

BUSINESS ADVISORY LETTER

The Executive Board
National Active and Retired Federal Employees Association

We recently completed our audit of the financial statements of National Active and Retired Federal Employees Association (NARFE) as of and for the year ended December 31, 2010. We would like to again bring the following matter to your attention. This matter is an observation only and does not represent a significant deficiency or material weakness in your system of internal control that would have impacted our audit scope.

CONTINUED FINANCIAL TRENDS

During the year ended December 31, 2010, NARFE experienced another significant operating loss of approximately \$1,300,000. Coupled with the operating losses for 2008 and 2009, NARFE has incurred approximately \$3 million in operating losses during the past three years. The primary reason for this decline is the loss of members and the resulting decline in dues revenues. We are aware that the National Executive Board (NEB) and management have identified several new revenue producing options, including a dues increase that was effective January 1, 2011. However, with the continued downward trend in the number of members over the past three years, the most likely scenario for dues income for 2011 would be to remain flat (primarily because of the dues rate increase), or at least not drop significantly.

Salaries and benefits continue to rise as staffing levels have remained constant, even though revenues are decreasing significantly. Since January 1, 2008, salaries and benefits have increased approximately 14 percent while dues (the primary revenue source) have declined 9 percent. The gap between declining revenue and increasing expenses has been covered by tapping into NARFE's investment reserves.

Considering the stock market plunge during the early part of the recession, the subsequent partial upswing, and the amount of withdrawals to fund operations, NARFE's reserves at the end of 2010 were approximately 31 percent less at December 31, 2010, than at January 1, 2008. Assuming an estimated operating loss of approximately \$1 million per year, it is not difficult to project that if new revenue programs and/or effective cost-cutting measures are not implemented in the near term, NARFE will face the possibility of totally consuming its existing reserves within the next four-to-five years and be faced with the task of identifying other, more expensive means to finance operations, such as bank financing. Ultimately, NARFE could face the possibility of a significant downsizing to survive, or consider a possible sale of the NARFE building to provide funds for continuing operations.

We recommend that the NEB consider engaging a management consultant to assist you in assessing NARFE's staffing and related office space needs, outsourcing certain production functions, and in considering the possibility of either selling or subleasing some part of the NARFE building. The objective of such a review would be to identify those strategies that could be implemented in the near term to reverse the trends of the past several years. We will be happy to provide the NEB with several individuals who specialize in operational consulting for not-for-profit organizations.

We would like to extend our appreciation to Richard Ostergren, Charles Saylor, Tayo Coker Polson and their staff for their cooperation during our audit. If you should have any questions, please contact us.

Councilor, Buchanan & Mitchell, P.C.,
Certified Public Accountants
Bethesda, Maryland
March 25, 2011

the year ended December 31, 2010.

NOTE 7. SUBSEQUENT EVENTS

The Association and Affiliate have evaluated subsequent events through March 24, 2011, the date on which the financial statements were available to be issued. ■

Additional Financial Information

The report of the National Executive Board Audit Committee and additional financial information required under the NARFE Bylaws to be published annually in NARFE magazine may be found on p. 44 of this issue.