



AAFMAA

2011

ANNUAL REPORT

AAFMAA Board of Directors

(as of 31 December 2011)

Executive Committee



Donald M. Babers
LTG, USA, Retired
Chairman of the Board



Jack N. Merritt
GEN, USA, Retired
*Vice Chairman of the Board
Chairman, Finance Committee*



William J. Lennox, Jr.
LTG, USA, Retired
Chairman, Membership Committee



Walter R. Lincoln, CFP®
MAJ, USA, Retired
President and Treasurer

Senior Management

Walter R. Lincoln, CFP®
President and Treasurer

Tiana Fallavollita
Assistant to the President

Lisa G. Milman
Vice President for Marketing and Sales

Brady M. Gruler, FLMI
Vice President for Insurance

Tom E. Hargis
Secretary

Ross H. Cutler
Assistant to the Secretary

Merilyn M. Bergstresser
Controller

James M. Malley, CPA
Executive Vice President and
Chief Operating Officer
AAFMAA Financial Advisors LLC

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

Membership Committee



John A. Dubia
LTG, USA, Retired



Donald W. Shepperd
Maj Gen, USAF, Retired



Elisabeth J. Strines
Col, USAF, Retired



John A. Shaud
Gen, USAF, Retired



Tyrus W. Cobb
COL, USA, Retired



Joseph E. DeFrancisco
LTG, USA, Retired



George L. Horvath, III
CSM, USA, Retired



Lewis E. Monroe
CMSgt, USAF, Retired

Finance Committee



L. Donne Olvey
BG, USA, Retired



George T. Greiling
LTC, USA, Retired



Robert L. Smolen
Maj Gen, USAF, Retired



James P. Gerstenlauer
COL, USA, Retired



Mack C. Hill
BG, USA, Retired



Dennis D. Porter
COL, USA, Retired

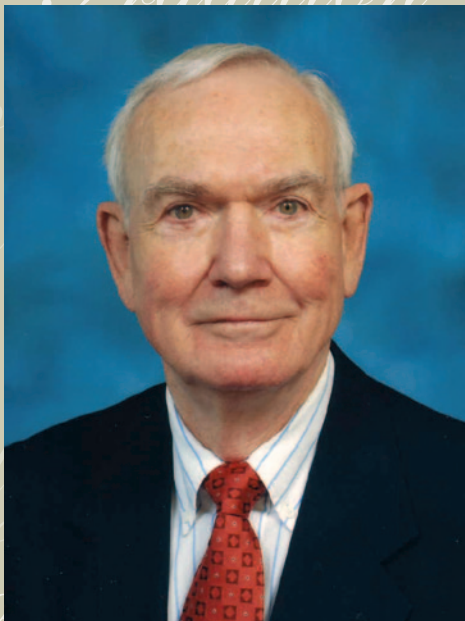


John T. Ridge
CMSgt, USAF, Retired

Thank you very much for all your time and attention that you have given me over the past few months. I couldn't have gotten through all the paperwork associated with my husband's death without your assistance. You were always patient with me and showed me only caring and kindness. I will never forget how helpful you were to me.

Barbara C. – AAFMAA widow

Our mission: to be the premier provider of insurance, financial and survivor services to the American Armed Forces community.



Message from the Chairman

For over 133 years, service members have trusted AAFMAA to take care of what they hold dear; their family. By offering high-quality, low-cost life insurance and critical assistance services AAFMAA provides financial and personal solutions that meet the needs of military families.

Of the many relevant financial solutions provided by AAFMAA, the Long Term Care Settlement Option (LTCISO), included in every Value-Added Whole Life policy at no additional cost, holds particular meaning for me. Financing long term health care is a significant issue for many families, especially the retired and elderly. Today people live longer, increasing the likely need for long term care. Long term care policies provide protection but are very expensive and if the need never arises during the policy's term, the money spent in premiums is lost. AAFMAA recognizes this important issue and offers the LTCISO as an alternate or supplemental solution. The LTCISO allows the owner of a Value-Added policy to convert the death benefit on an eligible insured life into monthly payments to help pay the cost of long term care. However, if you never need long term care, your policy cash value and death benefit continue to grow. One great policy; 3 valuable solutions: death benefit for survivors, LTCISO for owners or annuitized cash value for owners.

Still, AAFMAA represents more than just life insurance. Our legacy of caring for members and their survivors with unique Survivor Assistance Services truly sets us apart. AAFMAA's dedicated professional staff provides caring counsel and assistance, securing millions in financial and government benefits for members and their survivors. As members, we know that AAFMAA will always do the right thing for us and our survivors when we are gone. The stories shared throughout this report remind us of this important principle.

Because relationships built throughout the years with members and survivors live on for generations, AAFMAA continues to grow ever stronger. In 2011 we achieved tremendous results achieving all-time highs in membership, insurance in force and policies in force. Please see the Message from our President and Treasurer for more details. Your non-compensated Board of Directors is committed to making AAFMAA a success for all members. It is my honor to continue to serve the Membership as Chairman of the Board.

Respectfully,

A handwritten signature in dark ink that reads "Donald M. Babers". The signature is fluid and cursive, with a large initial "D" and "M".

DONALD M. BABERS
Lieutenant General, USA, Retired
Chairman, Board of Directors



Message from the President and Treasurer

Dear Fellow AAFMAA Members:

Peace of mind. Protection. Compassion. In 2011, AAFMAA's low-cost, high quality life insurance products and services provided important peace of mind and financial protection to our U.S. service members. Surviving widows, widowers and family members received compassionate and caring advice from the Survivor Assistance Services team which allowed them to breathe a little easier at a most difficult time in their lives...the loss of their loved one. Strong sales, controlled costs and wise investing allow AAFMAA to continue to provide these first class products and services, with superlative, personal attention.

AAFMAA *Life Insurance*

Results for 2011 include:

- Insurance sold — **\$2.85 billion**
- Insurance in Force — **6.3% increase** to **\$24.28 billion**
- New policies issued — **7,959**
- Policies in Force — **2% increase** to **122,137**
- New members joining in 2011 — **5,596**
- Total Membership — **2.4% increase** to **89,439**
- Total Lives Insured — **3% increase** to **99,907**

To ensure future growth, effective 1 September 2011, AAFMAA's membership eligibility expanded to include the Navy, Marine Corps and Coast Guard. Now all members of the U.S. Armed Forces and their families can enjoy the benefits that Army & Air Force members have enjoyed for over 133 years!

In addition to strong sales, investment performance further evidences our success. By adhering to strict investment guidelines, AAFMAA continues to invest successfully even in turbulent times. The Net Yield on Assets for 2011— **5.2%** vs 4.9% in 2010. Total admitted assets, on an amortized value basis, grew to over **\$977 million**, **\$26 million** over 2010.

As a non-profit, membership association, AAFMAA's successes directly benefit you. Over **\$61 million** returned to members, policy holders and their beneficiaries in 2011:

- | | |
|---|---------|
| • Cash value increases | \$10.6M |
| • Death benefit claims | \$47.6M |
| • Term insurance partial premium refunds | \$1.1M |
| • Services and Survivor Assistance Services | \$2.5M |

As a result of research and actions taken by members of AAFMAA's Survivor Assistance Services Team, two AAFMAA widows who were eligible for full SBP and DIC, but had fallen through the cracks, were awarded \$160,000 and \$126,000 respectively in retroactive annuity pay from DFAS in 2011. Due to the dedication and persistency of the staff, both of these widows now have all of their entitlements.

The success in 2011 supports a great crediting rate—6.8% for 2012 on our permanent insurance products. Value-Added Whole Life and **ANNUITY** Life policies provide the stability and reliability of a cash value insurance product. You can build security for you, your children, and your grandchildren. Generally, as your cash value grows due to our high crediting rate, your death benefit grows.

AAFMAA's two subsidiaries provided for more expansion in 2011. Both have exceeded expectations in delivering service to members and families and in profitability.

AAFMAA *Property*

AAFMAA Property LLC holds property in Reston, Virginia. Future real estate property investments will be structured as subsidiary LLCs under AAFMAA Property to minimize liabilities for real estate investments.

The Reston property provides a location for services to members, spouses and survivors as well as a source of income from tenants. The focal point for services is the 1898 Manor House. The office building provides space for current life insurance operations and room for expansion for AAFMAA. Ft. Myer remains AAFMAA's official headquarters. Members can receive great services from the staff at either Ft. Myer or Reston.

Financial results for AAFMAA Property reflect the successful leasing program during the renovation. Space excess to AAFMAA needs has been leased with staggered lease termination dates to allow expansion for AAFMAA growth. In the meantime, lease payments from tenants reduce carrying costs. As of 31 December 2011 100% of the space is leased and occupied. Net Operating Income totaled \$598,778. After depreciation and amortization (non-cash expenses) of \$493,543, Net Income for 2011 was \$105,234 vs a Net Income of \$10,083 in 2010.

AAFMAA *Financial Advisors*

AAFMAA Financial Advisors LLC delivers Living Services to Grandfathered Members, Survivor Assistance Services to members' survivors and beginning in April 2012, new Premier Services to new members and those who have not previously been eligible to benefit from Living Services. During 2011 we helped obtain all entitlements for 710 widows(ers) and provided continued lifetime assistance for approximately 12,800 survivors.

As AAFMAA expands, members continue to obtain unrivaled services provided by AAFMAA Financial Advisors at every location. AAFMAA Financial Advisors' outstanding team will offer great services at more bases/posts. AAFMAA Financial Advisors has saved AAFMAA 42% annually over the costs previously being paid to an outsourced provider. Through 31 December 2011 Net Income totaled \$467,060. When including AAFMAA Financial Advisors' share of overhead costs (\$599,748) the total benefit to AAFMAA for 2011 is \$1,066,808. Expanded services **plus** savings... better for every member and survivor.

As our Chairman referenced in his message, relationships built throughout the years with members and survivors live on for generations. Recognizing this important point, AAFMAA continues to explore expansion opportunities as prudent and relevant for the membership. Our commitment to provide more and better service for members on a **face-to-face** basis will always stand.

AAFMAA exists for the members, their families and survivors. We're here for the long term—a lifetime of benefits and services designed for the needs of all members of the Armed Forces. A pure non-profit, member-owned association. And remember, we never took a dime of bailout money...never needed it; never will.

AAFMAA's two priceless assets—trust of our members and truly unique staff. Without both, AAFMAA would not be what we are today. Superlative, personal service to members and survivors—our number one priority. Always has been...always will be. Developing and maintaining long-term relationships. Providing compassion, hope and lifetime services to survivors of deceased members. An unwavering commitment to provide the right solutions for members and survivors. These are the values we live by. These values make AAFMAA your reliable, respected and trusted choice. Thank you for your membership.

Sincerely,

Walter R. Lincoln

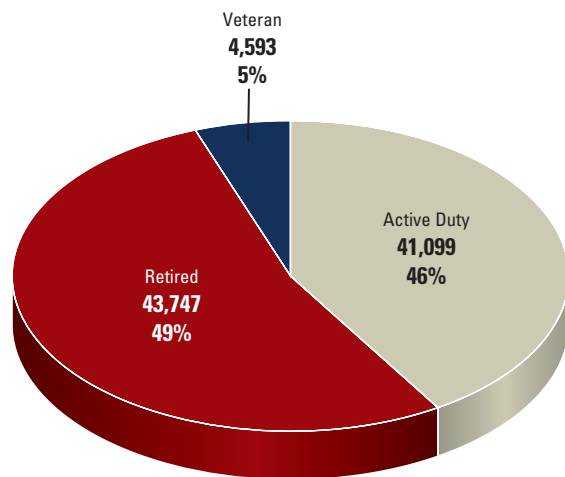
WALTER R. LINCOLN, CFP®
MAJ, USA, Retired
President and Treasurer

When my husband died in August, I faced a myriad of decisions and processes that demanded attention—despite the fact that I was in no emotional state to deal with such matters. I called AAFMAA and met Jennifer. She amazed me with her personal assistance in a series of easy calls; she took my information and proceeded to the claims that triggered payments of death benefits on four life insurance policies in addition to settling our AAFMAA policy. She also provided invaluable assistance to me with DFAS and the VA, to include suggesting how I can explore receiving additional benefits from the VA because of my husband's combat-related disability.

I knew AAFMAA provided special service and assistance as part of its offering, but Jennifer's attitude and service were over the top.

Sally W.— AAFMAA widow

AAFMAA Overview 2011



Member Profile

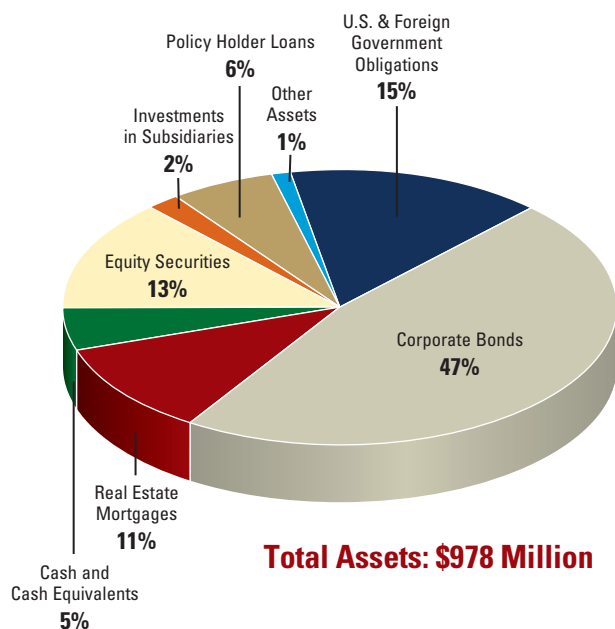
Comparative Highlights

	Year ended 31 December	
	2011	2010
Insurance in force (\$ billions)	\$24.3	\$22.8
Total reserves (\$ millions)	\$934	\$915
Number of members	89,439	87,317
Number of member deaths	1,000	906
Death benefits paid (\$ millions)	\$47.6	\$48.0
Net Yield on Assets	5.2%	4.9%

STATEMENT OF THE ASSOCIATION'S CONSULTING ACTUARY EDDY SQUARED, LLC, GREENSBORO, NC

AAFMAA held \$777,176,830 in contract reserves at 12/31/2011 which in our opinion are at least equal to the minimum requirements for such reserves by the Commonwealth of Virginia. In addition it held voluntary reserves of \$36,811,721, a reserve fund for the future support of investment earnings of \$40,573,137 (the Interest Maintenance Reserve), a reserve fund to offset future asset fluctuations of \$27,561,718 (the Asset Valuation Reserve) and a General Contingency Reserve of \$68,183,372.

2011 Assets



Total Assets: \$978 Million

Summary of Assets

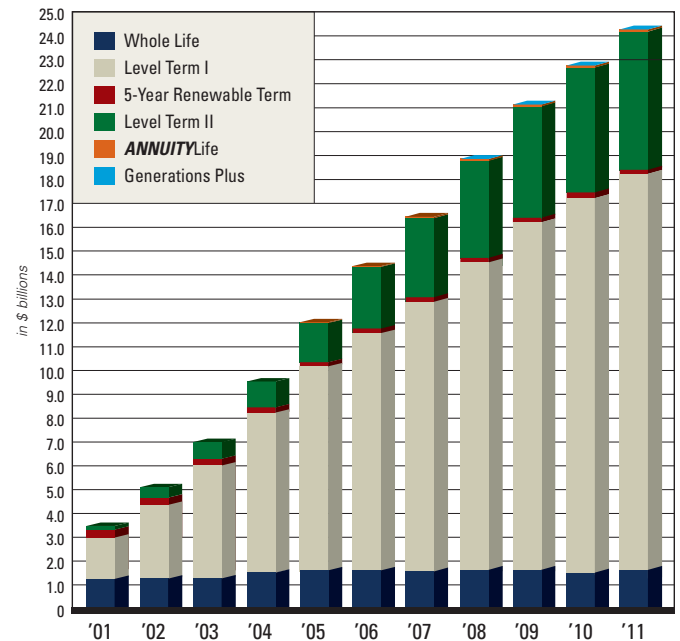
	Year ended 31 December	
INVESTMENTS	ADMITTED ASSET VALUE	MARKET VALUE
U.S. & Foreign Government Obligations	\$ 147,069,690	\$ 160,645,432
Corporate Bonds	458,258,305	510,665,012
Real Estate Mortgages	103,174,444	103,174,444
Cash and Cash Equivalents	49,142,407	49,142,309
Equity Securities*	123,312,718	123,312,718
Investment in Subsidiaries	21,955,389	21,955,389
Accrued Investment Income	10,030,196	10,030,196
TOTAL INVESTMENTS	912,943,149	978,925,500
Policy Holder Loans	63,263,075	63,263,075
Property & Equipment Net of Accumulated Depreciation	767,392	767,392
Other Assets	882,292	882,292
TOTAL ASSETS	\$ 977,855,908	\$1,043,838,259

*Valued at market

Insurance in Force

Insurance in force, beginning of year	\$22,841,431,328
Insurance sold	\$2,850,603,718
Death benefit growth	\$9,122,644
Death benefits incurred	(\$46,143,334)
Other terminations	(\$1,377,404,951)

**INSURANCE IN FORCE,
END OF YEAR \$24,277,609,405**

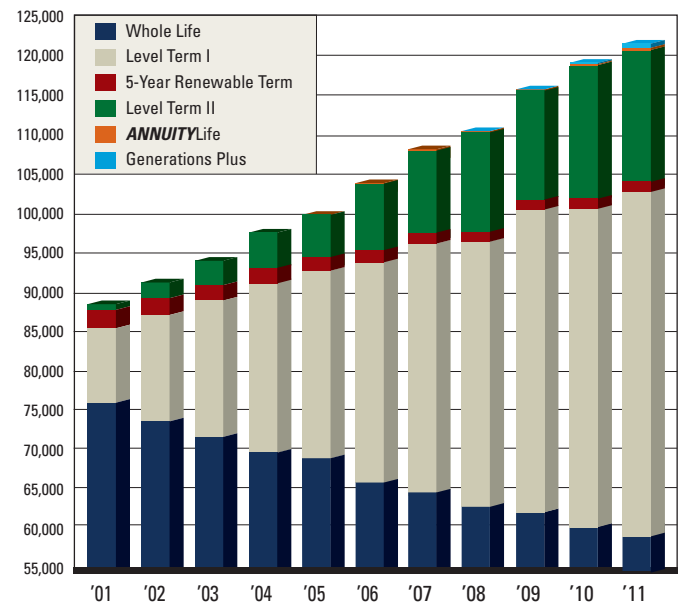


Policies in Force

Policies in force, beginning of year	119,517
New policies issued	7,959
Policies matured by death	(1,523)
Other policy net terminations	(3,816)

POLICIES IN FORCE, END OF YEAR 122,137

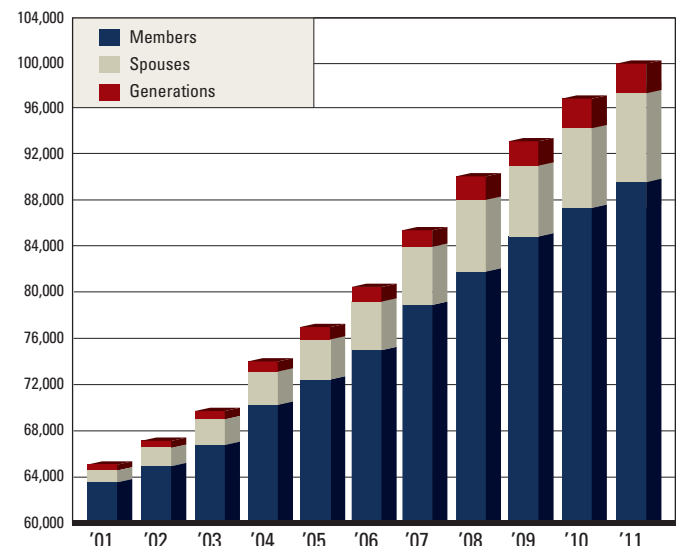
Note: Beginning balance includes 176 Service Only (SO) policies and ending balance includes 172 SO policies.



Lives Insured

Members, beginning of year	87,317
Gains	5,596
Losses	(3,474)
Members, end of year	89,439
Spouses and Generations, beginning of year	9,639
Gains	1,130
Losses	(301)
Spouses and Generations, end of year	10,468

LIVES INSURED, END OF YEAR 99,907



In the past few weeks, my wife and I have been reviewing our estate planning, and I have had questions to which the AAFMAA team has been fabulous in responding. I always knew that I had a good thing in your survivor support program, but now that I again have had the opportunity to experience this service personally, I know that my family will be in good hands when the time comes.

If "quality" can be defined as exceeding expectations, you are part of a quality organization! I will pass the word to my military friends.

Tom P.— AAFMAA Member

Statement of Assets, Liabilities and Reserves

STATUTORY BASIS

31 DECEMBER 2011

Assets

BONDS

U.S. and Foreign Government Obligations	\$ 147,069,690	
Corporate Bonds	<u>458,258,305</u>	
Total Bonds		\$ 605,327,995

REAL ESTATE MORTGAGES 103,174,444

EQUITY SECURITIES 123,312,718

INVESTMENT IN SUBSIDIARIES 21,955,389

POLICY HOLDER LOANS 63,263,075

CASH AND CASH EQUIVALENTS 49,142,407

ACCRUED INVESTMENT INCOME 10,030,196

PROPERTY AND EQUIPMENT, AT COST (less accumulated depreciation of \$1,439,821) 767,392

OTHER 882,292

TOTAL ASSETS **\$ 977,855,908**

Liabilities and Reserves

LIABILITIES

Death Benefits Payable	\$ 17,525,465	
Accounts Payable	7,259,764	
Deferred Revenue	2,599,406	
Settlement Options Payable	16,348,599	
Accrued Post-Retirement Benefits	22,017	
Related Party Payable	<u>164,496</u>	
TOTAL LIABILITIES		\$ 43,919,747

RESERVES

Insurance and Other	\$ 760,806,214	
War Risk	36,811,721	
Interest Maintenance	40,573,137	
Contingency Reserve		
Asset Valuation	\$ 27,561,718	
General Contingency	<u>68,183,371</u>	
Total Contingency Reserve	<u>95,745,089</u>	
TOTAL RESERVES		<u>933,936,161</u>

TOTAL LIABILITIES AND RESERVES **\$ 977,855,908**

See Notes to Financial Statements

My husband died on February 28, 2011. Upon his death, I contacted AAFMAA. My husband had previously explained to me the importance of contacting AAFMAA upon his death. He assured me all survivor documentation would be located with AAFMAA and the assistance I would need would be readily available. From my initial contact with AAFMAA, I was efficiently guided through the process of initiating the claims process for SBP, VA benefits and life insurance. It was a comfort in the midst of grief and uncertainty to have outstanding professional guidance in these areas. I am grateful my husband provided this Survivor Assistance through AAFMAA.

Daunn S. — AAFMAA widow

Statement of Income and Reserves

STATUTORY BASIS

FOR THE YEAR ENDED 31 DECEMBER 2011

Income

Premiums	\$	42,801,379	
Dues		57,016	
Consideration for supplemental contracts		752,848	
Net investment income		44,266,879	
Amortization of Interest Maintenance Reserve		4,730,234	\$ 92,608,356

BENEFITS AND EXPENSES

Death benefit claims	\$	47,658,203	
less war claims		(750,000)	
Net death benefit claims	\$	46,908,203	
Surrender benefits		6,089,007	
Service Benefits		2,476,141	
Premium refunds, term insurance		1,145,304	
Supplemental contracts payments		1,165,160	
Insurance expense			
Increase in aggregate reserves for life policies		13,949,495	
Increase in reserves for supplemental contracts		515,135	
Increase in reserves for dues		37,112	
General administrative and operation expenses		10,010,590	(82,296,147)

NET INCOME BEFORE EXCESS INTEREST CREDITS

AND INVESTMENT TRANSACTIONS			10,312,209
Excess interest credited to policies			(9,388,640)

NET INCOME AFTER EXCESS INTEREST CREDITING

Net realized gain on investments			923,569
(excluding Interest Maintenance Reserve gains of \$6,365,284)			126,294

NET INCOME

	\$	1,049,863	
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Reserve Transactions

INSURANCE AND OTHER RESERVES, BEGINNING OF YEAR

Increase in reserves for life policies	\$	13,949,495	736,915,832
Increase in reserves for supplemental contracts		515,135	
Increase in reserves for dues		37,112	
Excess interest credited		9,388,640	
Net change in reserves for the year			23,890,382

INSURANCE AND OTHER RESERVES, END OF YEAR

	\$	760,806,214	
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General Contingency Reserve

GENERAL CONTINGENCY RESERVE, BEGINNING OF YEAR

Net Income	\$	1,049,863	74,207,973
Increase in unrealized depreciation of equity securities		(2,566,018)	
Increase in non-admitted assets		(3,424,374)	
Increase in Asset Valuation Reserve		(1,084,073)	
Net change in reserves for the year			(6,024,602)

GENERAL CONTINGENCY RESERVE, END OF YEAR

	\$	68,183,371	
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See Notes to Financial Statements

In my struggles with the VA, due to exposure to Agent Orange in Vietnam in 1966-1967 and in South Korea in 1969-1972, I have never encountered a more kind, caring and efficient Veterans Benefits Specialist than at AAFMAA. You are to be congratulated on finding someone like Sarah to take up the mantle. We veterans are the real beneficiaries. Her efficiency played a significant role in helping me obtain 100 percent for Ischemic Heart Disease in addition to the 100 percent for prostate cancer.

James B.— AAFMAA Member

Statement of Cash Flows

STATUTORY BASIS

FOR THE YEAR ENDED 31 DECEMBER 2011

Cash Flows From Operating Activities

Net Income		\$	1,049,863
Adjustments to reconcile net income to net cash			
Amortization of Interest Maintenance Reserve	\$	(4,730,234)	
Equity (Earnings) in Subsidiaries		(567,634)	
Realized Net Gains from Investments		(6,458,917)	
Realized Net Gains included above transferred to Interest Maintenance Reserves		6,365,284	
Amortization/Accretion of Bond Discount/Premiums		(246,940)	
Net Increase in Life & Other Reserves		23,140,382	
Depreciation expense		1,417,738	
Bad debt expense		2,070,666	20,990,345
Changes in operating assets and liabilities			
Decrease in Accrued Investment Income	\$	178,471	
Increase in Other Assets		(191,044)	
Decrease in Related Party Receivable		147,780	
Increase in Death Benefits Payable		2,109,656	
Decrease in Accounts Payable		(102,787)	
Increase in Deferred Revenue		941,370	
Increase in Settlement Options Payable		3,694,832	
Decrease in Accrued Post-Retirement Benefits		(966)	
Decrease in Related Party Payable		(130,175)	6,647,137
NET CASH PROVIDED BY OPERATING ACTIVITIES			28,687,345

Cash Flows From Investing Activities

Policy Loans Issued	\$	(27,931,149)	
Policy Loan Repayments		27,853,695	
Securities Purchased		(295,027,245)	
Securities Sold/Redeemed		284,681,202	
Capital Contributions to Subsidiary		(85,305)	
Capital Distributions from Subsidiary		1,383,709	
Fixed Assets Purchased		(8,299)	
Non-admitted Assets Purchased		(4,779,779)	
Dispositions of Non-admitted Assets		164,566	
NET CASH USED IN INVESTING ACTIVITIES			(13,748,605)
INCREASE IN CASH AND CASH EQUIVALENTS			14,938,740
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR			34,203,667
CASH AND CASH EQUIVALENTS AT END OF YEAR			\$ 49,142,407

See Notes to Financial Statements

1. SIGNIFICANT ACCOUNTING POLICIES

These notes summarize major accounting policies followed by Army and Air Force Mutual Aid Association (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 in accordance with the National Association of Insurance Commissioners (NAIC). Equities are reported at fair market value. Investments in bonds are reported at amortized cost.

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 \$2,223,972 were written off due to non-performance during the year. This number represents approximately 7% 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 admitted asset value and market value of each category of investments 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 \$164,001,130 less unrealized losses of \$40,688,412 (market value of \$123,312,718).

AAFMAA originates fixed rate commercial real estate mortgages. The loans are first lien mortgages on income producing properties with loan to value ratios of 75% or less. They have characteristics similar to conventional single-family home mortgage loans. If repaid early, there is an additional prepayment premium due. The prepayment premium is usually a percentage of the outstanding principal balance corresponding to the years left between the prepayment date and the final maturity of the loan.

AAFMAA formed two wholly owned subsidiaries in 2009, AAFMAA Property LLC and AAFMAA Financial Advisors LLC, as single member limited liability companies (LLC). AAFMAA Property LLC was formed to hold the property in Reston, Virginia to be used as office space for AAFMAA, AAFMAA Financial Advisors LLC and future expansion. AAFMAA has leased the space not currently required for use by AAFMAA or AAFMAA Financial Advisors LLC to third parties. Renovations to the Reston property were completed in 2010. AAFMAA's investment as of 31 December 2011 is \$21,955,389. AAFMAA Financial Advisors LLC was formed to provide Living Services and Survivor Assistance Services to AAFMAA members and surviving widow(er)s. The company began providing these services effective 1 July 2010. AAFMAA also formed a wholly owned subsidiary, AAFMAA Wealth Management Inc., in December 2010 with the expectation of providing wealth management services in the future. No services were provided in 2011. Under statutory accounting practices, the net income or loss from these subsidiaries is accounted for by AAFMAA under the equity method of accounting. Income or loss from these subsidiaries earned in 2011 is included in the Net Investment Income on the Income Statement.

Property and Depreciation

Under statutory accounting practices, the book values (cost less accumulated depreciation) of certain office equipment, furniture and application software are considered "non-admitted assets". These assets are accorded no value. As non-admitted assets, they reduce the amount in the General Contingency Reserve by the amount of their book value. As of 31 December 2011, \$4,870,740 of assets considered non-admitted have reduced the General Contingency Reserve. The building, land improvements and certain other equipment (admitted assets) are being depreciated on a monthly basis. Depreciation for the year totaled \$1,417,738.

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 policies are equal to the sum of the individual benefit plan ac-

cumulation values, but not less than the minimum cash value for each policy. AAFMAA held certain additional reserves at 31 December 2011 such that the sum of accumulation values and these additional reserves were equal to or greater than minimum reserves for such policies 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 (IMR)/Asset Valuation Reserve (AVR)

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 risk. All of its real estate mortgages are in the Washington, DC metropolitan area. Also, AAFMAA maintains both interest-bearing and non interest-bearing accounts at a Federal Deposit Insurance Corporation (FDIC) insured bank. Interest-bearing accounts are insured up to \$250,000. In addition, the FDIC Transaction Account Guarantee (TAG) Program guarantees full deposit coverage through 31 December 2012 for all non interest-bearing transaction accounts, regardless of the dollar amount. Coverage under the TAG program is in addition to and separate from the coverage available under the FDIC's general deposit insurance rules. In addition, AAFMAA maintains various investment accounts, containing securities and cash, in trust with a large financial institution. These accounts are uninsured. The association has not experienced any loss in such account and does not believe it is exposed to any significant credit risk in its cash and cash equivalents.

Income Taxes

The Association is a tax-exempt, non-profit association as described in section 501(c) (23) of the Internal Revenue Code. The income and expenses of the Association, along with those of its wholly owned single-member limited liability companies, are reported on its Federal income tax return. Although the Association is tax exempt, it still evaluates uncertainty in income tax positions based on a "more-likely-than-not" recognition standard, effective 1 January 2010. If that threshold is met, the tax position is then measured at the largest amount that is greater than 50% likely of being realized upon ultimate settlement. As of 31 December 2011, the Association has evaluated its material tax positions and determined that no accruals for uncertain tax positions are required on the Association's financial statement. Returns filed for tax periods ending after 31 December 2008 are open to examination and any changes by the taxing authorities may affect the Association's income tax liability.

2. NATURE OF BUSINESS

AAFMAA was formed in 1879. It provides life insurance, benefits and Survivor Assistance Services. Members consist of all ranks of Army, Air Force, Coast Guard, Marine Corps and Navy personnel who are active duty (or within 120 days after separation), retirees, Guard or Reserve (full or part-time), U.S. Air Force Academy, U.S. Coast Guard Academy, U.S. Military Academy, U.S. Merchant Marine Academy and U.S. Naval Academy midshipmen and cadets, ROTC Contract/Scholarship midshipmen and cadets, and honorably discharged veterans in Florida, Hawaii, Maryland, North Carolina, Oklahoma, South Carolina and Virginia. AAFMAA also offers insurance to 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 whole life insurance, term life insurance, Living Services for members, and Survivor Assistance Services for surviving widow(er)s of deceased members.

3. SECURITIES IMPAIRMENTS

AAFMAA recognizes impairment losses when it is determined that the value of certain fixed maturity securities have other than temporary declines during the applicable reporting period, as well as when there are further declines in the value of securities that were initially written down in a prior period. During 2011, AAFMAA recognized total other-than-temporary impairments of \$94,728 on securities issued by Banc of America Mortgage Securities, Inc., Citigroup Mortgage Loan Trust Inc., Dynegy Holdings, LLC, First Horizon Asset Securities Inc., GS Mortgage Securities Corp., and Wells Fargo Asset Securities Corporation. During 2011, AAFMAA recognized recovery gains on impaired securities of \$142,234 when certain of these securities and securities that were impaired and written down in prior years were sold or paid down at prices above their impairment values (cost).

4. RELATED-PARTY TRANSACTIONS

AAFMAA Financial Advisors LLC provides Living and Survivor Assistance Services to AAFMAA. As part of the servicing agreement, certain personnel and software are shared between the two entities. The servicing expenses incurred by AAFMAA for the year ended 31 December 2011 were \$2,476,141. At 31 December 2011, AAFMAA is due \$51,439 and owes \$215,935 from/to AAFMAA Financial Advisors LLC for various shared expenses. AAFMAA Financial Advisors LLC's net income for 2011 was \$467,060 (\$462,400 when adjusted for straight-line rent for 2010). AAFMAA Property LLC's net income for 2011 was \$105,234. AAFMAA Wealth Management Inc. was not yet operational in 2011; hence, AAFMAA recognized no income or loss from that subsidiary in 2011. The combined net income of \$567,634 from these subsidiaries is included in Net Investment Income on the Statement of Income and Reserves.

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, AAFMAA may contribute an amount equal to 4% of compensation. The total retirement plan funding for the year ended 31 December 2011 was \$605,781 which includes \$303,840 of AAFMAA contributions and \$301,941 of employees' elective deferrals.

Notes to Financial Statements

(AS OF 31 DECEMBER 2011)

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 four retirees covered under the retiree health care plan until death. Retiree health care plan costs to AAFMAA in 2011 were \$3,784. The retiree health care plan costs AAFMAA 40% of premiums or a fixed monthly amount for select retirees; the retiree contributes 60%. The projected, cumulative obligations are \$22,017.

7. LEASE COMMITMENTS

Reston, Virginia

AAFMAA has an agreement with a related party, AAFMAA Property LLC, to lease office space. This wholly-owned subsidiary owns the Reston, Virginia commercial property where AAFMAA maintains daily operations. The lease term runs from 1 July 2010 to 31 December 2019. The annual rental amount is the "weighted average rent" of all non-AAFMAA related tenants at the Reston property and is recalculated annually. AAFMAA has estimated these amounts beyond December 2015 because non-AAFMAA leases do not currently run beyond that date. For the year ended 31 December 2011, AAFMAA incurred rent expense of \$276,976. Future minimum rental expense under this lease is as follows:

2012	\$295,157
2013	301,771
2014	312,637
2015	324,566
2016-2019 (estimated)	1,300,000
Total Minimum Required Rental Payments	<u>\$2,534,131</u>

Fort Myer, Virginia

In December 1998, AAFMAA entered into a 30-year agreement with the Department of the Army to lease the land upon which AAFMAA's building is located at Fort Myer, Virginia. The rent expense for this land lease for 2011 was \$13,473. A December 2011 supplemental agreement defines the annual lease payment increasing as follows:

12/11/2011-12/10/2012 - \$14,000 annually	\$14,000
12/11/2012-12/10/2017 - \$14,800 annually	74,000
12/11/2017-12/10/2022 - \$16,280 annually	81,400
12/11/2022-12/10/2028 - \$17,908 annually	107,448
Total Minimum Required Rental Payments:	<u>\$276,848</u>

8. FAIR VALUE MEASUREMENTS

Statement of Statutory Accounting Principles (SSAP) No. 100 (Fair Value Measurements) provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). Fair value disclosure is required

for any asset or liability reported at fair value in the Statement of Assets, Liabilities and Reserves. The three levels of the fair value hierarchy under SSAP No. 100 are described below:

Level 1 Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets.

Level 2 Inputs to the valuation methodology include: (1) Quoted prices for similar assets or liabilities in active markets; (2) Quoted prices for identical or similar assets or liabilities in active markets; (3) Inputs other than quoted prices that are observable for the asset or liability; (4) Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used attempt to maximize the use of observable inputs and minimize the use of unobservable inputs.

Following is a description of the valuation methodologies used for assets measured at fair value. Common stocks: Valued at closing price reported on the active market on which the individual securities are traded. Rights and warrants: Valued using over-the-counter trade pricing supplied by the Association's custodian bank. Short-term investment funds: Valued at the net asset value ("NAV") of shares held by the plan at year end.

Assets Measured and Reported at Fair Value on a Recurring Basis at 31 December 2011:

	Level 1	Level 2	Level 3
Included in equity securities:			
Common stock	\$123,312,718	\$0	\$0
Included in cash & cash equivalents:			
Short-term investment funds	36,097,241	0	0
Total assets at fair value	\$159,409,959	\$0	\$0

9. PENDING LITIGATION

AAFMAA is a defendant in a lawsuit involving denial of a death benefit claim. AAFMAA denied the plaintiff's claim for benefits because the insured allegedly committed suicide in 2005 within the two-year contestability period. Discovery has not commenced, and, to date, the plaintiff has not aggressively prosecuted the action. AAFMAA is vigorously defending itself in this action. At this juncture, it is premature to evaluate the likelihood of an unfavorable outcome, or to estimate the amount or range of potential loss in this litigation. Legal counsel recommended establishing a claim reserve in the 20-40% range. AAFMAA established a reserve of \$320,000, 40% of the death benefit plus accrued interest.

10. SUBSEQUENT EVENTS

Since 31 December 2011, the Association committed to fund up to \$25,000,000 for new real estate mortgage loans. 22 March 2012 is the date to which events subsequent to December 2011 (the date of the most recent balance sheet) have been evaluated for possible adjustment to the financial statements or disclosure. 22 March 2012 is the date on which the financial statements were available to be issued.

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

We have audited the accompanying statutory basis statement of assets, liabilities and reserves of Army and Air Force Mutual Aid Association as of December 31, 2011, 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 statutory basis 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 statutory basis financial statements referred to above do not present, and are not intended to present in conformity with GAAP, the financial position of the Army and Air Force Mutual Aid Association as of December 31, 2011, or 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, 2011, 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 financial statements as a whole. The supplementary information (Summary of Assets - 31 December 2011) is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Berlin Ramos & Company, P.A.

BERLIN, RAMOS & COMPANY, P.A.
March 27, 2012

AAFMAA Life Insurance



Level Term I

Inexpensive term life insurance for members and spouses.
Great low-cost supplement or alternative to SGLI.

- Level premium and death benefit to age 50 (40 for nicotine users)
- Save up to 27% over SGLI
- \$10,000 coverage, at no additional cost, for eligible children with member's policy
- Same low rates for member and spouse
- Children and grandchildren ages 18–23 eligible to purchase coverage up to \$800,000

Compare these rates before you decide.

Coverage	AAFMAA*	After Refund*	SGLI**
\$100,000	\$ 5.90	\$ 5.90	\$ 6.50
\$250,000	\$ 13.00	\$11.70	\$ 16.25
\$400,000	\$ 19.00	\$17.10	\$ 26.00
\$600,000	\$ 27.00	\$24.30	N/A
\$800,000	\$ 35.00	\$31.50	N/A

*Monthly rates. Non-nicotine users receive 10% annual premium refund on policies over \$100,000, NOT guaranteed and subject to change. \$5.90 is non-nicotine rate. Subject to complete terms and conditions of the policy.

**Premium shown does not include \$1.00 charge for TSGLI.



Level Term II

Flexible, cost effective coverage for members and spouses with short and long term needs.
Great alternative to VGLI.

- Pick the coverage (\$50,000 to \$800,000) and term (5 to 30 years)
- Coverage can last up to age 85
- Save thousands over VGLI!
- Rate NEVER increases/death benefit NEVER decreases for the life of the policy
- Purchase before age 76

20 Year Level Term II, Non-nicotine user, Super Select* monthly rate

Issue Age	Coverage Amount					
	\$100,000		\$400,000		\$600,000	
	Male	Female	Male	Female	Male	Female
45	\$ 14.00	\$ 12.10	\$ 41.00	\$ 33.40	\$ 59.00	\$ 47.60
50	\$ 19.70	\$ 15.50	\$ 63.80	\$ 47.00	\$ 93.20	\$ 68.00
55	\$ 28.00	\$ 22.60	\$ 97.00	\$ 75.40	\$ 143.00	\$ 110.60
60	\$ 44.60	\$ 33.60	\$ 163.40	\$ 119.40	\$ 242.60	\$ 176.60

*This is our BEST RATE CLASS. Rates may be higher depending on individual health and lifestyle. Subject to complete terms and conditions of the policy.

Call Now — 1-877-398-2263

A Tradition of Protecting U.S. Armed Forces Members and Families for 133 Years.



Who Can be a Member? All ranks of Army, Air Force, Coast Guard, Marine Corps, and Navy who are Active Duty (or within 120 days after separation), Retirees, National Guard or Reserve (full or part time), USAFA, USCGA, USMA, USMMA, and USNA midshipmen or cadets, and ROTC contract/scholarship cadets. Additionally, Honorably Discharged Veterans residing in Florida, Hawaii, Maryland, North Carolina, Oklahoma, South Carolina, or Virginia are also eligible.



Generations Plus

Provides children and grandchildren the option of **GUARANTEED INSURABILITY** in the future. **YOU** can help plan their financial security **NOW**.

- Permanent life insurance that builds cash value
- Initial coverage amount from \$10,000 to \$30,000
- Initial coverage amount **automatically doubles** at age 21 with **no increase in premium**
- 100% money back guarantee—all premiums paid at any time and no surrender charges
- Guaranteed 4% crediting rate
- For children 15 days–12 years old
- Guaranteed Purchase Options at ages 21, 25 and 28
- Get up to 4 times initial coverage at each eligible age

Sample Generations Plus Monthly Premiums

Coverage **AUTOMATICALLY DOUBLES** at age 21 at no added cost.

AGE	INITIAL COVERAGE AMOUNT				
	\$10,000	\$15,000	\$20,000	\$25,000	\$30,000
Under 1*	\$6.40	\$9.60	\$12.80	\$16.00	\$19.20
2	\$6.40	\$9.60	\$12.80	\$16.00	\$19.20
4	\$6.50	\$9.75	\$13.00	\$16.25	\$19.50
6	\$6.90	\$10.35	\$13.80	\$17.25	\$20.70
8	\$7.40	\$11.10	\$14.80	\$18.50	\$22.20
10	\$7.90	\$11.85	\$15.80	\$19.75	\$23.70
12	\$8.50	\$12.75	\$17.00	\$21.25	\$25.50

*Minimum age of 15 days. Premiums subject to change. Rates as of 3/1/12. Call for complete list of premium rates.

Contact a Membership Coordinator Today—
1-877-398-2263



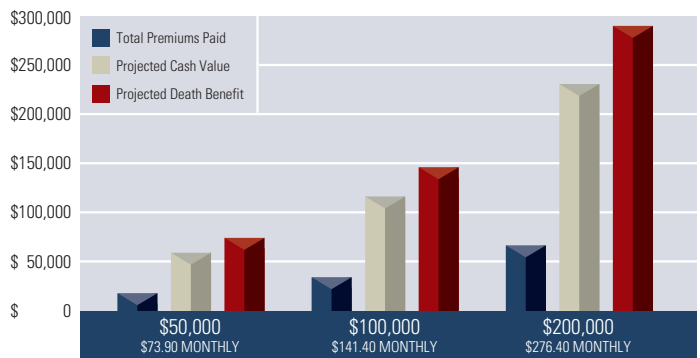
Value-Added Whole Life

Protection of permanent insurance, plus cash value growth of interest-sensitive life insurance.

- 100% money back guarantee for life (total premiums paid or cash surrender value, whichever is GREATER)
- Premiums guaranteed to NEVER increase
- Great crediting rate (6.8% for 2012 — NOT guaranteed, subject to change.) Guaranteed 4.5%
- Borrow up to 75% of the cash value at 1% above the current crediting rate
- Long Term Care Settlement Option included with policy
- Flexible payments — Single Payment, 7, 20, 30 years, or Pay to age 100
- Purchase through age 79 for members and spouses, and through age 23 for children and grandchildren

Value-Added Whole Life 35 Year Projection

Issued at age 45, 20 year payment plan, projected crediting rate of 6.8%, NOT guaranteed and subject to change.



Coverage Amounts and Monthly Premiums • 20 Year Payment Plan

Subject to complete terms and conditions of the policy.



ANNUITYLife

Great benefits of Value-Added Whole Life with minimal underwriting, regardless of age, sex or nicotine use.

- Minimal medical underwriting—only three questions
- Payment of single premium
- Option to annuitize the cash value immediately, at a later date, or never
- IF annuitized, guaranteed monthly payments to age 100, with an annual “bonus” check if Net Yield on Assets exceeds 4%
- Purchase before age 99

**Call for a Projection—
1-877-398-2263**

AAFMAA proudly serves all members of the U.S. Armed Forces and their families.



All AAFMAA policies offer these valuable features:

- NO war clause, NO aviation clause, NO terrorist clause
- Continues after separation or retirement from the military
- Survivor Assistance Services included with every member's policy
- No coverage limitations based upon rank or deployment status
- Coverage up to \$800,000



Survivor Assistance Services

At the heart of our 133 year tradition “to aid the families of the deceased members in a prompt, simple, and substantial manner,” and included with every member's policy, are AAFMAA's unique Survivor Assistance Services, including:

- Expeditious payment of the death benefit
- Claims initiation, plus continuous follow-up
- Claims representation, plus follow-up in disputes
- Lifetime individualized benefit notification
- Social Security notification
- Financial Awareness Service
- Annual statement of spouse entitlements

We take the pain out of the process.

AAFMAA
Life Insurance

Term Insurance

■
Whole Life

■
ANNUITYLife



**Army and Air Force
Mutual Aid Association**

102 Sheridan Avenue
Fort Myer, VA 22211-1110

INSURANCE SALES: 1-877-398-2263
Monday–Friday, 8:30 am–7:00 pm ET

MAIN OFFICE HOURS:
Monday–Friday, 8:30 am–4:30 pm ET

TOLL FREE: 1-800-522-5221

LOCAL: 703-707-4600

FAX: 703-522-1336

E-MAIL: info@aafmaa.com

WEB SITE: www.aafmaa.com

AAFMAA
Financial Advisors

Advice

■
Survivor Services

■
Veterans' Benefits



Yes!

Please send me complete information and an application for the insurance policies checked below:

MEMBER

SPOUSE

☐☐

Level Term I:

Save up to 27% over SGLI. Level coverage to age 50 (40 for nicotine users).

☐☐

Level Term II:

Save thousands over VGLI. Ideal for maturing families and retirees—short and long term coverage (5 to 30 years) can last to age 85.

☐☐

Value-Added Whole Life:

Permanent insurance with guaranteed cash value and death benefit. Attractive crediting rate. Long Term Care Settlement Option. Fixed premiums.

☐☐

ANNUITY Life:

Permanent insurance with option to annuitize cash value immediately. Minimal medical underwriting. Single Payments only. Designed for older insureds.

CHILD

GRANDCHILD

☐☐

Value-Added Whole Life:

Permanent insurance for children/grandchildren ages 6 months – 23 years.

☐☐

Generations Plus:

Permanent insurance up to \$30,000 for children 15 days through age 12. Coverage automatically doubles at age 21 with no increase in premiums.

☐☐

Level Term I:

Term insurance for children/grandchildren ages 18-23. Level coverage to age 50 (40 for nicotine users).

Coverage Desired:

Member: \$ _____ DOB: _____ (mm/dd/yy)

Spouse: \$ _____ DOB: _____ (mm/dd/yy)

Child/Grandchild \$ _____ DOB: _____ (mm/dd/yy)

Child/Grandchild \$ _____ DOB: _____ (mm/dd/yy)

Personal Information:

NICOTINE USE: (last 12 months) YOU: ☐ Yes ☐ No SPOUSE: ☐ Yes ☐ No

Check all that apply

- ☐ Army
- ☐ Air Force
- ☐ Marine Corps
- ☐ Navy
- ☐ Coast Guard

- ☐ Active or
- ☐ Retired

- ☐ Guard
- ☐ Reserve

- ☐ Veteran (any service—FL, HI, MD, NC, OK, SC and VA residents only)

Name: _____

Rank: _____

Member # (if applicable) _____

Spouse's Name: _____

Child/Grandchild's Name: _____

Child/Grandchild's Name: _____

Mailing Address: _____

City, State, Zip: _____

Email: _____

Phone: (recommended) _____ ☐ Day ☐ Evening

Call Toll-Free—1-877-398-2263
www.aafmaa.com

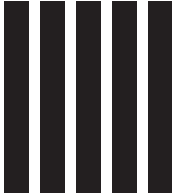


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