

# **AARP Foundation**

**Consolidated Financial Statements  
December 31, 2005 and 2004  
Together With Independent Auditors' Report**

**AARP Foundation**  
Consolidated Financial Statements  
December 31, 2005 and 2004

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**KPMG LLP**  
2001 M Street, NW  
Washington, DC 20036

## **Independent Auditors' Report**

The Board of Directors of the  
AARP Foundation:

We have audited the accompanying consolidated statements of financial position of the AARP Foundation as of December 31, 2005 and 2004, and the related consolidated statements of activities and cash flows for the years then ended. These consolidated financial statements are the responsibility of the AARP Foundation's management. Our responsibility is to express an opinion on these consolidated 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 includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the AARP Foundation's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the AARP Foundation as of December 31, 2005 and 2004, and the changes in its net assets and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Our audits were made for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The supplementary information included in the Schedule of Functional Expenses is presented for purposes of additional analysis and is not a required part of the basic consolidated financial statements. Such information has been subjected to the auditing procedures applied in the audit of the 2005 basic consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the 2005 basic consolidated financial statements taken as a whole.

**KPMG LLP**

March 31, 2006

**AARP Foundation**  
**Consolidated Statements of Financial Position**  
**As of December 31, 2005 and 2004**  
(in thousands)

	<b>2005</b>	<b>2004</b>
<b>Current assets:</b>		
Cash and cash equivalents	\$ 48,678	\$ 27,905
Deposit held with trustee (Note 7)	1,802	240
Contributions receivable (Note 6)	400	300
Grants receivable (Note 3)	3,685	5,054
Due from affiliates (Note 10)	14,946	7,361
Prepaid expenses and other assets	957	247
Total current assets	70,468	41,107
<b>Noncurrent assets:</b>		
Property and equipment, net (Note 4)	21,462	22,004
Deposit held with trustee (Note 7)	-	2,116
Investments (Note 5)	17,168	16,348
Charitable gift annuity investments (Note 5)	7,929	6,720
Contributions receivable (Note 6)	869	898
Debt issuance costs	495	512
Total noncurrent assets	47,923	48,598
Total assets	\$ 118,391	\$ 89,705
<b>Current liabilities:</b>		
Accounts payable and accrued expenses (Note 12)	\$ 13,216	\$ 5,925
Grants payable (Note 9)	1,292	236
Deferred revenue	1,825	87
Due to affiliates (Note 10)	8,753	664
Charitable gift annuity payable	681	530
Total current liabilities	25,767	7,442
<b>Noncurrent liabilities:</b>		
Due to AARP (Note 10)	1,550	1,550
Accrued pension (Note 11)	6,562	5,729
Charitable gift annuity payable	4,607	3,955
Bonds payable (Note 7)	25,000	25,000
Total noncurrent liabilities	37,719	36,234
Total liabilities	63,486	43,676
<b>Contingencies (Notes 10 and 15)</b>		
<b>Net assets:</b>		
Unrestricted:		
Undesignated	21,513	22,401
Board designated quasi-endowment	12,078	11,031
Board designated operating reserves (Note 2a)	8,256	-
Total unrestricted	41,847	33,432
Temporarily restricted (Note 14)	13,058	12,597
Total net assets	54,905	46,029
Total liabilities and net assets	\$ 118,391	\$ 89,705

See accompanying notes to financial statements.

**AARP Foundation**  
**Consolidated Statements of Activities**  
**Years ended December 31, 2005 and 2004**  
(in thousands)

	2005			2004		
	Unrestricted	Temporarily Restricted	Total	Unrestricted	Temporarily Restricted	Total
<b>Revenues:</b>						
Grant revenue (Note 8)	\$ 83,241	\$ -	\$ 83,241	\$ 81,813	\$ -	\$ 81,813
Related-party contributions (Note 10)	27,028	6,659	33,687	22,003	6,265	28,268
Charitable contributions	13,027	1,118	14,145	8,961	2,117	11,078
Change in value of charitable gift annuities	(464)	-	(464)	(378)	-	(378)
In-kind contributions (Note 2h)	15,035	-	15,035	15,569	-	15,569
Investment income (Note 5)	2,319	-	2,319	1,679	-	1,679
Litigation settlements and other	103	-	103	920	-	920
Net assets released from restrictions	7,316	(7,316)	-	3,273	(3,273)	-
<b>Total revenues</b>	<b>147,605</b>	<b>461</b>	<b>148,066</b>	<b>133,840</b>	<b>5,109</b>	<b>138,949</b>
<b>Expenses:</b>						
Program services (Note 9):						
SCSEP	90,347	-	90,347	90,714	-	90,714
Tax Counseling for the Elderly	10,411	-	10,411	5,587	-	5,587
Litigation services	5,195	-	5,195	4,775	-	4,775
Other programs	12,454	-	12,454	6,910	-	6,910
<b>Total program services</b>	<b>118,407</b>	<b>-</b>	<b>118,407</b>	<b>107,986</b>	<b>-</b>	<b>107,986</b>
Supporting services:						
Fundraising	14,641	-	14,641	5,936	-	5,936
Management and general	6,142	-	6,142	7,096	-	7,096
<b>Total supporting services</b>	<b>20,783</b>	<b>-</b>	<b>20,783</b>	<b>13,032</b>	<b>-</b>	<b>13,032</b>
<b>Total expenses</b>	<b>139,190</b>	<b>-</b>	<b>139,190</b>	<b>121,018</b>	<b>-</b>	<b>121,018</b>
<b>Change in net assets</b>	<b>8,415</b>	<b>461</b>	<b>8,876</b>	<b>12,822</b>	<b>5,109</b>	<b>17,931</b>
<b>Net assets, beginning of year</b>	<b>33,432</b>	<b>12,597</b>	<b>46,029</b>	<b>20,610</b>	<b>7,488</b>	<b>28,098</b>
<b>Net assets, end of year</b>	<b>\$ 41,847</b>	<b>\$ 13,058</b>	<b>\$ 54,905</b>	<b>\$ 33,432</b>	<b>\$ 12,597</b>	<b>\$ 46,029</b>

See accompanying notes to financial statements.

**AARP FOUNDATION**  
**Consolidated Statements of Cash Flows**  
**Years ended December 31, 2005 and 2004**  
**(in thousands)**

	<u>2005</u>	<u>2004</u>
<b>Cash flows from operating activities:</b>		
Change in net assets	\$ 8,876	\$ 17,931
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	651	196
Amortization of debt issuance costs	17	6
Net realized and unrealized gains on investments	(465)	(1,001)
Change in value of charitable gift annuities	464	378
Decrease (increase) in grants receivable	1,369	(3,150)
Increase in contributions receivable	(71)	(245)
Increase in due from affiliates	(7,585)	(5,313)
Increase in prepaid expenses and other assets	(710)	(13)
Increase (decrease) in accounts payable and accrued expenses	7,291	(752)
Increase in grants payable	1,056	236
Increase (decrease) in deferred revenue	1,738	(259)
Increase in charitable gift annuity payable	339	166
Increase (decrease) in due to affiliates	8,089	(68)
Increase in accrued pension payable	833	1,875
Total adjustments	<u>13,016</u>	<u>(7,944)</u>
Net cash provided by operating activities	<u>21,892</u>	<u>9,987</u>
<b>Cash flows from investing activities:</b>		
Purchase of property and equipment	(109)	(22,200)
Acquisition of charitable gift annuity investments	(1,040)	(783)
Purchase of investments	(533)	(12,289)
Proceeds from sales and maturities of investments	9	6,752
Net cash used in investing activities	<u>(1,673)</u>	<u>(28,520)</u>
<b>Cash flows from financing activities:</b>		
Proceeds from issuance of bonds	-	25,000
Debt issuance costs	-	(518)
Net bond proceeds transferred to trustee	-	(2,356)
Net bond proceeds transferred from trustee	554	-
Net cash provided by financing activities	<u>554</u>	<u>22,126</u>
<b>Net increase in cash and cash equivalents</b>	20,773	3,593
<b>Cash and cash equivalents, beginning of year</b>	<u>27,905</u>	<u>24,312</u>
<b>Cash and cash equivalents, end of year</b>	<u>\$ 48,678</u>	<u>\$ 27,905</u>
<b>Cash paid for interest</b>	<u>\$ 583</u>	<u>\$ 48</u>

See accompanying notes to financial statements.

**AARP Foundation**  
**Notes to Consolidated Financial Statements**  
**December 31, 2005 and 2004**

**1. Description of Organization**

The AARP Foundation was organized in 1961 as a District of Columbia not-for-profit corporation and is AARP's charitable organization dedicated to enhancing the quality of life for all as we age and to lead positive social change and value to those 50 and older with emphasis on those at social and economic risk. The AARP Foundation is a nonprofit organization qualified under Section 501(c)(3) of the Internal Revenue Code and is therefore exempt from federal income taxes on its charitable operations. In addition, the AARP Foundation is a public charity as defined in Section 509 (a)(2) of the Internal Revenue Code.

The AARP Foundation receives funding principally from the federal government, AARP, foundations, corporations, and individuals. The Foundation's Board of Directors is composed of eight members appointed by AARP's Board of Directors.

The AARP Institute (the Institute), a wholly owned subsidiary of the AARP Foundation, was organized in 1963 as a District of Columbia not-for-profit corporation. Like the AARP Foundation, the Institute is dedicated to enhancing the quality of life for all as we age and to lead positive social change and value to those 50 and older with emphasis on those at social and economic risk.

**2. Summary of Significant Accounting Policies**

**a) Basis of Presentation**

These consolidated financial statements include the accounts of AARP Foundation and the Institute (collectively, the AARP Foundation or Foundation). The Foundation prepares its financial statements on the accrual basis of accounting. The Foundation summarizes the costs of providing its various programs and other activities on a functional basis in the accompanying statements of activities. Accordingly, certain costs are allocated among program and supporting services based on specific identification or allocation methodologies.

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

*Unrestricted* – net assets that are not subject to donor-imposed stipulations including amounts designated by the Board of Directors to function as quasi-endowment and operating reserves. The level of operating reserves are reviewed annually by the Board of Directors as part of the budgeting process.

*Temporarily restricted* – net assets subject to donor-imposed stipulations that will be met either by actions of the Foundation and/or the passage of time.

**AARP Foundation**  
**Notes to Consolidated Financial Statements**  
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**b) Cash Equivalents**

All short-term deposits and investments with original maturities of three months or less are reported as cash equivalents. The Foundation has classified any cash or money market accounts held by external managers as investments.

**c) Investments**

Investments in fixed income and equity securities are reported at fair value based on quoted market prices. Classification of investments as noncurrent on the accompanying statements of financial position is determined by management based on intentions for use of the funds. Realized and unrealized gains or losses on investments are reported in the accompanying statements of activities within investment income. Interest and dividend income are recorded when earned.

**d) Property and Equipment**

Property, building improvements, and equipment are stated at cost, less accumulated depreciation. Management periodically evaluates whether events or circumstances have occurred indicating that the carrying amount of long-lived assets may not be recovered.

Depreciation is calculated using the straight-line method over the estimated useful lives of the assets, which are 26 years for the building, 10 years for building improvements, and 3 years for equipment. Land is not subject to depreciation. Maintenance and repair costs are expensed as incurred.

**e) Charitable Gift Annuities**

Charitable gift annuity agreements involve a contribution of assets with a corresponding annuity contract requiring payment to the donor or a designated beneficiary until his or her death.

The excess of the fair value of assets received over the present value of annuity payments to be made to the donor or beneficiary is recognized as contribution revenue. The assets held for all charitable gift annuities are reported in charitable gift annuity investments on the statements of financial position and stated at fair value. Gains and losses resulting from changes in actuarial assumptions are reported as increases or decreases in unrestricted net assets in the statements of activities. Liabilities for the expected annuity payments are reported at the estimated present value of future cash outflows, based on appropriate discount rates selected at the time of initial contribution and Internal Revenue Code mortality tables. The Foundation invests the charitable gift annuities in accordance with the limitations imposed by relevant state laws.

**AARP Foundation**  
**Notes to Consolidated Financial Statements**  
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In 2004, the AARP Board of Directors committed to assume the Foundation's charitable gift annuity liability in the event the Foundation is unable to fulfill its obligations.

**f) Grant Revenue**

Grant revenue is reported as exchange transactions and, accordingly, is recognized to the extent allowable expenses are incurred under program agreements. Amounts reported as grants receivable represent grant program expenses incurred in advance of the receipt of funds. Funds received in advance of grant program expenses are reported as deferred revenue in the statements of financial position.

**g) Contributions**

The Foundation reports contributions as revenue when received or pledged by the donor. The Foundation reports contributions as temporarily restricted revenue if such gifts are restricted by the donor to a specific program or include an implied time restriction.

Expirations of temporary restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as net assets released from restrictions. Gifts whose donor-stipulated purposes are met in the same year as received are reported as unrestricted revenue.

**h) Contributed Services**

A significant portion of the Foundation's contributed services involves the Senior Community Service Employment Program (SCSEP) through which the Foundation receives donated supervisory services. These contributed services are recorded at their estimated fair values as both revenues and expenses in the statements of activities.

Over 32,000 volunteers provide tax preparation assistance each year under the Tax Counseling for the Elderly program. These donated services are not recorded in the financial statements because they do not meet the requirements for recognition.

In addition, AARP contributes certain services and assets to the Foundation (see note 10).

**i) Litigation Settlement Revenue**

Litigation settlement revenue from lawsuits in which AARP Foundation attorneys participate is recognized when cash is received.

**AARP Foundation**  
**Notes to Consolidated Financial Statements**  
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**j) Use of Estimates**

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect reported amounts and disclosures in the financial statements. Actual results could differ from these estimates.

**k) Reclassifications**

Certain prior year amounts have been reclassified to conform to the current year presentation.

**3. Grants Receivable**

Grants receivable consist of amounts due from the following sources as of December 31, 2005 and 2004 (in thousands):

	<u>2005</u>	<u>2004</u>
Department of Labor	\$ 930	\$ 3,829
Internal Revenue Service	1,004	794
Department of Housing and Urban Development	1,676	376
Department of Health and Human Services	75	55
Total grants receivable	<u>\$ 3,685</u>	<u>\$ 5,054</u>

**4. Property and Equipment**

Property and equipment is summarized as follows at December 31, 2005 and 2004 (in thousands):

	<u>2005</u>	<u>2004</u>
Land	\$ 4,440	\$ 4,440
Building and improvements	17,864	17,760
Equipment	5	-
Accumulated depreciation	(847)	(196)
Property and equipment, net	<u>\$ 21,462</u>	<u>\$ 22,004</u>

On October 21, 2004, the Foundation acquired two condominium units located within the AARP headquarters building at 601 E Street NW, Washington, DC. These units were purchased for \$22,200,000 from AARP Properties LLC, an AARP affiliated entity. The acquisition price of the condominium units was assessed by an independent appraiser.

**AARP Foundation**  
**Notes to Consolidated Financial Statements**  
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**5. Investments**

Foundation investments include participation in AARP's unitized pooled investment fund. The Foundation's share of the investment pool is based on an initial investment in 2004 of \$10,000,000 plus accumulated earnings. Income and gains/losses are allocated based on the Foundation's pro rata share of total investments of the fund.

The fair value of the Foundation's share of pooled assets was \$10,794,637 and \$10,198,000 at December 31, 2005 and 2004, respectively.

Investments, including amounts held for charitable gift annuities, are summarized as follows at December 31, 2005 and 2004 (in thousands):

	<u>2005</u>	<u>2004</u>
Stock index mutual fund	\$ 13,436	\$ 10,060
Fixed income securities	8,571	8,641
U.S government and agency obligations	273	479
Mortgage-backed securities	913	1,124
Institutional mutual funds	1,904	2,764
Total investments	<u>\$ 25,097</u>	<u>\$ 23,068</u>

Investment income for the years ended December 31, 2005 and 2004 is summarized as follows (in thousands):

	<u>2005</u>	<u>2004</u>
Interest and dividend income	\$ 1,854	\$ 678
Net realized and unrealized gains	465	1,001
Total investment income	<u>\$ 2,319</u>	<u>\$ 1,679</u>

**AARP Foundation**  
**Notes to Consolidated Financial Statements**  
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**6. Contributions Receivable**

Contributions receivable are due from three donors at December 31, 2005 and two donors at December 31, 2004, all of whom are making annual payments on multi-year commitments. Contributions receivable at December 31, 2005 and 2004 are expected to be received as follows (in thousands):

	<u>2005</u>	<u>2004</u>
Within one year	\$ 400	\$ 300
Between two and five years	800	1,100
Thereafter	203	-
	<u>1,403</u>	<u>1,400</u>
Unamortized discount (4% and 7%)	<u>(134)</u>	<u>(202)</u>
Net contribution receivable	1,269	1,198
Less: current portion	<u>(400)</u>	<u>(300)</u>
Contributions receivable, noncurrent	<u>\$ 869</u>	<u>\$ 898</u>

**7. Bonds Payable**

On October 21, 2004, the Foundation issued 30-year District of Columbia Variable Rate Revenue Bonds Series 2004 in the amount of \$25,000,000 to finance the purchase of office space in the AARP headquarters building (see note 4). The bonds bear interest at a variable rate determined by the Remarketing Agent based upon market conditions of reselling the bonds in a secondary market sale. Accrued interest is payable monthly. Total interest expense incurred for the years ended December 31, 2005 and 2004 was \$614,300 and \$83,100, respectively. The Foundation may elect at any time to convert to a fixed interest rate.

The bond proceeds were placed in an account held by a trustee. The Foundation will use the remaining proceeds to finance the costs of renovating, rehabilitating, and equipping the purchased office space, as well as for the payment of interest costs.

The Foundation has obtained a letter of credit to secure repayment of the bond. The letter of credit constitutes an irrevocable obligation to pay the bond trustee up to an amount equal to the sum of the principal amount of the Series 2004 Bonds outstanding, plus an amount equal to interest for 35 days on the principal amount of each bond outstanding.

AARP has entered into a Standby Bond Purchase Agreement with the AARP Foundation and the issuer of the Letter of Credit to purchase all bonds in the event the Foundation defaults on the bonds under the terms and conditions of the agreement.

**AARP Foundation**  
**Notes to Consolidated Financial Statements**  
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**8. Grant Revenue**

Grant revenue from the following sources was recognized in the years ended December 31 (in thousands):

	2005	2004
Department of Labor	\$ 76,196	\$ 74,954
Internal Revenue Service	3,646	3,550
Department of Housing and Urban Development	2,593	2,127
Department of Health and Human Services	468	517
State of Florida	-	364
State of Colorado and other	338	301
	\$ 83,241	\$ 81,813

**9. Program Services**

During the years ended December 31, 2005 and 2004, the Foundation's programs were as follows:

Senior Community Service Employment Program (SCSEP) provides subsidized assignments and job training for persons 55 and older whose income is at or below 125% of the federal poverty level. The SCSEP project is primarily funded by the U.S. Department of Labor. Department of Labor revenue represented approximately 51% and 54% of the Foundation's revenue for the years ended December 31, 2005 and 2004, respectively. The current federal grant to the Foundation expires on June 30, 2006.

Tax Counseling for the Elderly (Tax-Aide) provides volunteer assistance for federal income tax preparation to low and moderate income persons, with special attention to those 60 and older throughout the country. In the 2005 tax season, approximately 2 million older persons were assisted. The Tax-Aide project is funded by AARP and the Internal Revenue Service. The current federal grant to the Foundation expires on September 30, 2006.

Litigation services protects and preserves the rights of older Americans through both amicus curiae ("friend of the court") briefs on behalf of AARP, and third-party litigation.

Other programs provide information, counseling, research, training, and technical assistance to older persons and their service providers on various matters including consumer, legal, and housing issues.

In 2005, other programs also include assistance provided to local organizations to assist individuals 50 and over affected by the 2005 hurricanes in the Gulf Coast region. To assist these individuals, the Foundation made grants of approximately \$1,600,000 of which

**AARP Foundation**  
**Notes to Consolidated Financial Statements**  
**December 31, 2005 and 2004**

\$1,238,000 remains undisbursed at December 31, 2005. This amount is included as a component of grants payable in the accompanying 2005 statement of financial position.

Management anticipates that the SCSEP and Tax-Aide grants will be renewed. The continuation of grant-funded programs beyond the expiration dates of current agreements is subject to future funding decisions by sponsoring agencies.

**10. Related-Party Transactions**

**a) Contributions**

The Foundation obtains services from AARP under a contractual agreement covering personnel costs and other direct and indirect costs. Pursuant to that agreement, AARP made contributions totaling \$32,877,000 and \$27,468,000 for the years ended December 31, 2005 and 2004, respectively. These totals included donated services valued at \$6,365,000 and \$7,809,000 for the years ended December 31, 2005 and 2004, respectively, and amounts intended to fund future period operations of \$5,852,000 and \$6,265,000 for the years ended December 31, 2005 and 2004, respectively.

AARP contributions represented approximately 22% and 20% of the Foundation's revenue for the years ended December 31, 2005 and 2004, respectively.

AARP Services, Inc., an AARP affiliated entity, contributed \$810,000 and \$800,000 to the Foundation in 2005 and 2004, respectively, to support general operations.

**b) Due to or from Affiliates**

Amounts reported as due to or from affiliates included in the accompanying statements of financial position arise from intercompany activities in the normal course of business and are settled on a quarterly basis. Due to AARP is an advance for direct expenses of the Tax-Aide program, which is expected to be repaid when the program terminates.

**c) Postretirement Health Benefits Obligation**

A resolution in 1997 by the AARP Board of Directors stated AARP's intent to assume responsibility for postretirement health benefits relating to the Foundation's employees. The accrued obligation, which totaled \$9,811,000 and \$6,066,000 at December 31, 2005 and 2004, respectively, is recorded by AARP. AARP currently funds these benefits as claims are received from eligible Foundation retirees.

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**d) Office Space**

Prior to October 21, 2004, the Foundation utilized office space at AARP's national headquarters under terms of an operating lease with AARP Properties LLC, a wholly owned subsidiary of AARP. Rent expense, including utilities, maintenance, and other services such as security and building management, which continued subsequent to the termination of the leasing arrangement, was approximately \$1,029,000 for the year ended December 31, 2004. Under the continuing operations agreement with AARP, these other costs were approximately \$412,000 for the year ended December 31, 2005, of which \$100,400 was contributed to the Legal Counsel for the Elderly as in-kind contribution.

**e) Intercompany Grant Awards**

The Foundation has awarded grants to AARP in support of several of AARP's charitable programs, such as Staying Sharp, Driver's Safety Initiatives, Grandparenting Information Center, Caregiver, Scholars Program, Home Modification Project, Aging in Place, and Public Policy Institute Research Projects. The total amount awarded to AARP was \$2,620,000 and \$379,000 in 2005 and 2004, respectively, of which \$1,231,000 and \$135,000 was recognized in 2005 and 2004, respectively. Approximately \$573,900 and \$90,000 of the recognized amounts remained unpaid as of December 31, 2005 and 2004, respectively, and are included as a component of due to affiliates in the accompanying statements of financial position.

**11. Defined-Benefit Pension Plan**

The Foundation participates with other AARP affiliates in the AARP Employees' Pension Plan (the Plan), a noncontributory defined-benefit pension plan. The Plan covers all Foundation employees after they meet specified eligibility requirements.

Plan assets, investment income, and administrative expenses generally are allocated to the Foundation based on its proportion of the Plan's total projected benefit obligation as determined by the Plan actuaries. The general funding policy for the Plan is to contribute an amount equal to or greater than the minimum funding requirements of the Employee Retirement Income Security Act of 1974, as actuarially determined, calculated on a level percentage of payroll costs basis, but not greater than the maximum tax deductible limit. There were no employer contributions by the Foundation to the Plan in 2005 and 2004. The Foundation is not required to make a contribution to its pension plan in 2006. However, supplemental contributions may be made that are not estimable at this time.

The net periodic pension expense for the years ended December 31, 2005 and 2004 was \$893,000 and \$1,890,000, respectively.

**AARP Foundation**  
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**December 31, 2005 and 2004**

The following table sets forth the Foundation's portion of the Plan's funded status at September 30, 2005 and 2004 (the actuarial measurement date) and the amounts recognized in the Foundation's financial statements as of and for the years ended December 31, 2005 and 2004 (in thousands):

	<u>2005</u>	<u>2004</u>
Change in benefit obligation:		
Benefit obligation at beginning of year	\$ (27,293)	\$ (24,755)
Service cost	(1,242)	(1,294)
Interest cost	(1,562)	(1,456)
Actuarial gain (loss)	218	(451)
Benefits paid	679	663
	<u>679</u>	<u>663</u>
Benefit obligation at end of year	<u>\$ (29,200)</u>	<u>\$ (27,293)</u>
Change in plan assets:		
Fair value at beginning of year	\$ 18,331	\$ 17,319
Expected return on plan assets	1,634	1,454
Actuarial gain	-	220
Benefits paid	(679)	(663)
	<u>(679)</u>	<u>(663)</u>
Fair value at end of year	<u>\$ 19,286</u>	<u>\$ 18,330</u>
Funded status	\$ (9,914)	\$ (8,963)
Unrecognized net actuarial loss	3,308	3,175
Unrecognized prior service cost	44	59
	<u>44</u>	<u>59</u>
Accrued pension liability	<u>\$ (6,562)</u>	<u>\$ (5,729)</u>

The accumulated benefit obligation for the plan was approximately \$25,258,000 and \$24,060,000 as of September 30, 2005 and 2004, respectively.

The assumptions used to determine net periodic benefit cost in the actuarial valuations at the September 30, 2005 and 2004 measurement dates are as follows:

	<u>2005</u>	<u>2004</u>
Discount rate	5.80%	5.95%
Expected long-term rate of return on plan assets	8.50%	8.50%
Future salary increases	4.00%	4.00%

**AARP Foundation**  
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The assumptions used to determine the benefit obligation in the actuarial valuations at the September 30, 2005 and 2004 measurement dates are as follows:

	<u>2005</u>	<u>2004</u>
Discount rate	5.70%	5.80%
Expected long-term rate of return on plan assets	8.00%	8.50%
Future salary increases	4.00%	4.00%

As of December 31, 2005 and 2004, the weighted-average asset allocation for the Plan is as follows:

	<u>2005</u>	<u>2004</u>
Asset Categories:		
Equity securities	68%	70%
Debt securities	30%	29%
Cash equivalents	2%	1%
	<u>100%</u>	<u>100%</u>

The targeted allocation of the investment assets in the Plan is for equities to comprise 65% of the investment portfolio, debt securities to comprise 30%, and alternatives to comprise the remaining 5%. These targets are not intended to serve as a rigid constraint on the investment allocation. The following chart sets out the minimum and maximum positions for the various asset classes in the Plan:

Asset Class:	Minimum	Target	Maximum
Equity securities	61%	65%	71%
Debt securities	24%	30%	32%
Alternatives	0%	5%	7%
Cash equivalents	0%	0%	7%

**AARP Foundation**  
**Notes to Consolidated Financial Statements**  
**December 31, 2005 and 2004**

The following benefit payments, which reflect expected future service, are expected to be paid as follows (in thousands):

Years ending December 31,	\$	
2006		710
2007		788
2008		884
2009		990
2010		1,118
2011–2014		8,251

**12. Employee Healthcare Benefits**

The Foundation provides certain healthcare and other welfare benefits for active employees as a participating employer in the AARP Employees' Welfare Plan. The Welfare Plan receives contributions from all participating employers to provide benefits based on expected costs of providing these benefits. Expenses incurred by the Foundation for healthcare benefits were \$1,606,000 and \$1,718,000 for the years ended December 31, 2005 and 2004, respectively. The total estimated liability, including incurred but not reported claims, at December 31, 2005 and 2004 was approximately \$454,000 and \$476,000, respectively, and is included as a component of accounts payable and accrued expenses in the accompanying statements of financial position.

**13. Defined-Contribution Plan**

The Foundation participates in a single-employer defined-contribution plan called the AARP Employees' 401(k) Plan. To participate in the 401(k) Plan, an employee must be at least 18 years of age and have been employed for a minimum of one month of continuous service with the AARP Foundation.

The Foundation makes contributions to the 401(k) Plan for its employees, matching employee contributions at 100% of the first 3%, and 50% of the next 2% of employee compensation up to the maximum limits allowed by current law.

Employer contributions totaled \$494,000 and \$397,000 for the years ended December 31, 2005 and 2004, respectively.

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**Notes to Consolidated Financial Statements**  
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**14. Temporarily Restricted Net Assets**

Temporarily restricted net assets consist of the following at December 31, 2005 and 2004 (in thousands):

	<u>2005</u>	<u>2004</u>
Restricted for grant funded programs	\$ 4,153	\$ 9,709
Restricted for research and education	7,636	1,690
Available in future periods	<u>1,269</u>	<u>1,198</u>
Total temporarily restricted net assets	<u>\$ 13,058</u>	<u>\$ 12,597</u>

**15. Contingencies**

The Foundation is a party to various claims and potential legal actions. Management believes, based upon advice of counsel, that the disposition of these matters will not have a significant effect on the financial position of the Foundation.

The Foundation receives a substantial portion of its revenue from government grants, which are subject to audit by various federal and state agencies. The ultimate determination of amounts received under these projects generally is based upon allowable costs reported to and audited by the governments or their designees. The liabilities, if any, arising from such compliance audits cannot be determined at this time. In the opinion of management, adjustments resulting from such audits, if any, will not have a significant effect on the financial position of the Foundation.

**AARP Foundation**  
**Schedule of Functional Expenses**  
**For the Year Ended December 31, 2005**  
**(with Comparative Totals for the Year Ended December 31, 2004)**

	Program Services				Supporting Services			2005 Total Expenses	2004 Total Expenses	
	SCSEP	Tax Counseling for the Elderly	Litigation Services	Other Programs	Total Program Services	Fundraising	Management and General			Total Supporting Services
<b>Expenses</b>										
Enrollee wages & benefits	\$ 61,393	\$ -	\$ -	\$ -	\$ 61,393	\$ -	\$ -	\$ -	\$ 61,393	\$ 61,254
In-kind services	15,035	-	-	-	15,035	-	-	-	15,035	15,569
Personnel costs	8,295	906	3,548	2,875	15,624	2,259	1,086	3,345	18,969	18,248
Consulting & professional services	650	110	335	1,159	2,254	1,629	338	1,967	4,221	1,997
Volunteer travel	-	4,423	1	37	4,461	-	27	27	4,488	3,963
Printing & postage	400	404	63	952	1,819	5,991	33	6,024	7,843	2,632
Promotion	115	-	1	57	173	2,581	3	2,584	2,757	1,135
Meetings & travel	748	38	68	230	1,084	241	20	261	1,345	1,339
Facilities	1,334	44	104	228	1,710	96	40	136	1,846	2,225
Telephone	392	59	17	65	533	16	2	18	551	543
Office supplies	583	4	11	45	643	28	161	189	832	1,143
Computers & software	4	3,101	6	34	3,145	4	112	116	3,261	88
Data processing	123	-	5	-	128	831	-	831	959	12
Grant awards	-	-	-	5,389	5,389	-	-	-	5,389	1,751
Depreciation & amortization	83	53	128	240	504	116	48	164	668	202
Insurance & taxes	46	28	84	125	283	62	97	159	442	232
Interest	76	49	118	221	464	107	43	150	614	83
Miscellaneous	433	437	131	232	1,233	322	48	370	1,603	1,366
Information technology	637	755	575	565	2,532	358	69	427	2,959	2,153
AARP allocated general & administrative	-	-	-	-	-	-	4,015	4,015	4,015	5,083
<b>Total expenses</b>	<b>\$ 90,347</b>	<b>\$ 10,411</b>	<b>\$ 5,195</b>	<b>\$ 12,454</b>	<b>\$ 118,407</b>	<b>\$ 14,641</b>	<b>\$ 6,142</b>	<b>\$ 20,783</b>	<b>\$ 139,190</b>	<b>\$ 121,018</b>

See accompanying notes to financial statements.