. AAFMAA also insures the spouses, children and grandchildren of members. Spouses, children, and grandchildren are NOT members unless qualified as such in their own right. AAFMAA provides interest-sensitive and term life insurance and Survivor Assistance Services.

3. RELATED-PARTY TRANSACTIONS

Armed Forces Services Corporation (AFSC) was created 1 July 2000 to provide living services and survivor services under contract to AAFMAA. For the year ending 31 December 2004, AAFMAA incurred servicing expenses of \$2,355,778. Based on a modification to the AAFMAA/AFSC Services Contract in May 2004, AAFMAA exchanged AFSC's debt (principal and accrued interest) of \$707,557 for greater flexibility for the members and expanded survivor services for members' beneficiaries.

4. OTHER ASSETS

Other Assets on the Statement of Assets, Liabilities and Reserves consist of the following:

• Prepaid Expenses	\$ 58,034
• Other receivable-AFSC	10,050
• Deferred Compensation Assets	382,183
	<u>\$450,267</u>

5. EMPLOYEE BENEFITS**Retirement Plan**

AAFMAA has a 401(k) and profit-sharing plan that covers all employees who meet certain minimum eligibility requirements. AAFMAA may contribute as a matching contribution up to 6% of employee compensation. In addition, it may contribute an amount equal to 3% of compensation. The total retirement plan expense for the year ended 31 December 2004 was \$475,617 which includes \$240,354 of employees' elective deferrals.

Life Insurance

AAFMAA self-insures each employee for \$50,000 after one year of employment. Employees may obtain additional life insurance coverage with AAFMAA at their own expense if they qualify. Employees are NOT members of AAFMAA unless qualified as such in their own right.

6. POST-RETIREMENT BENEFITS

All retiree benefits have been eliminated except for those retirees and/or surviving spouses of retirees previously covered under the retiree health care plan. There are currently seven retirees covered under the retiree health care plan, two are covered until age 65, and five are covered until death. Retiree health care plan costs to AAFMAA in 2004 were \$10,686.

The retiree health care plan costs AAFMAA 40% of premiums or a fixed monthly amount for select retirees; the retiree contributes 60%. Projected, cumulative obligations follow:

Five Retirees until death	\$51,414
Two Retirees until age 65	<u>7,864</u>
Seven Total projected retiree costs	<u>\$59,278</u>

The deferred compensation plan has been eliminated. Three retirees will receive payouts of the amounts the retirees funded with deferrals from their compensation.

7. COMMITMENTS

AAFMAA has committed \$2,350,839 to AFSC to provide services to AAFMAA's members for 2005. Since 31 December 2004, the Association has committed to fund approximately \$7,875,000 for commercial real estate loans.

8. LAND LEASE

In December 1998, AAFMAA entered into a 30-year lease with the Department of the Army to lease the land upon which AAFMAA'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.

TO THE BOARD OF DIRECTORS, ARMY AND AIR FORCE MUTUAL AID ASSOCIATION

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, 2004, 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 auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

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 reasonable 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, 2004, 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, 2004, 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 2004) is presented for purposed 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.

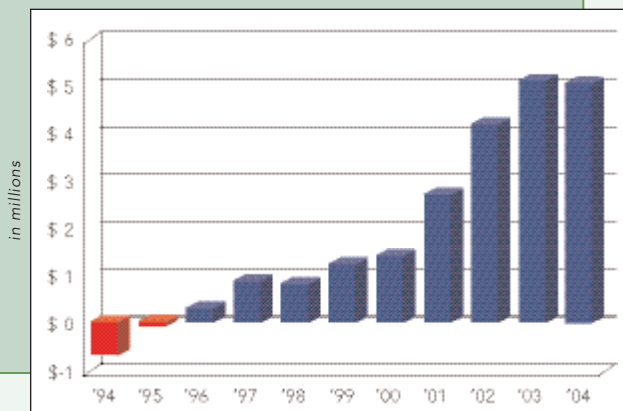
BERLIN, RAMOS & COMPANY, P.A.

March 15, 2005

STARCO PROPERTIES

In January of 2004, AAFMAA restructured the ownership of its real estate equity investments into multiple single purpose entities under the brand name of Starco Properties (Starco). The purpose of this restructuring was to insulate each of the commercial properties so that risks and liabilities from one commercial real property do not spill over and adversely affect other commercial real properties owned by AAFMAA. AAFMAA still retains 100% ownership of the assets.

ANNUAL NET RENTAL INCOME



Starco 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. Starco expands its holdings by either constructing buildings on its own land or by purchasing existing properties.

As of year end 2004, Starco's holdings totaled 414,755 square feet of rentable space, among six buildings. All space is fully leased and performing. In addition to the six operating properties, Starco owns two parcels of



CHARLES B. BETANCOURT
GENERAL MANAGER
STARCO PROPERTIES

land. Plans for 2005 include the design development and permitting of a two building complex on one of the land parcels.

Central to Starco's mission is the introduction of efficiencies among real estate investment properties through greater attention by management, and lease-up to high quality tenants.

As a result of these efficiencies, during 2004, Starco distributed to AAFMAA \$6.9 million earned from its operations.

The graph on this page depicts the change in net rental income since 1994.

DURING 2004 STARCO WELCOMED THE FOLLOWING NEW TENANTS:



AOC Solutions, Inc.



The Protection Engineering Group, PC.



Millennium Science & Engineering, Inc.



Eye Street Software Corporation

Individual needs differ. Whether you're just starting out, building a family or planning for the future, with the variety of coverages offered by AAFMAA there is a plan to fit your needs.

AAFMAA PRODUCTS AND SERVICES

AAFMAA Offers **Six Ways** to Protect You and Your Family

TERM INSURANCE PLANS

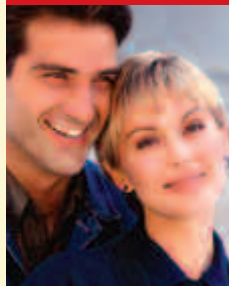
AAFMAA Level Term I is inexpensive term life insurance designed for active duty members under age 50.

- Low-cost coverage up to \$600,000
- Level premium and coverage to age 50 (non-nicotine users), 40 (nicotine users)
- Continues after separation/retirement
- NO war, NO aviation, NO terrorist clauses
- Maximum coverage available even in war zones
- No coverage limitations based on rank



AAFMAA Level Term II is one of AAFMAA's most flexible, cost effective types of coverage.

- You pick how long and how much
- Coverage available for member and spouse up to \$600,000 each
- Spouse eligible for same low rates
- Coverage can take you up to age 85
- Select coverage period from 5 to 25 years
- Rates never change for life of policy
- Can be purchased through age 70 for member and spouse



AAFMAA Family Value Plan saves money on coverage for you, your spouse and children.

- Savings up to 50% over SGLI
- Includes all the features of Level Term I
- Designed for young families
- Coverage available for member and spouse up to \$600,000 each
- Same low level rates for member and spouse
- \$10,000 coverage at no additional cost for eligible children with member's policy
- Convertible to Value-Added Whole Life without a physical exam

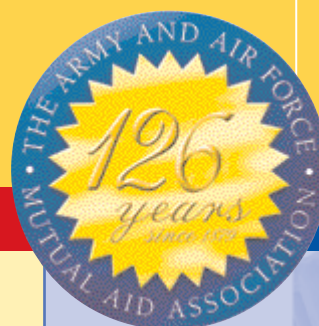


Survivor Assistance Services are included with all member policies at no additional cost. AAFMAA will be there for your family with:

- Expedient payment of death benefit
- Prompt claims initiation plus continuous follow-up
- Claims representation plus follow-up in disputes
- Lifetime individualized benefit notification
- Other valuable services



GROWTH BUILT
ON TRUST WITH
THE HIGHEST
STANDARD OF
INTEGRITY AS
OUR STEADY
GUIDE.



A TRADITION OF PROTECTING ARMY/AIR FORCE MEMBERS AND FAMILIES FOR 126 YEARS

AAFMAA was established as the Army Mutual Aid Association in 1879 to aid the families of deceased soldiers with their final expenses. For more than 126 years AAFMAA has offered its members low-cost life insurance and unsurpassed Survivor Assistance Services. Two things distinguish AAFMAA from other military benefit and service providers. First, as a non-profit, member-owned organization, every penny we make above expenses goes back to the members as increased cash value, term refunds, lower cost insurance, increased reserves or more services. Secondly, AAFMAA always puts the member's best interest first. For over 126 years we have been there for members and families in their time of need.

Who can be a member?

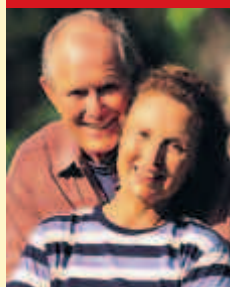
All Army and Air Force personnel, active, retired, Guard and Reserve below the age of 66, USMA and USAFA cadets, ROTC contract and scholarship cadets are eligible for membership.

Value-Added Whole Life offers you the protection of permanent life insurance, plus the cash value growth of interest sensitive life insurance.

- \$800,000 coverage available including children and grandchildren
- 100% money back guarantee for life
- Premiums guaranteed to never increase
- Borrow up to 75% of the cash value
- Current crediting rate of 7%, NOT guaranteed—subject to change
- Great for settling an estate—helps defray costs
- Long Term Care Settlement Option included in policy. Unused amount remains available as death benefit.
- Flexible payment terms — single payment, 7, 20, 30 years, or pay to age 100
- Can be purchased through age 79 for members and spouses/children and grandchildren through age 23



NEW



ANNUITYLife is our new, Net Single Premium Value-Added Whole Life policy with a cash value and death benefit, designed with our older members' needs in mind.

- Annuitize the cash value immediately or at a later date
- Guaranteed payments to age 100 at 4% with annual bonus check if Net Yield on Assets exceeds 4%
- Minimal medical underwriting
- Policy can be approved regardless of age, sex, or nicotine use



Photo Credit: U.S. Army

*"Let us have faith that right makes might:
and in that faith let us to the end, dare to
do our duty as we understand it."*

— ABRAHAM LINCOLN

ARMY AND AIR FORCE MUTUAL AID ASSOCIATION

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E-mail: info@aafmaa.com • Web Site: www.aafmaa.com

Main Office Hours: 8:30am – 4:30pm • Monday – Friday

Membership and Insurance Sales Telephone Hours until 7:00pm at 1-877-398-2263



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

STABILITY • REPUTATION • LOW COST • SINCE 1879