



American Arbitration Association

Dispute Resolution Services Worldwide

2005 PRESIDENT'S LETTER
& FINANCIAL STATEMENTS



American Arbitration Association

Dispute Resolution Services Worldwide

OUR SHARED MISSION

The American Arbitration Association is dedicated to the development and widespread use of prompt, effective, and economical methods of dispute resolution. As a not-for-profit organization, our mission is one of service and education.

We are committed to providing exceptional neutrals, proficient case management, dedicated personnel, advanced education and training, and innovative process knowledge to meet the conflict management and dispute resolution needs of the public now and in the future.

OUR SHARED VISION

The American Arbitration Association will be the global leader in conflict management – built on integrity, committed to innovation, and embracing the highest standards of client service achievable in every undertaking.

OUR SHARED COMMITMENT TO DIVERSITY

The American Arbitration Association is the global leader in conflict management with core values of integrity and service. Our integrity demands impartial and fair treatment of all people with whom we come in contact, regardless of gender, race, ethnicity, age, religion, sexual orientation, or other characterization. Our conflict management services put into practice our goal for the resolution of disputes between parties with different perspectives, experiences, and backgrounds.

Because of the breadth of the Association's work and the global reach of its services, we recognize the importance and contribution of a diverse work force, a diverse Roster of Neutrals, a diverse Board, and commit to respect and increase diversity in all our endeavors.

2005 PRESIDENT'S LETTER

In many respects, 2005 was a watershed year for the American Arbitration Association. It was a time for looking and moving forward, for rededication and renewal, for continued expansion of services in targeted areas, and for strengthening our organization's financial footing in an increasingly competitive environment.

If there were a single theme for the year, it would be one of being faithful to our roots and history while building confidently for the future. This entailed:

- continued commitment to the AAA's traditional role of public service,
- building on core competencies to develop innovative new services,
- supporting the AAA's leading international presence and commitment,
- preparing for the future by building a stronger, more nimble organization with a better financial footing, and
- reemphasizing the vision and values that go hand in hand with our mission as a not-for-profit institution.

The backdrop for these undertakings was an appropriate one – the 80th anniversary of the Federal Arbitration Act (FAA), the legislation that shaped modern arbitration and dramatically affected the conduct of both domestic and international commerce. The Association played a principal role in the celebration of the Act's passage, sponsoring and hosting a series of four lectures examining the value and influence of the FAA from a number of perspectives. Three of the four lectures were delivered in 2005, including one lecture presented in Dublin at our first annual meeting held outside the United States.

Particularly encouraging in this milestone year was the strong continuing support that the landmark FAA received after eight decades. A significant majority of the nearly 50 ADR-related bills introduced in the 109th session of Congress would, if promulgated, have a positive impact on the use of alternative dispute resolution (ADR), promoting arbitration, mediation, and other methods of dispute resolution. Four of the bills directly mentioned the AAA or referred to specific rules or protocols that we have adopted.

In February of 2006, the Supreme Court of the United States handed down their opinion in *Buckeye Check Cashing v. Cardegna*, which has been viewed as a firmly pro-arbitration decision, and one in a long line of Supreme Court decisions supporting the use of arbitration to resolve a wide range of disputes. In *Buckeye*, the Court ruled that when a contract as a whole is alleged to be illegal, the decision regarding the validity of that contract is to be made by an arbitrator rather than by a court. *Buckeye* also reaffirmed the Court's commitment to important holdings from two prior cases; the severability doctrine from *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, which provides that arbitrators decide whether contracts are enforceable where attacks are made on the contract as a whole and not the arbitration agreement specifically, and *Southland Corp. v. Keating*, where the Court found that the FAA established a federal substantive law favoring arbitration, which is applicable in state and federal courts.

A CONTINUING PUBLIC SERVICE COMMITMENT

Our mission statement reads in part: “The American Arbitration Association is dedicated to the development and widespread use of prompt, effective, and economical methods of dispute resolution. As a not-for-profit organization, our mission is one of service and education.” 2005 was a year in which we put the AAA’s resources squarely behind major efforts in both these areas.

In October, in the aftermath of hurricanes Katrina and Rita, we moved quickly to establish a new mediation-based Disaster Recovery Claims Resolution Services program to be used in resolving what we knew would be a sizeable volume of insurance claim disputes between homeowners and businesses and their insurance carriers. We chose to build the program around mediation, in which we have extensive experience, because of its low cost, its informality, and its speed. Previously, working with the Florida Department of Insurance, we had established a program in the wake of hurricane Andrew that handled more than 2,400 claims with a 92% settlement rate, and we administered a volunteer ADR program for the California Department of Insurance after the Northridge earthquake.

In December, Louisiana and Mississippi selected the AAA to serve as administrator of new state-mandated mediation programs dealing with disputed residential claims arising out of Katrina. By mid-April 2006, more than 5,500 requests for mediation had been filed in the two jurisdictions. Programs we put in place in both states were designed to speed claim settlement and reduce costs, enabling policyholders to rebuild quickly. In both Louisiana and Mississippi, the insurer, not the policyholder, pays the mediators’ fees and the administration costs, both of which were capped below normal commercial rates.

While our own staff was temporarily displaced from our New Orleans office, we were fortunate that no one on our team was injured. Since there was no serious damage to our office, we were able to provide facilities for mediation conferences at a time when useable office space was difficult to find.

As we further our public service mission, we remain committed to our core ideology and our commitment to diversity. For the second successive year we helped sponsor the National Conference for Minority Professionals in Alternative Dispute Resolution. With a theme of promoting opportunities for minorities in the field of ADR, the conference attracted some 300 people representing 25 states and the District of Columbia.

AAA MISSION OF EDUCATION

Under the heading of education initiatives, we continue to break new ground. We are taking more and more educational programs online, we are offering an increasingly broader range of international educational programs, and we are expanding the scope of research we conduct. Among the activities we undertook in 2005 were:

- We laid plans to establish an AAA Foundation, an organization whose mission would essentially be to mine the 80 years of data that the AAA has gathered on domestic and international commercial arbitration, mediation, and conciliation, as well as to carry out selected research projects in new areas. It made perfect sense to put the work done by the six-year-old self-governing Global Center for

Dispute Resolution Research under the auspices of the new foundation. The Global Center was the first research facility dedicated to examining the use and effectiveness of dispute resolution practices on a worldwide basis, an expertise that dovetails perfectly with the mandate of the new foundation.

- The AAA was honored to participate in a detailed, substantive briefing on the current state of arbitration at the Florida Judicial Conference.
- In December, we moved quickly to create a new training program for property tax arbitrators, in partnership with the Texas Association of Realtors. The program was created in response to legislation enacted in Texas in May that required the establishment of a registry of qualified arbitrators with at least 30 hours of certified training in arbitration and alternative dispute resolution procedures. When the legislation was enacted, there was no training program in place and no list of arbitrators qualified to resolve disputes over property values. Since November 30, almost 400 real estate brokers, salespeople, and appraisers had been trained under the AAA program.
- In November, we put together a “Straight Talk about Construction Arbitration” conference in Irving, Texas that focused on a discussion of best practices for parties involved in construction industry arbitration and an examination of difficult, real world issues likely to arise in construction disputes. The highly experienced group of construction professionals and arbitrators heard presentations on topics ranging from selecting the right arbitrator to dealing with discovery and disclosure problems, tips on preparing and presenting a case, writing arbitration awards that minimize challenges, and drafting clauses that work. Earlier, we had also published for the construction industry a well-received 20-page brochure entitled “The Construction Industry’s Guide to Dispute Avoidance and Resolution.”
- The Association held two conferences for neutrals in 2005, unveiling the full version of the AAA Neutrals eCenter and introducing new arbitrator conference workshops, including “The Challenge of Mediating Disputes” and “Labor and Employment Arbitration: Similarities and Differences in Practice,” and two new Arbitrator Continuing Education (ACE) programs, “Chairing an Arbitration Panel: Managing Procedures, Process & Dynamics” and “Dealing with Delay Tactics in Arbitration,” that are available for in-person and online neutrals training.
- We continued to retool and find new uses for the data gathered in our seminal study of Dispute-WiseSM conflict management and avoidance practices. In May, we introduced the Dispute-Wise Business Management Workshop that focuses on enhancing the strategic value of a company’s legal organization, discussing leading practices that get results, determining what works and why, and assessing the bottom-line benefits.
- Among other pro bono activities during the year, we provided neutral meeting facilities and other support to the New York City Family Homelessness Special Master Panel and The Legal Aid Society as they came together as part of a continuing effort to resolve difficult issues with respect to New York’s homeless families.

CLASS ACTION ARBITRATIONS

In a substantial undertaking, the number of class action arbitrations we administer continues to grow, as does the debate around how these cases should be handled. This new area of service arose when the Supreme Court in *Green Tree Financial Corporation v. Bazzle* held that it was for an arbitrator, not a court, to decide whether an arbitration agreement permits or precludes class actions where the arbitration agreement itself is silent on that issue. Implicit in the decision is that class action proceedings could take place in an arbitration setting. In response, the AAA created Supplementary Rules for Class Arbitrations, the first set of procedures created for administering these complex and difficult cases.

In 2005, considerable controversy arose in the legal and ADR communities over class action arbitrations and, in particular, about the inclusion of class action waivers in arbitration clauses. It has been the practice of the AAA since its Supplementary Rules for Class Arbitrations were first enacted to require a party seeking to bring a class arbitration under an agreement that on its face prohibits class actions to first seek court guidance as to whether a class arbitration may be brought under such an agreement. The AAA's practice has been neither to commence administration of a case nor to refer such a matter to an arbitrator until a court decides that it is appropriate to do so. The AAA's determination not to administer class arbitrations where the underlying arbitration agreement explicitly precludes class procedures was made because the law on the enforceability of class action waivers remains unsettled. Furthermore, the AAA takes no position as to whether such clauses are or should be enforceable.

After a review of these policies, we concurred – while others were changing their procedures only to have to change them back later – that the correct course of action was to continue to follow our established policy of deferring to the courts on the issue of whether such waivers are enforceable in a particular case. We are proud that this carefully considered, consistent approach to the administration of class arbitrations has served the public well from its inception, giving it confidence that our policies will remain unchanged pending the further development of the law in this area.

We currently maintain a docket of more than 90 class action arbitrations with a range of dispute types that includes franchise, consumer, and employment issues. Hearing dates, awards, court orders, and – in the interest of transparency – counsel communications are posted on the publicly available docket on the AAA's website, www.adr.org.

BUILDING ON CORE COMPETENCIES TO DEVELOP INNOVATIVE NEW SERVICES

Technology continues to be the driving force as we seek ways to improve the delivery and effectiveness of ADR services of all types. Equally important, we are using a combination of core competencies and developing technology to broaden our reach and offer exciting services in entirely new areas.

AAAWebFileSM is a case in point.

Introduced in 2001, AAWebFile is our online framework for communications and case management. Easy to use, it enables parties, counsel, and AAA case managers to file and to track case progress online – even when a case is filed offline. In the past year, the volume of cases filed through AAWebFile increased 49%, and since AAWebFile's introduction, 3,834 cases involving more than \$1.4 billion in claims have been filed online. In addition to a sharp increase in the use of online filing by the labor community, international and construction online filings were up 24% and 35%, respectively.

In the no-fault insurance arena, we have introduced in our work with the New York State Department of Insurance the Electronic Case Folder (ECF), through which all aspects of dispute resolution are handled online. In this paperless system, cases are filed and administered electronically – hearings are scheduled and conducted online and all documents are available electronically. Clearly, greater efficiency is a pathway to success. Since we took over the management of the New York State no-fault conciliation process in 1999, the conciliation settlement rate has doubled.

In a further extension of AAAWebFile applications, last year we entered into an exclusive agreement with The National Research Exchange (NRE), whose sole purpose is to foster the creation of better equity investment research, to use AAAWebFile's core capabilities in the creation of Rapid Alternative Dispute Resolution (R|ADR), a custom designed ADR system for resolving code of conduct disputes. As David Weild IV, Chief Executive of NRE, explains, core AAA expertise was the key to the project, "The American Arbitration Association was a great collaborative partner in developing our R|ADR for member disputes. Our joint goal was to design a quick and inexpensive dispute resolution process that still retained all of the AAA's expertise. We accomplished this by conducting much of the mediation and arbitration processes in parallel, and by moving as many activities as possible to the AAA's online system. The AAA fielded a great team of quality professionals committed to innovative problem solving."

The NRE program has already begun to serve as a template for services we can offer other membership organizations. In October, we formed a strategic alliance with the National Community Reinvestment Coalition's (NCRC) Center for Responsible Appraisals and Valuations to use our expertise to help insure fair, accurate home mortgage appraisals and valuations. We have made our staff, neutrals, and state-of-the-art online case management systems available to help handle disputes among lenders, appraisers, brokers, and realtors who have agreed to follow the NCRC's code of conduct, and we have been appointed exclusive administrator for disputes involving code of conduct issues with respect to real estate lending and appraisals.

Because of the 20% growth in technology filings over the past five years and the convergence of disputes involving multiple aspects of intellectual property, science, and technology, we established a new Large Case Technology, Science & Intellectual Property Panel that parallels special panels created by the AAA in the employment, construction, large complex case, and commercial areas. The panel will be called upon for claims involving more than \$500,000 in disputes arising in the telecommunications, computer hardware and software, Internet, electronics, e-commerce, nanotechnology, biotechnology, pharmaceuticals, and material sciences sectors.

Once again this past year we expanded the list of awards we publish online. For the first time, about 2,000 redacted labor awards are being made available through a cooperative agreement with LexisNexis. The full text of these awards issued since 2003 provides an unparalleled database resource for the research on current trends in arbitral awards in the labor sector. In a similar vein, we have entered into an agreement with West International to publish selected international arbitration awards.

As noted earlier, the full version of the Neutrals eCenter was unveiled in 2005 at the Palm Springs neutrals conference, and it has received widespread praise. The eCenter is a personalized online business management tool made available to all AAA neutrals. It enables users to update resumes, view current cases online, maintain calendars of case activities, submit and track compensation and expense payments, and register for continuing education courses.

GROWING MEDIATION SERVICES

As part of a renewed commitment to be a leader in fostering the increased use of sophisticated mediation techniques as dispute resolution tools, in August we appointed 20-year AAA veteran Neil Carmichael to the newly created position of Vice President-U.S. and International Mediation Services. In his new role, Neil is responsible for overseeing our global mediation strategy and operations, developing policies and priorities for our mediation-based activities, managing relationships with neutrals, and heading mediation training and business development efforts.

In two important mediation initiatives – in addition to our mediation work with hurricane Katrina victims and a new agreement to provide construction mediation services for New York’s Metropolitan Transit Authority – we introduced a comprehensive introductory online mediation course entitled “Fundamentals of Effective Mediation Advocacy.” We also established a roster of AAA staff mediators who will provide a new option, within our full range of ADR services, for parties interested in immediate, low-cost expedited dispute resolution. The program offers a cadre of well-trained AAA staff mediators who will conduct up to four hours of telephonic mediation under the Association’s Commercial Mediation Procedures for a flat fee.

AAA ELECTIONS AND ENHANCED CASE MANAGEMENT SERVICES

The AAA’s election services, which enjoys the steadily growing support of both management and labor, continues to be called upon to conduct a growing number of major elections. In 2005, the AAA administered elections for, among others, the New York Transit Workers Union Local 100, the United Federation of Teachers, the Uniformed Firefighters Association, the Civil Service Employees Association, the New York State Corrections Officers & Police Benevolent Association, and several chapters of the Service Employees International Union, for one of which we administered the largest union election ever held in the State of Illinois.

We continued to introduce elements of our enhanced and expanded service program, an initiative begun in 2004 with the launch of AAA adr+ and AAA adr+ for Large Complex Cases, which were designed to help parties resolve disputes more efficiently and effectively across a broad range of industries. In 2005, we introduced two new service modules – AAA Arbitration RoadmapSM and AAA Resolution ServicesSM. The AAA Arbitration Roadmap helps guide parties from the pre-ADR stage onward, outlining the options available to them and how best to manage the arbitration process and the costs involved, offering a yardstick with which to measure both the probable time and cost of arbitration. AAA Resolution Services is a tool kit that provides a suite of early dispute resolution options – such as early neutral evaluation and mini-trials – that assist parties in minimizing the

impact of disputes and resolving them at the earliest possible stage.

The AAA Solutions ManagerSM program, piloted in the fall of 2004, has been rolled out to all commercial and international case management centers. AAA Solutions Managers guide parties through a broad range of alternative – and often customized – options, helping to structure dispute resolution solutions that can be faster and less expensive than traditional methods. All of this is part of ongoing programs to strengthen the services we provide through the case management centers, an effort – to judge from the anecdotal evidence we gather – that is being enthusiastically received.

SUPPORTING THE ASSOCIATION'S GROWING INTERNATIONAL PRESENCE AND COMMITMENT

Once again, this was an active year for us in the international arena. Holding our annual meeting in Dublin – the first ever outside the United States – was a statement about how seriously we wear the mantle of leadership in international dispute resolution. In its ninth year, the International Centre for Dispute Resolution (ICDR), the AAA's international division, remains the largest international provider of dispute resolution services, recording 580 new filings in 2005.

South American, Middle Eastern, and Asian case filings rose 31%, 13%, and 26%, respectively. Importantly, the number of cases being heard in non-U.S. locales under AAA rules and procedures continues to grow – an indication that we are no longer viewed as a strictly U.S. organization. ICDR announced in February of 2006 that it is expanding its international footprint by opening its second and third international offices – in Mexico City under a cooperative agreement with the Mediation and Arbitration Commission of the Mexico City National Chamber of Commerce, and the other in Singapore, a joint venture with the Singapore International Arbitration Centre.

Two anecdotes provide an additional indication of how favorably ICDR is being viewed in its markets. First, in July, the Irish Minister for Justice, Equality and Law Reform signed an order designating the ICDR a body that may, upon request, nominate mediators for personal injury matters that come before Irish courts – the first time we have been named in this way by a foreign government. Second, according to the “Second Annual Litigation Trends Survey,” an independent survey of 354 U.S. and U.K. corporate general counsel commissioned by the international law firm of Fulbright & Jaworski, two-thirds of American corporate counsel prefer AAA/ICDR rules for international arbitration agreements.

ICDR Young and International, a networking and educational program for ADR practitioners under the age of 40, continues to gain momentum. Established in 2004 with the support and cooperation of leading international law firms, it boasted 550 associates from 55 countries early in 2006, a highly engaged membership which represents the next generation of international arbitrators and arbitration practitioners. Also in 2005, we either sponsored or participated significantly in international conferences or meetings in multiple Latin American nations, Japan, Australia, China, Singapore, New Zealand, Egypt, Romania, and most of the major countries of Western Europe.

**PREPARING FOR THE FUTURE:
BUILDING A STRONGER, MORE NIMBLE ORGANIZATION**

In a difficult economic climate for the ADR sector, caseload figures dropped to 142,000 filings in 2005 as compared to 159,000 cases in 2004. Much of the decrease was attributable to a lower number of no-fault automobile insurance cases as backlogs from prior years were cleared, and construction case filings – our largest commercial caseload area – were essentially even year over year. We did, however, experience solid growth in the employment, franchise and partnership, energy, and consumer sectors.

A diminution in large complex case filings that led to lower revenues and a loss, net of investment gains, of about \$3.5 million for the year, most impacted our 2005 bottom line. We responded by taking forward-looking steps that strengthened our core organization and financial footing, making us more nimble and competitive. A consolidation of offices and selective staff reductions took about \$4 million of expense out of our overhead immediately with an additional \$2 million in savings expected in 2007, and we incurred one-time reorganization costs of \$1.5 million that were part of the \$3.5 million loss. We were also able to improve our cash position without using our lines of credit, and I am happy to report that we are off to an excellent start in 2006.

We first began to see improvement in case filing trends in the closing months of 2005, and in January and February of 2006 our situation improved dramatically. We showed strong operating results, as well as solid investment returns. Comparing the 1st Quarter 2005 to the 1st Quarter 2006, aggregate revenues grew 10%, with commercial revenue growth of 13%. Most importantly, the number of large, complex commercial case filings grew steadily toward the end of 2005, and in January 2006, alone, they increased 50% compared to a year earlier.

REEMPHASIZING THE VISION AND VALUES THAT UNDERLIE OUR MISSION

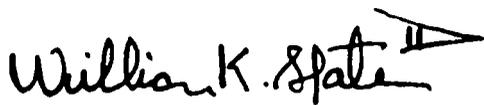
Much of what we did in 2005 is emblematic of how we set our course for the future – proud of our history, knowing who we are, faithful to our roots, yet forward-focused with a deep-rooted tradition based on the importance of integrity, fair dealing, diversity, and inclusiveness.

In 2005, we revised our codes of ethics and business conduct, moved the Ethics Officer function under the General Counsel's responsibility, and installed both a web-based violations reporting system and a hot line – all indications of the firmness of our commitment in this area.

In every way we can, we seek to keep our vision and values prominent in the day-to-day thinking of our staff, and the President's Award for Living the Values is one important way in which we achieve this. The award is given annually to the person who best exemplifies the core values that will help the Association build and achieve its vision for the future. The 2005 winner, Jeff Coble from our Philadelphia office, was selected by his peers and presented to the Board of Directors at our Dublin Annual Meeting.

As I noted at the outset of this letter, 2005 was a period of rededication and renewal, but also a time for looking ahead. As we go forward, we remain proud of the leadership role we play – it's part of who we are. We keep examining the landscape, asking how the process can be improved – made more efficacious, more transparent, more responsive to the needs of those who turn to us and entities like us for help. Implicit in all of this is that we are not just talking about the AAA – we are talking about the field, the totality of what's going on in the ADR community worldwide, and that's exactly what leadership is about.

Once again, my personal and heartfelt thanks go out to our Board, our staff, and our senior management for their dedication, hard work, and support in a difficult but – on balance – a highly successful year.

A handwritten signature in black ink that reads "William K. Slate II". The signature is written in a cursive style with a prominent flourish at the end that resembles a stylized arrow or a large '2'.

William K. Slate II

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- Hon. John Charles Thomas
Hunton & Williams
- John M. Townsend, Esq.
Hughes Hubbard & Reed LLP
- Christi L. Underwood, Esq.
General Contractor,
Arbitrator, Mediator
Christi L. Underwood, P.A.
- Howard D. Venzie, Jr., Esq.
Venzie, Phillips & Warshawer, P.C.
- Dr. Claus von Wobeser
von Wobeser y Sierra S.C.
- Richard S. Ward, Esq.
- Hon. William H. Webster
Consulting Partner
Milbank, Tweed,
Hadley & McCloy LLP
- David A.R. Williams, Q.C.
Bankside Chambers
- J. Warren Wood III, Esq.
Greenbaum, Rowe,
Smith & Davis, LLP
- + *Director Proposed for*
Reelection to the 2006-2010 term
- + *Past Chairman of the Board*
- + *Honorary Member of the*
Executive Committee

2006 BOARD NOMINEES

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Vice Chairman
Brunswick Corporation

Howard O. Hunter
President
Singapore Management University

Gabrielle Kaufmann-Kohler
Partner
Schellenberg Wittmer

Elizabeth J. Keefer
General Counsel
Columbia University

Michelle Coleman Mayes
Senior Vice President
and General Counsel
Pitney Bowes

Hon. Stephen Schwebel

Larry D. Thompson
Senior Vice President and
General Counsel
PepsiCo, Inc.

2006 OFFICERS & EXECUTIVE STAFF

James H. Carter
Chairman of the
Board of Directors

John M. Townsend
Chairman of the Executive
Committee of the Board of Directors

William K. Slate II
President and
Chief Executive Officer

Francesco Rossi
Senior Vice President,
Chief Financial Officer
and Treasurer

Eric P. Tuchmann
General Counsel and
Corporate Secretary

Mark E. Appel
Senior Vice President

Jennifer J. Coffman
Senior Vice President

John C. Emmert, Jr.
Senior Vice President

India Johnson
Senior Vice President

Robert E. Meade
Senior Vice President

Richard W. Naimark
Senior Vice President

Christine L. Newhall
Senior Vice President

Fern Schair
Senior Vice President

Steven K. Andersen
Vice President –
International Development

Sasha A. Carbone
Associate General Counsel

Neil Carmichael
Vice President – U.S. and
International Mediation Services

Oslene Carrington
Vice President –
Marketing and Sales Programs

Carl Cheesman
Vice President –
Corporate Services

Kenneth Egger
Vice President –
Elections

Christopher Heelan
Vice President –
Finance and Controller

Harry Kaminsky
Vice President –
Neutrals Training

Anthony Kreindler
President –
ADRWorld.com

Luis M. Martinez
Vice President –
International Development

Debi Miller-Moore
Vice President –
eCommerce Services,
Claims Programs & IFFS

Ted E. Pons
Vice President –
Publications and ADR Resources

Morag Rollins
Vice President –
Human Resources

Gene Truncellito
Vice President –
Staff and Outreach Training

Joseph Williams
Vice President –
Information Services

Jeffrey Zaino
Vice President –
Elections

Frank T. Zotto
Vice President –
Case Management



American Arbitration Association
Dispute Resolution Services Worldwide

AMERICAN ARBITRATION ASSOCIATION, INC. AND SUBSIDIARIES

REPORT ON CONSOLIDATED FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 2005 AND 2004

AMERICAN ARBITRATION ASSOCIATION, INC. AND SUBSIDIARIES

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REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

**TO THE BOARD OF DIRECTORS
AMERICAN ARBITRATION ASSOCIATION, INC.**

We have audited the accompanying consolidated balance sheets of American Arbitration Association, Inc. and Subsidiaries as of December 31, 2005 and 2004, and the related consolidated statements of operations and changes in net assets and cash flows for the years 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 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 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 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 American Arbitration Association, Inc. and Subsidiaries as of December 31, 2005 and 2004, and the changes in their net assets and cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.



New York, New York
March 24, 2006

CONSOLIDATED BALANCE SHEETS
DECEMBER 31, 2005 AND 2004

| ASSETS | <u>2005</u> | <u>2004</u> |
|---|-----------------------------|-----------------------------|
| Cash and cash equivalents | \$ 598,000 | \$ — |
| Investments, at fair value (Note 2) | 73,351,000 | 68,180,000 |
| Administration fees receivable, net of allowances for cancellations and uncollectible accounts of \$1,005,000 in 2005 and \$1,240,000 in 2004 | 18,320,000 | 25,097,000 |
| Other receivables | 363,000 | 225,000 |
| Prepaid expenses and other assets (Note 4) | 2,608,000 | 3,348,000 |
| Deferred pension costs (Note 3) | 520,000 | 646,000 |
| Furnishings, equipment, and leasehold improvements, net (Note 4) | 11,072,000 | 13,639,000 |
| Total Assets | <u>\$106,832,000</u> | <u>\$111,135,000</u> |
| | | |
| LIABILITIES AND NET ASSETS | | |
| | | |
| Liabilities | | |
| Accounts payable and accrued expenses (Notes 3 and 5) | \$ 57,054,000 | \$ 58,680,000 |
| Accrued postretirement medical costs (Note 3) | 9,668,000 | 9,227,000 |
| Accrued pension liability (Note 3) | 9,944,000 | 9,134,000 |
| Deferred rent | 4,153,000 | 4,762,000 |
| Deferred revenue | 2,110,000 | 2,202,000 |
| Total Liabilities | <u>82,929,000</u> | <u>84,005,000</u> |
| Commitments and contingencies (Note 5) | — | — |
| Unrestricted net assets | 23,903,000 | 27,130,000 |
| Total Liabilities and Net Assets | <u>\$106,832,000</u> | <u>\$111,135,000</u> |

See Notes to Consolidated Financial Statements.

**CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS
YEARS ENDED DECEMBER 31, 2005 AND 2004**

| OPERATING REVENUES | <u>2005</u> | <u>2004</u> |
|--|----------------------|----------------------|
| Administration fees earned: | | |
| Commercial | \$ 42,744,000 | \$ 44,989,000 |
| No-fault and uninsured motorist | 17,399,000 | 18,162,000 |
| Labor | 4,888,000 | 4,970,000 |
| Elections | 2,731,000 | 4,346,000 |
| Total | 67,762,000 | 72,467,000 |
| Publications and education | 1,785,000 | 1,935,000 |
| Total | 69,547,000 | 74,402,000 |
| OPERATING EXPENSES | | |
| Administration of tribunals | 67,345,000 | 65,981,000 |
| Elections | 2,554,000 | 3,678,000 |
| Publications and education | 3,453,000 | 3,387,000 |
| General and administration | 3,380,000 | 3,197,000 |
| Total | 76,732,000 | 76,243,000 |
| Net operating loss | (7,185,000) | (1,841,000) |
| NON OPERATING INCOME AND EXPENSES | | |
| Interest and dividends on investments, net of fees (Note 2) | 2,635,000 | 1,809,000 |
| Net realized and unrealized gains on investments | 2,249,000 | 4,202,000 |
| Contribution expense (Note 6) | (623,000) | (799,000) |
| Loss on disposal of assets (Note 4) | (649,000) | (3,000) |
| Change in unrestricted net assets before minimum pension liability and discontinued operations | (3,573,000) | 3,368,000 |
| Minimum pension liability adjustment (Note 3) | 346,000 | 4,000 |
| Change in unrestricted net assets before discontinued operations | (3,227,000) | 3,372,000 |
| Discontinued operations (Notes 4 and 7) | - | (156,000) |
| Change in unrestricted net assets | (3,227,000) | 3,216,000 |
| Unrestricted net assets, beginning of year | 27,130,000 | 23,914,000 |
| Unrestricted net assets, end of year | \$ 23,903,000 | \$ 27,130,000 |

See Notes to Consolidated Financial Statements.

**CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2005 AND 2004**

| OPERATING ACTIVITIES | <u>2005</u> | <u>2004</u> |
|--|---------------------------------|---------------------------|
| Change in net assets | \$ (3,227,000) | \$ 3,216,000 |
| Adjustments to reconcile the change in net assets to net cash provided by operating activities: | | |
| Depreciation and amortization | 3,817,000 | 3,690,000 |
| Net realized and unrealized gain on investments | (2,249,000) | (4,202,000) |
| Postretirement benefits other than pensions | 441,000 | 612,000 |
| Loss on disposal of assets | 649,000 | 327,000 |
| Changes in operating assets and liabilities: | | |
| Decrease/(Increase) in administration fees receivable | 6,777,000 | (1,822,000) |
| Increase in other receivables | (138,000) | (33,000) |
| Decrease/(Increase) in prepaid expenses and other assets | 247,000 | (204,000) |
| (Decrease)/Increase in accounts payable and accrued expenses | (1,626,000) | 1,233,000 |
| Increase/(Decrease) in accrued pension liability | 936,000 | (242,000) |
| Decrease in deferred rent | (609,000) | (638,000) |
| (Decrease)/Increase in deferred revenue | (92,000) | 623,000 |
| Net cash provided by operating activities | <u>4,926,000</u> | <u>2,560,000</u> |
| INVESTING ACTIVITIES | | |
| Purchase of furnishings, equipment, and leasehold improvements | (1,375,000) | (1,230,000) |
| Proceeds from sales of investments | 66,821,000 | 6,000 |
| Purchase of investments | (69,743,000) | (6,168,000) |
| In-progress construction | (31,000) | (530,000) |
| Net cash used in investing activities | <u>(4,328,000)</u> | <u>(7,922,000)</u> |
| Net increase/(decrease) in cash and cash equivalents | 598,000 | (5,362,000) |
| Cash and cash equivalents, beginning of year | <u>—</u> | <u>5,362,000</u> |
| Cash and cash equivalents, end of year | <u><u>\$ 598,000</u></u> | <u><u>\$ —</u></u> |

See Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BUSINESS AND PRINCIPLES OF CONSOLIDATION

The accompanying consolidated financial statements include the financial position and operating activities of the American Arbitration Association, Inc. and the subsidiaries it controls, ADRWorld.com and The International Centre for Dispute Resolution, LLC. All intercompany accounts and transactions have been eliminated in consolidation. As used herein, the "Association" includes the American Arbitration Association, Inc. and subsidiaries.

The American Arbitration Association, Inc. ("AAA") is a not-for-profit organization that provides administrative, educational, and development services for the widespread use of dispute resolution procedures.

ADRWorld.com ("ADRW"), a Delaware limited liability company, delivers via the internet alternative dispute resolution news research and industry information.

The International Centre for Dispute Resolution, LLC ("ICDR, LLC"), an Irish subsidiary of the Association, promotes, facilitates, and provides dispute management services.

ADMINISTRATION FEES

The initial filing fee for commercial cases, which is subject to a minimum fee, is billed at the commencement of the dispute resolution process. Over the next 60 days, which is the time period for refund eligibility, a portion of the refundable initial filing is recognized as revenue as services are performed. Under certain circumstances the 60-day time period for refund eligibility is extended indefinitely for arbitration cases that utilize the AAA's mediation services. Based on analysis of current trends, the Association recorded a provision for deferred revenue in 2005 and 2004 of \$39,000 and \$78,000, respectively, which is included in the accompanying consolidated balance sheets and represents the estimated amount of future refunds.

A case service fee is payable in advance prior to the first scheduled hearing. The case service fee is refundable at the conclusion of the case if no hearings have occurred. Case service fee revenue is recognized, net of estimated refunds, as case administration services are provided.

Deferred case service fee revenues of \$1,933,000 and \$1,949,000 as of December 31, 2005 and 2004, respectively, are included in deferred revenue in the accompanying consolidated balance sheets.

CONTRIBUTIONS

The Association contributed money to fund expenses incurred by the Global Center for Dispute Resolution Research ("GCDRR"). On an annual basis, the Association also contributes money to the ICDR, LLC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

CASH AND CASH EQUIVALENTS

The Association considers all highly liquid investments with maturities of three months or less on date of purchase to be cash equivalents.

CONCENTRATIONS OF CREDIT RISK

Financial instruments, which potentially subject the Association to concentrations of credit risk, include cash and cash equivalents and administration fees receivable. The Association maintains cash and cash equivalents in bank deposit and other accounts, the balances of which, at times, may exceed federally insured limits. The Association places its cash and cash equivalents with creditworthy, high-quality financial institutions. Credit risk with respect to fees receivable is also limited because the Association deals with a large number of customers in a wide geographic area. The Association closely monitors the extension of credit to its customers while maintaining allowances for potential credit losses. On a periodic basis, the Association evaluates its fees receivable and establishes an allowance for doubtful accounts, based on a history of past write-offs and collections and current credit considerations.

INVESTMENTS

Investments are reported at fair value. Cash equivalents included in investments are held for investment purposes. Changes in unrealized investment gains or losses are reported in the statements of operations and changes in net assets.

FURNISHINGS, EQUIPMENT, AND LEASEHOLD IMPROVEMENTS

Furnishings, equipment, and leasehold improvements are stated at cost. Depreciation and amortization are computed using the straight-line method over the estimated useful lives of the individual asset or the lease term, if shorter than the useful life. The cost of maintenance and repairs is charged to expense as incurred.

CAPITALIZATION OF SOFTWARE

The Association capitalized expenses incurred for the development of software for internal use in accordance with Statement of Position No. 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use." The costs associated with the development of software are amortized over five years.

USE OF ESTIMATES

The preparation of financial statements in conformity 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. Accordingly, actual results could differ from those estimates.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONCLUDED)

TAX STATUS

The AAA is exempt from federal income tax under the provisions of Section 501(c)(3) of the Internal Revenue Code; therefore, no provision for income taxes is included in the Association's consolidated financial statements.

ICDR, LLC is a taxable entity in Ireland. There are no provisions for income taxes for 2005 and 2004 due to losses incurred. As of December 31, 2005 and 2004, ICDR, LLC has offset the deferred tax asset related to its loss carry forwards by a valuation allowance of an equivalent amount as such deferred tax asset is not expected to be realized. Accordingly, there are no credits for income taxes reflected in the accompanying consolidated statements of operations and changes in net assets to offset pretax losses.

As a single member LLC, any taxable income or loss of ADRW is passed on to the member and taxable in accordance with the member's tax status.

FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying amounts of cash and cash equivalents, administration fees receivable, accounts payable, and accrued expenses approximate fair value because of the short-term nature of the items. The fair value of investments is determined by quoted market prices.

RECLASSIFICATIONS

Certain prior year balances have been reclassified to conform with the current year financial statement presentation.

NOTE 2 - INVESTMENTS

Investments at December 31, 2005 and 2004 consist of the following:

| | 2005 | | 2004 | |
|-----------------------------------|----------------------------|----------------------------|----------------------------|----------------------------|
| | Cost | Fair Value | Cost | Fair Value |
| Fixed income funds | \$ 34,117,000 | \$ 33,947,000 | \$ 31,492,000 | \$ 32,185,000 |
| Domestic equity mutual funds | 20,852,000 | 23,494,000 | 17,060,000 | 23,474,000 |
| International equity mutual funds | 7,054,000 | 8,069,000 | 5,258,000 | 7,524,000 |
| Real estate mutual funds | 7,151,000 | 7,841,000 | 4,213,000 | 4,997,000 |
| Totals | <u>\$69,174,000</u> | <u>\$73,351,000</u> | <u>\$58,023,000</u> | <u>\$68,180,000</u> |

Interest and dividends on investments are reported net of fees of \$560,000 and \$404,000 in 2005 and 2004, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 3 - PENSION AND OTHER POSTRETIREMENT BENEFITS PLANS

The Association maintains a noncontributory, qualified defined benefit pension plan covering all eligible employees. The Association makes contributions to the plan based on actuarial calculations. Total employer contributions required for the fiscal year beginning January 1, 2006 are zero. The Association expects to make a discretionary contribution of up to \$3,000,000 to the plan during 2006.

The Association also provides certain healthcare benefits for substantially all of its retirees. The Association is required to accrue the estimated cost of these retiree benefit payments during the employees' active service period. The Association pays the cost of the postretirement benefits as incurred.

Employees hired on or after July 1, 2003 are not eligible for retiree healthcare coverage. Active employees hired on or before June 30, 2003 are eligible for retiree healthcare coverage upon retirement with at least 10 years of service after age 45.

The Association also maintains a nonqualified Supplemental Retirement Plan. For 2005 and 2004, the expense associated with this plan, which is included in general and administrative expenses, was \$67,000 and \$51,000, respectively. For 2005 and 2004, the accrued benefit obligation, which is included in accounts payable and accrued expenses, was \$409,000 and \$342,000, respectively.

The following tables set forth each plan's funded status and amounts recognized in the Association's financial statements at December 31, 2005 and 2004:

| | Pension Benefits | | Other Benefits | |
|--|-----------------------|-----------------------|-----------------------|----------------------|
| | 2005 | 2004 | 2005 | 2004 |
| Benefit obligation at December 31 | \$ 39,235,000 | \$ 37,699,000 | \$ 8,193,000 | \$ 8,150,000 |
| Fair value of plan assets at December 31 | 25,713,000 | 24,888,000 | — | — |
| Funded status | <u>\$(13,522,000)</u> | <u>\$(12,811,000)</u> | <u>\$(8,193,000)</u> | <u>\$(8,150,000)</u> |
| Accrued benefit costs recognized in the balance sheets | <u>\$ (9,944,000)</u> | <u>\$ (9,134,000)</u> | <u>\$ (9,668,000)</u> | <u>\$(9,227,000)</u> |
| Benefit costs | \$ 2,999,000 | \$ 2,762,000 | \$ 782,000 | \$ 966,000 |
| Employer's contribution | 1,715,000 | 3,000,000 | 341,000 | 354,000 |
| Plan participants' contributions | — | — | 21,000 | 14,000 |
| Benefits paid | 2,327,000 | 2,396,000 | 362,000 | 368,000 |
| Weighted-average assumptions to determine the benefit obligation as of December 31: | | | | |
| Discount rate | 5.75% | 5.75% | 5.75% | 5.75% |
| Expected return on plan assets | 7.50% | 7.50% | N/A | N/A |
| Rate of compensation increase | 4.80% | 5.30% | N/A | N/A |
| Weighted-average assumptions to determine the net benefit cost for the year ended December 31: | | | | |
| Discount rate | 5.75% | 6.00% | 5.75% | 6.00% |
| Expected return on plan assets | 7.50% | 7.50% | N/A | N/A |
| Rate of compensation increase | 4.80% | 5.30% | N/A | N/A |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 3 - PENSION AND OTHER POSTRETIREMENT BENEFITS PLANS (CONTINUED)

The accumulated benefit obligation related to the defined benefit pension plan as of December 31, 2005 and 2004 was \$35,658,000 and \$34,022,000, respectively.

For measurement purposes, an 8.25% annual rate of increase in the per capita cost of covered healthcare benefits was assumed for 2006. The rate was assumed to decrease gradually to 4.50% until 2011 and remain at that level thereafter.

The pension plan provides a benefit equal to the sum of (a) for each year of benefit accrual service (or any fractional part thereof) credited on or before January 1, 1997, 1.75% of earnings in effect on January 1, 1997, and (b) for each year of benefit accrual service credited after January 1, 1997, 1.75% of earnings in effect on January 1 of such year.

The provisions of SFAS No. 87, "Employers' Accounting for Pensions" ("SFAS 87"), require the Association to recognize a minimum pension liability relating to certain unfunded obligations, establish an intangible asset relating thereto, and adjust net assets. At year-end, this minimum pension liability is remeasured as required by SFAS 87. As a result, at December 31, 2005 and 2004, the Association's additional minimum liability was \$9,439,000 and \$9,911,000, respectively, and the related intangible asset was \$520,000 and \$646,000, respectively. Net assets increased by \$346,000 and \$4,000 in 2005 and 2004, respectively, to reflect the net change in the additional minimum liability offset by the net change in the related intangible asset. The Association recognized an accrued pension liability in 2005 of \$9,944,000, which is related to the accrued benefit cost of \$505,000 and an additional minimum liability of \$9,439,000. The Association recognized an accrued pension liability in 2004 of \$9,134,000, which is related to the prepaid benefit cost of \$777,000 and an additional minimum liability of \$9,911,000.

Estimated future benefit payments attributable to estimated future employee service in each of the five years subsequent to December 31, 2005 and in the aggregate for the five years beginning in 2011 are as follows:

| <u>January 1,</u> | <u>Pension Benefits</u> | <u>Other Benefits</u> |
|-------------------|-------------------------|-----------------------|
| 2006 | \$ 2,442,000 | \$ 349,000 |
| 2007 | 2,456,000 | 384,000 |
| 2008 | 2,523,000 | 410,000 |
| 2009 | 2,597,000 | 423,000 |
| 2010 | 2,625,000 | 455,000 |
| Thereafter | 14,831,000 | 2,676,000 |

The target allocations of pension assets are outlined below:

| | <u>Target Allocation</u> | <u>Percentage of Plan Assets at December 31,</u> | |
|-------------------------------------|------------------------------|--|--------------------|
| | | <u>2005</u> | <u>2004</u> |
| Plan assets: | | | |
| Equity securities | 40 - 70% | 55% | 56% |
| Fixed income/Group annuity contract | 30 - 60% | 45 | 44 |
| Total | | <u>100%</u> | <u>100%</u> |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 3 - PENSION AND OTHER POSTRETIREMENT BENEFITS PLANS (CONCLUDED)

The overall objective of these allocations is to provide for long-term growth while maintaining an acceptable level of risk. The expected long-term rate of return on assets is 7.5%. The assumption is based on future rates of return for the investment portfolio, with consideration given to the distribution of investments by asset class and historical rates of return for each individual asset class. All investments are chosen with prudence and due diligence by investment managers to ensure that results over time meet the goals and objectives of the Association's Pension Investment Objectives and Policies Statement.

The Medicare Prescription Drug, Improvement, and Modernization Act of 2003 ("DIMA") introduces a prescription drug benefit under Medicare, as well as a Federal subsidy to sponsors of retiree medical benefit plans that provide a benefit that is similar to Medicare. In accordance with Financial Accounting Standards Board Staff Position ("FSP") No. 106-2, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement, and Modernization Act of 2003," the Association has elected to recognize the effects of DIMA on its retiree medical benefits expense in 2005. Due to the inclusion of DIMA, the plan's benefit obligation decreased by \$1,777,000 in 2005. The reduction in the net periodic postretirement benefit cost for 2005 was \$218,000.

NOTE 4 - FURNISHINGS, EQUIPMENT, AND LEASEHOLD IMPROVEMENTS

Furnishings, equipment, and leasehold improvements consist of the following:

| | 2005 | 2004 |
|--|-----------------------------|-----------------------------|
| Furnishings and equipment | \$ 17,961,000 | \$ 18,591,000 |
| Leasehold improvements | 14,314,000 | 14,576,000 |
| | <u>32,275,000</u> | <u>33,167,000</u> |
| Less accumulated depreciation and amortization | (21,203,000) | (19,528,000) |
| Total | <u>\$ 11,072,000</u> | <u>\$ 13,639,000</u> |

In 2005 and 2004, the Association recognized a net loss of approximately \$649,000 and \$327,000 relating to the disposal of certain assets with original costs totaling \$2,789,000 and \$1,115,000, respectively. Included in these amounts and recorded as part of operations in 2005 were \$650,000 in losses related to the disposal of certain assets due to office consolidations that had original costs of \$1,622,000. In 2004, and recorded in discontinued operations, were \$324,000 in losses related to the disposal of certain assets with original costs of \$790,000.

Furnishings and equipment as of December 31, 2005 and 2004 includes costs associated with the development of software for internal use of \$4,907,000. Related accumulated amortization for 2005 and 2004 were \$4,457,000 and \$3,476,000, respectively.

Included in prepaid expenses are in-progress construction costs for leased facilities of \$31,000 in 2005 and \$530,000 in 2004. When placed into service, these in-progress construction costs will be included in capital assets and amortized over the lives of the underlying leases. In-progress construction amounting to \$524,000 and \$499,000 was completed and placed into service during 2005 and 2004, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 5 - COMMITMENTS AND CONTINGENCIES

LEASE COMMITMENTS

The Association conducts all of its activities from leased office space and is currently a party to various leases that expire between 2006 and 2017. Most of the leases provide for future escalation charges relating to real estate taxes and other building operating expenses. Rental expenses charged to continuing operations for the years ended December 31, 2005 and 2004 amounted to \$12,499,000 and \$12,034,000, respectively. In addition, the Association leases certain computer equipment under various operating leases, all of which expire over the next one to five years.

Due to the consolidation of certain offices during 2005, AAA recorded expenses of approximately \$652,000, which accounted for future lease payments and related costs and early termination payouts for those leased offices. These expenses are included in the administration of tribunals in the accompanying consolidated statements of operations and changes in net assets. The related liability of \$652,000 is included in accounts payable and accrued expenses in the accompanying 2005 consolidated balance sheet.

Minimum noncancelable lease commitments for office facilities, equipment, and software, exclusive of any future escalation charges, due in each of the five years subsequent to December 31, 2005 and thereafter are as follows:

| <u>Year Ending December 31,</u> | <u>Amount</u> |
|---------------------------------|-----------------------------|
| 2006 | \$ 9,787,000 |
| 2007 | 9,350,000 |
| 2008 | 7,780,000 |
| 2009 | 7,418,000 |
| 2010 | 7,053,000 |
| Thereafter | <u>22,542,000</u> |
| Total | <u>\$ 63,930,000</u> |

CONTINGENCIES

The Association is a defendant in certain lawsuits arising in the ordinary course of business. While the outcome of lawsuits or other proceedings against the Association cannot be predicted with certainty, the Association does not expect that those matters will have a material adverse effect on its consolidated financial position.

The Association bills and collects amounts in advance for unearned arbitrators' compensation. At December 31, 2005 and 2004, advance deposits collected totaled \$52,867,000 and \$52,988,000, respectively. These amounts are included in accounts payable and accrued expenses in the accompanying consolidated balance sheets.

The Association has a letter of credit agreement totaling \$1,065,000 at December 31, 2005. This agreement guarantees an operating lease rental obligation and is secured by the investment portfolio.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**NOTE 6 - GLOBAL CENTER FOR DISPUTE RESOLUTION RESEARCH**

In the ordinary course of business, the Association has made contributions to GCDRR, a research organization dedicated to exploring the effectiveness and enhancing the utility of business dispute resolution methods throughout the world. These contributions, which were used to fund expenses incurred by GCDRR, reflected an economic interest by the Association. Since the Association maintained only a minority voting interest on GCDRR's Board of Directors, the Association did not have direct control over how GCDRR operated or derived other contributions. In accordance with Statement of Position 94-3, "Reporting of Related Entities by Not-for-Profit Organizations," the Association did not consolidate the operating results of GCDRR and, accordingly, reports these contributions on the statements of operations and changes in net assets.

As of August 1, 2005, GCDRR's Board of Directors agreed to dissolve itself and to place control of GCDRR with the CEO and chairmen of the Association. The Association, as the primary contributor to GCDRR, has also ceased contributing to GCDRR as of August 1, 2005.

For the years ended December 31, 2005 and 2004, amounts contributed to GCDRR totaled \$623,000 and \$799,000, respectively. Contributions to GCDRR have aggregated \$3,787,000 through December 31, 2005.

NOTE 7 - DISCONTINUED OPERATIONS

As of April 15, 2004, the Association no longer administers the New Jersey Personal Injury Protection ("no-fault") Program. Included in the 2004 statement of operations and changes in net assets are net no-fault revenues of \$3,460,000 and direct expenses, excluding corporate shared services costs, of \$3,616,000. Included in the direct expenses are one-time charges related to the disposal of assets as well as an accrued liability for future arbitrator compensation, direct payroll costs, and operating costs totaling \$821,000. These accrued costs represent the estimated cost of completing the administration of cases pending at December 31, 2004. As of December 31, 2005, the accrued liability amounted to \$54,000.



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