

**Audited Financial Statements
and Supplementary Information**

AIR FORCE AID SOCIETY, INC.

December 31, 2013

Air Force Aid Society, Inc.

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T A T E



T R Y O N

A Professional Corporation

Certified Public

Accountants

and Consultants

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2021 L STREET, NW

.....

SUITE 400

.....

WASHINGTON, DC

20036

.....

TELEPHONE

202/293-2200

.....

FACSIMILE

202/293-2208

.....

WWW.TATETRYON.COM

Independent Auditor's Report on the Financial Statements

To the Board of Trustees
Air Force Aid Society, Inc.

We have audited the accompanying financial statements of the Air Force Aid Society, Inc. (the Society), which comprise the statements of financial position as of December 31, 2013 and 2012, and the related statements of activities and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Air Force Aid Society, Inc. as of December 31, 2013 and 2012, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Washington, DC
July 18, 2014

Air Force Aid Society, Inc.

Statements of Financial Position

December 31,	2013	2012
Assets		
Cash and cash equivalents	\$ 3,945,572	\$ 3,096,639
Investments	176,533,831	157,046,599
Emergency assistance and education loans receivable, net	5,531,517	5,765,851
Pledges receivable	24,290	48,223
Other assets	183,422	121,020
Property and equipment, net	635,534	440,968
Total assets	\$ 186,854,166	\$ 166,519,300
Liabilities and net assets		
Liabilities		
Accounts payable and accrued expenses	\$ 356,749	\$ 212,851
Other liabilities	1,248,644	1,190,698
Total liabilities	1,605,393	1,403,549
Net assets		
Unrestricted	183,224,679	163,136,130
Temporarily restricted	237,290	229,817
Permanently restricted	1,786,804	1,749,804
Total net assets	185,248,773	165,115,751
Commitments and contingencies	-	-
Total liabilities and net assets	\$ 186,854,166	\$ 166,519,300

Air Force Aid Society, Inc.

Statements of Activities

Year Ended December 31,	2013	2012
Unrestricted activities		
Operating revenues		
Contributions:		
Air Force Assistance Fund	\$ 4,550,860	\$ 4,649,943
Other donations	2,575,750	1,902,810
Total contributions	7,126,610	6,552,753
Investment return designated for current operations	7,283,920	7,330,380
Miscellaneous income	6,624	71,061
Collections on loans previously written off	5,603	8,740
Net assets released from restriction	228,817	33,811
Total operating revenues	14,651,574	13,996,745
Expenses		
Program services		
Educational assistance	6,488,633	6,213,278
Emergency assistance	2,163,376	2,147,927
Community enhancement	1,853,834	2,163,515
Total program services expenses	10,505,843	10,524,720
Supporting services		
Management and general	1,338,243	1,207,999
Fundraising	565,863	674,302
Total supporting services	1,904,106	1,882,301
Total operating expenses	12,409,949	12,407,021
Change in unrestricted net assets from operations	2,241,625	1,589,724
Nonoperating activities		
Post-retirement benefits charges other than net periodic cost	(16,711)	(61,671)
Allowance for doubtful accounts estimate adjustment	-	28,438
Investment return in excess of amounts designated for current operations	17,875,635	10,938,277
Transfer to permanently restricted net assets	(12,000)	
Change in unrestricted net assets	20,088,549	12,494,768
Temporarily restricted activities		
Contributions	236,290	229,817
Net assets released from restriction	(228,817)	(33,811)
Change in temporarily restricted net assets	7,473	196,006
Permanently restricted activities		
Contributions	25,000	-
Transfer from unrestricted net assets	12,000	-
Change in permanently restricted net assets	37,000	-
Change in net assets	20,133,022	12,690,774
Net assets, beginning of year	165,115,751	152,424,977
Net assets, end of year	\$ 185,248,773	\$ 165,115,751

See notes to the financial statements.

Air Force Aid Society, Inc.

Statements of Cash Flows

Year Ended December 31,	2013	2012
Cash flows from operating activities		
Change in net assets	\$ 20,133,022	\$ 12,690,774
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Stock gifts	(94,337)	(6,861)
Depreciation and amortization	197,981	234,745
Bad debt expense	28,864	32,717
Net realized and unrealized gain on investments	(21,425,049)	(14,692,289)
Donated property and equipment	-	(8,680)
Changes in assets and liabilities:		
Emergency and education loans receivable	205,470	(302,610)
Pledges receivable	23,933	(20,912)
Other assets	(62,402)	(80,355)
Investment income receivable	(51,218)	(81,622)
Accounts payable	143,898	(18,570)
Other liabilities	57,946	65,582
Total adjustments	(20,974,914)	(14,878,855)
Net cash used in operating activities	(841,892)	(2,188,081)
Cash flows from investing activities		
Purchases of investments	(117,495,486)	(116,399,623)
Proceeds from sales and maturities of investments	119,578,858	119,096,632
Purchases of property and equipment	(392,547)	(197,846)
Net cash provided by investing activities	1,690,825	2,499,163
Net increase in cash and cash equivalents	848,933	311,082
Cash and cash equivalents, beginning of year	3,096,639	2,785,557
Cash and cash equivalents, end of year	\$ 3,945,572	\$ 3,096,639

See notes to the financial statements.

Air Force Aid Society, Inc.

Notes to the Financial Statements

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization: The Air Force Aid Society, Inc. (the Society), the official charity of the United States Air Force (USAF or Air Force), is incorporated under the laws of Virginia as a private, nonprofit organization. Its three-pronged charter promotes the Air Force mission by providing worldwide emergency assistance to members and their families, sponsoring education assistance programs, and offering a variety of base community enhancement programs that impact member/family welfare.

The Society operates worldwide at every major USAF installation. The Society's programs to provide relief loans and grants are administered, in part, by the USAF Airman and Family Readiness Centers located at these bases.

Income taxes: The Society is exempt from payment of income taxes under the provisions of Section 501(c)(3) of the Internal Revenue Code. The Society believes that it has appropriate support for income tax positions taken. Therefore, management has not identified any uncertain income tax positions. Generally, income tax returns related to the current and three prior years remain open for examination by taxing authorities.

Basis of accounting: The accompanying financial statements of the Society are presented on the accrual basis of accounting. Consequently, revenue is recognized when earned and expense is recognized when the obligation is incurred.

Use of estimates: Preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from those estimates.

Cash and cash equivalents: Cash on-hand, deposits in banks, and short-term highly liquid debt instruments with original maturities of three months or less are considered to be cash and cash equivalents. Money market investments managed at the discretion of the investment manager are considered to be investments.

Emergency assistance and education loans receivable: Loans receivable are reviewed for potential write off when the loan is 90 to 120 days past due. The Society wrote off \$31,184 and \$28,271 of loans receivable in 2013 and 2012, respectively. The allowance for doubtful accounts amounts to \$54,558 and \$56,877 for the years ended December 31, 2013 and 2012, respectively. During the year ended December 31, 2012, the Society adjusted the estimate for the allowance for doubtful accounts from 1.5% to 1.0% of the outstanding emergency assistance and education loans receivable, resulting in a \$28,438 increase to the change in net assets. There was no change in the percentage estimate for the allowance for the year ended December 31, 2013.

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

Investments: Investments consist of equity and fixed income securities, real estate funds, hedge funds, a private equity fund, and money market funds. All the investments, except money market funds, are carried at fair value and are held for long-term purposes to provide continuous funding in support of the Society's mission. The money market funds are carried at cost. Investments in publicly traded securities are reflected in the financial statements at fair value based on quoted market prices. The hedge funds and a private equity fund contain commingled trusts, which are not listed on national markets or over-the-counter markets and for which quoted market prices are not readily available. Management estimates of the fair value of these investments in commingled trusts are based on the net asset value, unless additional adjustments are deemed warranted by management. The net asset values are provided by the fund administrator and external investment managers and may include information based on historical cost appraisals, obtainable prices for similar assets, or other estimates.

Property and equipment: Purchases of property in excess of \$1,000 are capitalized. Depreciation of property is provided on the straight-line basis over the estimated service lives of the assets, which range from three to eight years. Capitalized Software is included in property and equipment and is amortized over the estimated service life of the software, which is three years. Donated property is recorded at its fair value at the date of donation. Leasehold improvements are recorded at cost and are amortized over the remaining life of the lease, which is currently scheduled to end on August 31, 2018.

Net assets: Net assets, revenues, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, the net assets of the Society and changes therein are classified and reported as follows:

Unrestricted: Unrestricted net assets include those net assets whose use is not restricted by donors, even though their use may be limited in other respects, such as by Board designation. The unrestricted net assets of the Society consist only of undesignated net assets, which are funds currently available to support the Society's daily operations.

Temporarily restricted: Temporarily restricted net assets include those net assets whose use has been donor restricted by specified purpose limitations or by the passage of time.

Permanently restricted: Permanently restricted net assets include those net assets whose use has been limited by donor-imposed restrictions that neither expire by the passage of time nor can be fulfilled or otherwise removed by actions of the Society.

Contributions: The Society receives contributions from Air Force members through the Air Force Assistance Fund (AFAF) (see note below). Revenue is recognized in the period in which the Society is notified by the AFAF of amounts received on its behalf. Other contributions are received directly from individuals and organizations and may include unconditional promises to give (pledges), which are recognized as revenue in the period received or when the promise is made.

When donor restrictions are met by actions of the Society and/or the passage of time, related net assets are reclassified to unrestricted and reported in the statements of activities as net assets released from restrictions.

Contributions with donor-imposed restrictions that are met in the same year as received are reported as unrestricted revenues.

Air Force Aid Society, Inc.

Notes to the Financial Statements

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

The Air Force Assistance Fund – Annual Campaign: The Society is one of four affiliates of the Air Force Assistance Fund (AFAF). The annual AFAF Campaign, which is managed within the Air Force, includes solicitation on behalf of the Society. Air Force members are able to designate which affiliate will receive their donation and are encouraged to contribute through payroll deductions/allotment. This annual campaign is the primary source of donations to the Society and supports the “Airmen helping Airmen” philosophy on which the Society was founded.

Contributed services: Services provided by the USAF Airman and Family Readiness Center staff are not recorded in the accompanying statements of activities since they do not require specialized skills as defined by U.S. generally accepted accounting principles. As a result of the 2003 Defense Authorization Bill, the Department of the Air Force was given the authorization to pay certain space and services costs for the benefit of the Society. This included \$191,755 and \$269,721 in rent-related costs for 2013 and 2012, respectively. The Society also received and recorded \$0 and \$8,680 in donated computer equipment in 2013 and 2012, respectively. The Society capitalizes any equipment donated by the Air Force that meets the \$1,000 capitalization threshold, expensing \$8,782 and \$8,546 in related depreciation during the years ended December 31, 2013 and 2012, respectively. A total of \$191,755 and \$278,401 of in-kind donations were received in 2013 and 2012, respectively, and are recorded as other donations in the statements of activities.

Measure of operations: The Society defines operations as all revenues and expenses that are an integral part of its current year programs and supporting activities. Investment returns in excess (deficit) of the Society’s aggregate board-authorized spending guideline, if any, plus the unexpended portion of the current year’s temporarily restricted contributions are recognized as a nonoperating activity.

The Society follows a total return spending guideline that is based on a 36 month moving average of the investment portfolio’s monthly fair value. The long-term target for the spending guideline is set by the Finance Committee and for 2013 and 2012 was 4.88% and 5.21%, respectively. The Finance Committee reviews the distribution rate and dollar amount annually.

Functional expenses: Expenses of the Society are reported on a functional basis, dividing costs between program services and support services. The three functional departments under program services are: emergency assistance, education assistance, and community enhancement programs. The two departments under support services are: management and general support and fundraising. The Society uses a head count allocation system to spread certain operational expenditures, including staffing costs, across the five functional units of the organization.

Program and supporting services: The Society’s operations include the following programs and supporting services:

Emergency Assistance – This program provides interest free loans and grants to Air Force members, retirees, and widows based on the individual situation. These loans and grants are provided to meet immediate financial needs in an emergency situation as a step toward a lasting solution to a problem. The Society started a new Falcon Loan program in March 2008 to make emergency assistance funds more easily accessible to Air Force members in need by streamlining the application process. The Falcon loan program initially provided interest-free loans of up to \$500 to active duty Air Force members to be used for emergency financial needs. During the year ended December 31, 2012, the loan maximum limit for a Falcon loan was increased to \$750.

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

Educational Assistance – Educational assistance has two major programs (see note F)

Spouse Tuition Assistance Program (STAP) – This community-oriented program provides tuition assistance grants to spouses that accompany active duty members on their overseas assignments. STAP motivates spouses to accompany members in overseas locations where they will have the opportunity to take on-base classes that may enhance their potential for employment upon returning to the United States. STAP is also a helpful morale-building tool for commanders who want spouses to feel active and engaged in base activities and have forums where spouses can interact. The STAP program was terminated in July 2012. Spouses who utilized the program can now receive education support through the General H.H. Arnold grant program.

General H.H. Arnold Education Grant Program – This program provides need-based grants to sons, daughters, and spouses of Air Force members that are enrolled full-time in undergraduate programs. To ensure an unbiased selection, the Society contracts with Scholarship America for the determination of financial need, selection of grant recipients, and the final disbursement services.

Community Enhancement – This program involves programs in four main areas: Child Care, Parenting, Readiness (phone cards and vehicle safety checks), and Spouse/Youth (education/orientation/job skills). These programs are designed to improve quality of life and meet current and emerging needs of Air Force members during all stages of their career/life.

Management and General – Management and general expenses include those costs that provide for the overall support and direction of the Society.

Fundraising – Fundraising activities include providing support materials for the AFAF Campaign in addition to publicizing and conducting other fundraising activities that may involve soliciting contributions from individuals, corporations, and others. These costs also include the costs of the Society's biggest fundraising event, the US Air Force Charity Ball, which generated \$717,021 and \$655,827 for the Society during the years ended December 31, 2013 and 2012, respectively.

Subsequent events: Subsequent events have been evaluated through July 18, 2014, which is the date the financial statements were available to be issued.

B. CONCENTRATIONS

Credit risk: The Society maintains demand deposits with commercial banks and money market funds with financial institutions. At times, certain balances held within these accounts may not be fully guaranteed or insured by the U.S. federal government. The uninsured portions of cash and money market accounts are backed solely by the assets of the underlying institution. As such, the failure of an underlying institution could result in financial loss to the Society.

Market value risk: The Society also invests funds in a professionally managed portfolio that contains various securities detailed in Note C. The portfolio includes professionally managed hedge and private equity funds which are reported at their estimated fair value as determined by the fund managers. Management believes the fund managers' estimates to be reasonable approximations of the fair values of the hedge funds. Such investments are exposed to various risks, such as fluctuations in market value and credit risk. Thus, it is at least reasonably possible that changes in these risks in the near term could materially affect investment balances and the amounts reported in the financial statements.

Air Force Aid Society, Inc.

Notes to the Financial Statements

C. INVESTMENTS

In accordance with generally accepted accounting principles, the Society uses the following prioritized input levels to measure fair value. The input levels used for valuing investments are not necessarily an indication of risk.

Level 1 – Observable inputs that reflect quoted prices for identical assets or liabilities in active markets such as stock quotes;

Level 2 – Includes inputs other than level 1 inputs that are directly or indirectly observable in the marketplace such as yield curves or other market data; and

Level 3 – Unobservable inputs which reflect the reporting entity's assessment of the assumptions that market participants would use in pricing the asset or liability including assumptions about risk such as bid/ask spreads and liquidity discounts.

Investments are recorded at fair value and consist of the following at December 31,:

2013	Total	Level 1	Level 2	Level 3
Investments, at fair value				
<u>Equity investment fund</u>				
Common stock	\$ 94,320,137	\$ 7,852,053	\$ 86,468,084	\$ -
<u>Fixed income fund</u>				
Corporate bonds and notes	9,713,020		9,713,020	
U.S. Treasury and federal agencies	19,325,327		19,325,327	
Aggregate bond index fund	3,840,018		3,840,018	
Fixed income mutual fund	11,699,288	11,699,288		
<u>Alternative investment fund</u>				
Hedge funds	12,716,233			12,716,233
Real estate investment trust	17,443,945		4,180,910	13,263,035
Private equity fund	1,880,715			1,880,715
Investment income receivable	518,868	518,868		
	171,457,551	20,070,209	123,527,359	27,859,983
Investments, at cost				
Money market funds	5,076,280			
Total Investments	\$ 176,533,831			

Air Force Aid Society, Inc.

Notes to the Financial Statements

C. INVESTMENTS - CONTINUED

2012	Total	Level 1	Level 2	Level 3
Investments, at fair value				
<u>Equity investment fund</u>				
Common stock	\$ 87,192,368	\$ 11,397,812	\$ 75,794,556	\$ -
<u>Fixed income fund</u>				
Corporate bonds and notes	10,587,992		10,587,992	
U.S. Treasury and federal agencies	21,069,491		21,069,491	
Aggregate bond index fund	5,139,929		5,139,929	
Fixed Income Mutual Fund	11,202,083	11,202,083		
<u>Alternative Investment Fund</u>				
Hedge Funds	9,974,597			9,974,597
Real estate investment trust	8,483,789		8,483,789	
Private equity fund	674,523			674,523
Investment income receivable	467,650	467,650		
	154,792,422	23,067,545	121,075,757	10,649,120
Investments, at cost				
Money market funds	2,254,177			
Total Investments	\$ 157,046,599			

Level 3 investments are reconciled as follows for the year ended December 31,:

	2013	2012
Beginning balance	\$ 10,649,120	\$ 4,947,916
Purchases	15,254,597	5,294,659
Sales	(218,231)	(158,279)
Realized and unrealized gains	2,174,497	564,824
Ending balance	\$ 27,859,983	\$ 10,649,120

Investments using Level 2 inputs consist of index funds, corporate bonds, government agency securities, and real estate investment trusts. The real estate investment trust is classified as Level 2 based on the ability of the Society to redeem amounts at a net assets value (NAV) per share in the short-term. The index funds and real estate investment trust are priced by determining the net asset value of the fund using an outside pricing vendors. The fixed income securities are priced using the outside pricing vendor. In determining the fair value of the investments, Northern Trust uses a market approach and prices assets using multiple prices, types of bid/offer, last traded, settlement, evaluated and the official primary exchange close-time pricing. Management believes Northern Trust's estimate to be a reasonable approximation of the fair value of the investments.

Investments using Level 3 inputs consist of two hedge funds of funds, real estate investment trust and a private equity fund. The fair values of these investments are determined based on the fair values of the underlying investments as determined by the fund managers. Management monitors the reports provided by the fund managers and believes the estimates of fair value to be an approximation of the exit price for these investments.

Air Force Aid Society, Inc.

Notes to the Financial Statements

C. INVESTMENTS – CONTINUED

Investments recorded at cost include money market funds. Investments at cost are not required to be classified in one of the levels prescribed by the fair value hierarchy.

Investment income consists of the following for the years ended December 31,:

	2013	2012
Interest	\$ 1,787,989	\$ 1,930,021
Net realized and unrealized gain on investments	21,425,049	14,692,289
Dividends	2,367,312	2,013,362
Investment supervision fee	<u>(420,795)</u>	<u>(367,015)</u>
Total net investment income	<u>\$ 25,159,555</u>	<u>\$ 18,268,657</u>
Investment return designated for current operations	7,283,920	7,330,380
Investment return in excess of amounts designated for current operations	<u>17,875,635</u>	<u>10,938,277</u>
Total net investment income	<u>\$ 25,159,555</u>	<u>\$ 18,268,657</u>

The following presents further information regarding the composition of the Society's alternative investments at December 31, 2013:

Alternative Investment	Fair Value	Unfunded Commitments	Redemption Frequency	Redemption Notice Period
Commonfund Multi-Strategy Global Hedged Partners	\$ 6,385,311	\$ -	See (a) below	See (a) below
Northern Trust Alpha Strategies Fund	6,330,922	-	See (b) below	See (b) below
SSgA Tuckerman Global Real Estate Real Estate Securities Index Non-Lending Strategy	4,180,910	-	See (c) below	See (c) below
Commonfund Capital Partners V	1,880,715	9,130,000	See (d) below	See (d) below
UBS Trumbull Property Fund	13,263,035	-	See (e) below	See (e) below

(a) Commonfund Multi-Strategy Global Hedged Partners

Commonfund Multi-Strategy Global Hedged Partners include investments in a hedge fund. The investment objective of the fund is to provide equity-like returns with substantially reduced volatility over a full market cycle. The fund attempts to achieve its investment objective by investing in other collective investment funds which have characteristics consistent with the Fund's overall investment objective. A notice period of 90 calendar days is required to redeem shares semi-annually on June 30 and December 31.

(b) Northern Trust Alpha Strategies Fund

Northern Trust Alpha Strategies Fund is a fund-of-funds that seeks to achieve attractive, risk adjusted returns with low volatility. A notice period of 60 days written notice is required to redeem shares. The fund generally pays 100% of partial redemption 30 days after the redemption date on a quarterly basis and 95% of a full redemption within 30 days after the redemption date with the balance paid after the completion of the Fund's fiscal year audit.

C. INVESTMENTS – CONTINUED

(c) SSgA Tuckerman Global Real Estate Securities Index Non-Lending Strategy

SSgA Tuckerman Global Real Estate Securities Index Non-Lending Strategy investments is managed using a passive investment strategy, investing most of its assets in equity securities of Real Estate Investment Trusts (REITs) and Real Estate Operating Companies (REOCs). The investment objective of the fund is to seek an investment return that approximates as closely as practicable, before expenses, the performance of its benchmark index over the long term. A notice period of 15 days is required to redeem significant shares; however there are no limits on the frequency of the Society to redeem shares.

(d) Commonfund Capital Partners V

Commonfund Capital Partners V is a partnership that manages a broadly diversified multi-strategy program that provides access to US private equity, global private equity, and global venture capital investments. The Society is a limited partner in this partnership that strives to provide a solid return of capital. This is an illiquid investment and redemptions are not permitted. Quarterly distributions will be made by the partnership as individual investments reach maturity.

(e) UBC Trumbull Property Fund

The UBS Trumbull Property Fund is a partnership that actively manages a core portfolio of equity real estate. The fund seeks to provide attractive returns while limiting downside risk. The Society is a limited partner in the fund. Redemptions are allowed on a quarterly basis with 60 days notice and may be subject to a redemption queue.

D. PROPERTY AND EQUIPMENT

Property and equipment consisted of the following at December 31,:

	2013	2012
Furniture and equipment	\$ 304,398	\$ 365,320
Capitalized software	1,295,533	1,140,446
Computer equipment	85,708	110,849
Leasehold improvements	<u>353,533</u>	<u>219,921</u>
	2,039,172	1,836,536
Less accumulated depreciation and amortization	<u>(1,403,638)</u>	<u>(1,395,568)</u>
	<u>\$ 635,534</u>	<u>\$ 440,968</u>

Air Force Aid Society, Inc.

Notes to the Financial Statements

E. POSTRETIREMENT BENEFITS

The Society provides life insurance benefits to retired employees. The Society accounts for these benefits in accordance with the provisions of the accounting standards topic regarding postretirement benefits other than pensions, which requires that the expected cost of these benefits be recognized during the years in which employees render service. The plan is not funded and therefore has no assets. The unfunded status of this post-retirement plan is included as a liability in the Statements of Financial Position. The measurement date for the valuation is December 31.

The net postretirement benefit expense recognized for the years ended December 31, 2013 and 2012 included the following components:

	2013	2012
Service cost for benefits earned during the year	\$ 8,460	\$ 7,249
Interest cost on accumulated postretirement benefit obligation	<u>21,367</u>	<u>21,046</u>
Total postretirement benefit expense	29,827	28,295
Change in actuarial assumptions	(16,492)	30,696
Actuarial loss	33,203	30,975
Contributions paid on behalf of current retired participants	<u>(39,268)</u>	<u>(37,267)</u>
Change in accrued postretirement benefit cost	<u>\$ 7,270</u>	<u>\$ 52,699</u>

The following table shows the plan's obligation as well as the liability recognized in the Society's statements of financial position at December 31,:

	2013	2012
Retirees	\$ 287,358	\$ 272,761
Other active participants	<u>186,280</u>	<u>193,607</u>
Accrued postretirement benefit cost	<u>\$ 473,638</u>	<u>\$ 466,368</u>
Weighted average assumed discount rate	4.75%	4.5%
Rate of salary increase assumed	2.5%	2.5%

The expected future benefit payments are as follows:

Year Ending December 31,	Amount
2014	\$ 20,900
2015	22,200
2016	23,100
2017	24,500
2018	25,500
2019 - 2023	<u>143,600</u>
	<u>\$ 259,800</u>

Air Force Aid Society, Inc.

Notes to the Financial Statements

F. EDUCATIONAL PROGRAM EXPENSES

Educational program expenses consisted of the following for the years ended December 31,:

	2013	2012
General H.H. Arnold Education Grants	\$ 5,692,119	\$ 5,175,289
Educational Program Administration	796,514	818,300
Spouse Tuition Assistance Grants		219,689
	<u>\$ 6,488,633</u>	<u>\$ 6,213,278</u>

G. RETIREMENT PLAN

The Society has a defined contribution pension plan in which all employees participate. Bi-weekly employer contributions were equal to 9% of participants' gross compensation as defined in the plan for both 2013 and 2012. During 2013 and 2012, the Society contributed \$168,424 and \$165,037, respectively, to this plan.

In addition, the Society sponsors a 403(b) plan available to all employees, allowing them to set aside for retirement a portion of their compensation on a pre-tax basis. No employer contributions are made through the Society's 403(b) plan and participation in the plan is voluntary.

H. NET ASSETS

Temporarily restricted: The December 31, 2013 balance of temporarily restricted net assets is \$237,290, which is comprised of \$24,290 which is time-restricted and \$213,000, which is restricted for use on specific Society programs. The December 31, 2012 balance of temporarily restricted net assets is \$229,817, which is comprised of \$48,223 which is time-restricted and \$181,594 which is restricted for use on specific Society programs.

Permanently restricted: Permanently restricted net assets at December 31, 2013 and 2012 are held to provide earnings to pay scholarships under the General H.H. Arnold Education Grant Program.

Notes to the Financial Statements

I. ENDOWMENT

The Society's Education Grant endowment consists of one fund held to provide earnings to pay scholarships under the General H.H. Arnold Education Grant Program. The Education Grant endowment is donor-restricted to be held in perpetuity. All returns generated by the restricted funds are used to fund the grants on an annual basis. As required by accounting principles generally accepted in the United States of America, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

Interpretation of Relevant Law

The Society has interpreted the *Uniform Prudent Management of Institutional Funds Act of 2008 (UPMIFA)* enacted by the General Assembly of the Commonwealth of Virginia as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Society classifies as permanently restricted net assets (1) the original value of gifts donated to the permanent endowment, (2) the original value of subsequent gifts to the permanent endowment, and (3) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Society in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Society considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- (1) The duration and preservation of the fund
- (2) The purposes of the organization and the donor-restricted endowment fund
- (3) General economic conditions
- (4) The possible effect of inflation and deflation
- (5) The expected total return from income and the appreciation of investments
- (6) Other resources of the Society
- (7) The investment policies of the Society

Changes in endowment net assets for the year ended December 31, 2013:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Balances at January 1, 2013	\$ -	\$ -	\$ 1,749,804	\$ 1,749,804
Contributions			25,000	25,000
Investment return:				
Interest and dividends		41,820		41,820
Investment fees		(4,259)		(4,259)
Net appreciation (realized and unrealized)		216,856		216,856
Total investment return	-	254,417	25,000	279,417
Appropriation of endowment assets for expenditure		(254,417)		-
Transfer from unrestricted			12,000	12,000
Balances at December 31, 2013	\$ -	\$ -	\$ 1,786,804	\$ 1,786,804

Air Force Aid Society, Inc.

Notes to the Financial Statements

I. ENDOWMENT – CONTINUED

Changes in endowment net assets for the year ended December 31, 2012:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Balances at January 1, 2012	\$ (1,218)	\$ -	\$ 1,749,804	\$ 1,748,586
Investment return:				
Interest and dividends		43,819		43,819
Investment fees		(4,089)		(4,089)
Net appreciation (realized and unrealized)		163,701		163,701
Total investment return	\$ (1,218)	203,431	-	203,431
Appropriation of endowment assets for expenditure		(202,213)		(202,213)
Transfer from reserve to preserve donor restricted fund value	1,218	(1,218)		-
Balances at December 31, 2012	\$ -	\$ -	\$ 1,749,804	\$ 1,749,804

Funds with deficiencies

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that current law requires the Society to retain for a fund of perpetual duration. In accordance with accounting principles generally accepted in the United States of America, deficiencies of this nature are reported in unrestricted net assets. Such deficiencies may result from unfavorable market fluctuations. There were no deficiencies as of December 31, 2013 and 2012.

Return objectives and risk parameters

The Society has adopted investment and spending policies for its consolidated investment portfolio reserve funds of which a small portion of these assets are endowed for a particular purpose by donors. The investment policy seeks a long-term rate of return on the portfolio that ensures that the growth of the Society's assets will be sufficient to offset or exceed inflation, required program spending, investment management fees, and operating expenses, over a full market cycle. The Society has a low to moderate risk philosophy, but recognizes the need for higher long-term results to fund the current level of program spending. The investment policy calls for a diverse portfolio utilizing various asset classes with a goal of reducing volatility and risk. All returns generated by the permanently-restricted Education Grant funds are used to fund the named education grants set up by the donor, with excess returns used to fund additional grants distributed by the program during the year.

Strategies employed for achieving objectives

To satisfy its long-term rate-of-return objectives, the Society relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Society targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints. The permanently restricted Education Grant endowment funds are a subset of the total investment fund held by the Society. The total reserve fund balances were \$176,533,831 and \$157,046,599, respectively, for the years ended December 31, 2013 and 2012.

Air Force Aid Society, Inc.

Notes to the Financial Statements

I. ENDOWMENT – CONTINUED

Spending policy and how the investment objectives relate to spending policy

The Society has a policy of maintaining the full historical value of the permanently restricted endowments. As of December 31, 2013, the full investment portfolio is invested using a target asset mix of 48% equity, 27% fixed income securities and cash, and 25% alternative investments, per the Board approved investment policy, in an effort to generate returns to cover the long-term spending target of 5.0%. Included in the 5%, the total return generated by the permanently restricted funds is used each year to fund the education grants designated by donor restriction. The distribution rate and dollar amount of the Society's spending plan is reviewed annually by the Finance Committee as part of the normal budget process.

J. OFFICE LEASE COMMITMENT

The Society has a non-cancelable operating lease to rent office space, which expires in August 2018. The Society's 2013 and 2012 rental expense was \$274,671 and \$260,590, respectively. In accordance with Section 1066 (Provision of Space and Services to Military Welfare Societies) of the 2003 Defense Authorization Bill, the Air Force was given authorization to pay the Society's lease obligations effective May 1, 2003. The Air Force paid the Society's lease in both 2013 and 2012, therefore, the Society records this rent payment as contribution revenue – other donations and rent expense in the accompanying statements of activities.

The future minimum rental payments due are as follows:

Year Ending December 31,	Amount
2014	207,529
2015	282,231
2016	288,581
2017	295,075
2018	199,645
	\$ 1,273,061

T A T E



T R Y O N

A Professional Corporation

Certified Public

Accountants

and Consultants

Independent Auditor's Report on Other Financial Information

To the Board of Trustees
Air Force Aid Society, Inc.

We have audited the financial statements of the Air Force Aid Society, Inc. (the Society) as of and for the years ended December 31, 2013 and 2012 and issued our report thereon dated July 18, 2014 which contained an unmodified opinion on those financial statements. Our audit was performed for the purpose of forming an opinion on the financial statements as a whole. The other financial information on the following pages is presented for the purposes of additional analysis 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 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.

Washington, DC
July 18, 2014

2021 L STREET, NW

SUITE 400

WASHINGTON, DC

20036

TELEPHONE

202/293-2200

FACSIMILE

202/293-2208

Air Force Aid Society, Inc.

Schedule of Functional Expenses Year Ended December 31, 2013

	Program Services				Supporting Services			Total
	Emergency Assistance	Educational Assistance	Community Enhancement	Total Program Services Expenses	Management and general	Fundraising	Total Supporting Services Expenses	
Grants and conversions	\$ 663,133	\$ 5,691,894	\$ 1,624,995	\$ 7,980,022	\$ -	\$ -	\$ -	\$ 7,980,022
Salary and benefits	1,104,812	341,694	173,695	1,620,201	979,521	247,728	1,227,249	2,847,450
Bad debt expense	28,864			28,864			-	28,864
Education grant program fees		346,563		346,563			-	346,563
Occupancy	106,572	32,961	16,755	156,288	94,487	23,896	118,383	274,671
Fundraising				-		239,488	239,488	239,488
Professional services	36,232	11,206	5,696	53,134	32,125	8,124	40,249	93,383
After hours phone support	9,119			9,119	706		706	9,825
Miscellaneous	22,685	6,151	3,127	31,963	17,630	4,459	22,089	54,052
Depreciation and amortization	69,143	21,385	10,870	101,398	61,303	15,504	76,807	178,205
Printing and publications	6,767	889	452	8,108	2,547	644	3,191	11,299
Accounting fees				-	42,429		42,429	42,429
Maintenance agreements and contracts	23,773	7,353	3,738	34,864	21,077	5,331	26,408	61,272
IT systems upgrade and maintenance	54,422	16,832	8,556	79,810	48,250	12,203	60,453	140,263
Telephone	952	294	150	1,396	844	213	1,057	2,453
Insurance	19,057	5,894	2,996	27,947	16,896	4,273	21,169	49,116
Supplies	7,965	2,463	1,252	11,680	7,061	1,786	8,847	20,527
Postage	5,095	1,574	800	7,469	4,512	1,141	5,653	13,122
AFAS Board & Committee expenses	-		-	-	4,613		4,613	4,613
Travel	4,785	1,480	752	7,017	4,242	1,073	5,315	12,332
Total expenses by program	\$ 2,163,376	\$ 6,488,633	\$ 1,853,834	\$ 10,505,843	\$ 1,338,243	\$ 565,863	\$ 1,904,106	\$ 12,409,949
Percentage of total expenses	17%	52%	15%	84%	11%	5%	16%	100%

*The above Emergency Assistance "Grants and conversions" line reflects only \$663,132 in grants and none of the \$9.0 million in interest free loans issued during 2013, which per accounting rules remain a statement of financial position asset until paid off. In 2013, the Air Force Aid Society was able to assist 18,731 emergency assistance cases through a combination of grants and/or interest free loans.

Air Force Aid Society, Inc.

Schedule of Functional Expenses Year Ended December 31, 2012

	Program Services				Supporting Services			
	Emergency Assistance	Educational Assistance	Community Enhancement	Total Program Services Expenses	Management and general	Fundraising	Total Supporting Services Expenses	Total
Grants and conversions	\$ 742,625	\$ 5,394,978	\$ 1,894,108	\$ 8,031,711	\$ -	\$ -	\$ -	\$ 8,031,711
Salary and benefits	1,031,571	364,248	202,978	1,598,797	873,082	308,637	1,181,719	2,780,516
Bad debt expense	32,717			32,717			-	32,717
ACT fees		334,845		334,845			-	334,845
Occupancy	96,679	34,137	19,023	149,839	81,826	28,925	110,751	260,590
Fundraising				-		264,657	264,657	264,657
Professional services	33,552	11,847	6,602	52,001	28,398	10,038	38,436	90,437
After hours phone support	620			620	986		986	1,606
Miscellaneous	19,405	5,865	3,269	28,539	14,060	4,971	19,031	47,570
Depreciation and amortization	78,853	27,843	15,516	122,212	66,739	23,592	90,331	212,543
Printing and publications	7,374	2,604	1,451	11,429	6,241	2,206	8,447	19,876
Accounting fees				-	43,933		43,933	43,933
Maintenance agreements and contracts	27,007	9,536	5,314	41,857	22,858	8,080	30,938	72,795
IT systems upgrade and maintenance	47,544	16,788	9,355	73,687	40,241	14,225	54,466	128,153
Insurance	12,837	4,533	2,526	19,896	10,864	3,841	14,705	34,601
Supplies	6,598	2,330	1,298	10,226	5,585	1,974	7,559	17,785
Postage	5,142	1,816	1,012	7,970	4,352	1,539	5,891	13,861
AFAS Board & Committee expenses				-	4,262		4,262	4,262
Travel	5,403	1,908	1,063	8,374	4,572	1,617	6,189	14,563
Total expenses by program	\$ 2,147,927	\$ 6,213,278	\$ 2,163,515	\$ 10,524,720	\$ 1,207,999	\$ 674,302	\$ 1,882,301	\$ 12,407,021
Percentage of total expenses	17%	50%	17%	85%	10%	5%	15%	100%

*The above Emergency Assistance "Grants and conversions" line reflects only \$742,625 in grants and none of the \$9.4 million in interest free loans issued during 2012, which per accounting rules remain a statement of financial position asset until paid off. In 2012, the Air Force Aid Society was able to assist 20,076 emergency assistance cases through a combination of grants and/or interest free loans.