TREASURER'S REPORT

Paul L. Craig, PhD
Treasurer

. . . Cost reductions, in concert with the development of our strategic plan, should set APA on a course that will preserve our resources and allow us to continue to deliver the products and services deserving of our membership.

As we all know, every facet of the business community and our own personal lives have been affected by the worldwide economic downturn. The American Psychological Association has been anything but immune; in many ways, 2008 was a "perfect storm" for APA. The economic downturn impacted all aspects of our 2008 financial operations:

- We sustained substantial losses from APA operations of roughly $4.9 million (after consideration of a $2.5 million operational subsidy from building cash flow and net activity from APA Board of Directors' designations of $678,000).
- We took advantage of the favorable interest rate environment in 2008 and refinanced our long-term debt. By refinancing, we lowered our interest rate, extended the bank's commitment, extended the amortization of principal, and simplified our reporting requirements. To do this, we had to absorb a prepayment penalty ($3.69 million) to pay off our existing obligations. In short, we traded the prepayment penalty for long-term stability and certainty.
- Our long-term investment portfolio was severely affected by the 2008 Wall Street freefall, and our long-term assets declined (on paper) from $72 million at the beginning of 2008 to $39.8 million as of December 31, 2008.
- The market values of the interest rate swaps declined (on paper) by nearly $15.8 million as of December 31, 2008, because of the steep decline in long-term interest rates.

The good news is that our long-term portfolio is recovering nicely (as of May 31, 2009), the entire prepayment penalty was absorbed in 2008 and will not recur in 2009, and management and governance are taking significant steps to balance the 2009/2010 operating budgets.

TABLE 1 INCOME AND EXPENSE STATEMENT

APA OPERATIONS (UNCONSOLIDATED)

	2005	2006	2007	2008
REVENUES				
Dues and fees	$13,925	$14,038	$14,695	$14,531
Journal subscriptions	18,903	17,891	16,933	16,736
Licensing/royalties	31,037	32,971	37,805	42,052
Sales	15,451	15,093	14,608	14,212
Other	17,550	17,163	16,285	15,517
Total Revenues	**$96,866**	**$97,156**	**$100,326**	**$103,048**
EXPENSES				
Salaries and benefits	$44,713	$45,476	$47,560	$52,322
Publication production costs	8,432	9,591	9,093	9,960
Space costs	8,249	8,130	8,609	8,801
Boards/committees	2,034	2,367	2,608	2,786
Consulting/contractual	10,001	11,240	11,199	11,898
Other	21,123	23,909	23,059	25,436
Total Expenses	**$94,552**	**$100,713**	**$102,128**	**$111,203**
Net Gain/(Loss) From APA Operations	**$2,314**	**$(3,557)**	**$(1,802)**	**$(8,155)**

NONOPERATING ACTIVITY (CONSOLIDATED)

	2005	2006 Restated[a]	2007	2008
LONG-TERM INVESTMENT ACTIVITY				
Realized gain/(loss) on sale of investments & interest on LT	$1,109	$1,961	$4,823	$(3,387)
Investment management fees	(392)	(446)	(505)	(464)
Unrealized gain/(loss) - (Net) (FAS 124)	1,981	7,134	(1,495)	(28,046)
Net Long-Term Investment Activity	**$2,698**	**$8,649**	**$2,823**	**$(31,897)**
REAL ESTATE ACTIVITY				
Ten G Street operations	$1,429	$429	$808	$2,166
750 First Street operations	3.520	4,048	5,465	5,823
Unrealized gain/(loss) on interest rate swap (LLC)	1,500	467	(1,635)	(10,036)
Unrealized gain/(loss) on interest rate swap (APA)	—	—	—	(5,738)
Series B interest	(2,148)	(2,148)	(2,148)	(512)
Interest on 750 term loan (BoA)	—	—	—	(1,056)
Deferred rent	633	149	(806)	(545)
Prepayment penalty & financing costs	—	—	—	(3,604)
Net Real Estate Activity	**$4,934**	**$2,945**	**$1,684**	**$(13,502)**
OTHER NONOPERATING ACTIVITY				
Deferred income tax fluctuation	$(992)	$(144)	$(811)	$(342)
Income tax expense	(60)	1	(55)	(248)
Retiree gap insurance adjustment (FAS 158)	—	—	(719)	—
Net Other Nonoperating Activity	**(1,052)**	**(143)**	**(1,585)**	**(590)**
Total Nonoperating Activity	**$6,580**	**$11,451**	**$2,922**	**$(45,989)**

(All figures shown in thousands. BoA = Bank of America; FAS = Financial Accounting Standards; LT = long-term investments.)

[a]Restated to reflect a change in accounting method to adopt the appropriate recording of an income tax provision for Ten G LLC.

TABLE 2 BALANCE SHEET (CONSOLIDATED)

	2005	2006 Restated[a]	2007	2008
ASSETS				
Cash and ST investments	$49,186	$49,749	$46,249	$42,345
Long-term investment portfolio	56,873	67,536	72,051	39,756
Real estate/equipment	81,668	79,309	81,617	82,679
Other	31,526	32,154	34,530	35,913
Total Assets	**$219,253**	**$228,748**	**$234,447**	**$200,693**
LIABILITIES				
Divisions/other groups	$5,679	$6,523	$7,311	$9,552
Long-term debt/swap liability	117,468	115,338	114,517	131,828
Accounts payable/accrued expenses/other	15,697	14,669	18,106	19,146
Deferred revenues	44,686	47,693	48,802	48,506
Total Liabilities	**$183,530**	**$184,223**	**$188,736**	**$209,032**
Net Assets	**35,723**	**44,525**	**45,711**	**(8,339)**
Total Liabilities and Net Assets	**$219,253**	**$228,748**	**$234,447**	**$200,693**

(All figures shown in thousands. ST = short term.)

[a] Restated to reflect a change in accounting method to adopt the appropriate recording of an income tax provision for Ten G LLC.

Operations

During the summer of 2008, it was clear that the recession was upon us and that action was needed to minimize its impact on APA operations. Fortunately, our 2008 revenues were up 2.8% over 2007 levels, but there was little time to control expenses in a reasoned and thoughtful manner. Salary savings planned for in the 2008 probable were not realized because of record-low staff turnover during the year. We had inflation to absorb and contractual obligations to meet, and, for 2008, our overall expenses exceeded 2007 levels by 8.8%. In the end, we sustained a sizeable loss from operations of approximately $4.9 million ($8.155 million loss less the $2.5 million from the building cash flow and the $678,000 net activity from the APA Board designations) (see Table 1).

APA implemented various cost control measures in late 2008 to curtail the growing operating deficit, most notably a hiring freeze effective November 2008 and an association-wide reduction in staff travel, consulting, and contractual and special projects. Management and governance have agreed on massive expense reductions in an attempt to adjust operational expenses and balance the 2009 and future budgets in a reasoned and thoughtful manner.

Building Operations

In 2008, operations for the Ten G Street and the 750 First Street buildings resulted in solid gains, with net income of $2.2 million from the Ten G LLC and $5.8 million from the 750 LLC. However, the 750 LLC gain excludes the $10 million paper loss resulting from the change in the value of the interest rate swap. The buildings distributed a total of $5.31 million in cash to APA in 2008.

In spite of the current economic challenges, we are pleased to report that our buildings remain 100% leased, and demand for space is growing. Amtrak, one of APA's tenants, is in an expansion mode due to their receipt of stimulus funding from the federal government and their business plan to consolidate near Union Station in Washington, DC. During the latter part of 2008, Amtrak expanded by 9,141 square feet in APA's building at Ten G

TABLE 3 CONSOLIDATED NET ASSETS SUMMARY

	2005	2006 Restated [a]	2007	2008
Net Assets Beginning Balance (Consolidated)	**$26,290**	**$36,358**	**$44,525**	**$45,711**
APA operations (see also Table 1)	2,314	(3,557)	(1,802)	(8,155)
APA nonoperating activity (see also Table 1)	6,580	11,451	2,922	(45,989)
APAPO operations	539	273	66	94
Total Change in Net Assets	**$9,433**	**$8,167**	**$1,186**	**$(54,050)**
Prior Period Adjustment–Ten G LLC[b]	635	—	—	—
Net Assets Ending Balance (Consolidated)	**$36,358**	**$44,525**	**$45,711**	**$(8,339)**
COMPOSITION OF ENDING NET ASSETS				
APA unrestricted/undesignated activities	$30,206	$38,238	$31,454	$(22,012)
Designated activities				
Publications and Databases R & D	1,888	1,654	2,181	2,489
Accreditation	2,095	2,141	1,985	1,647
APAPO	2,169	2,442	2,508	2,602
Convention	—	50	198	441
Web relaunch	—	—	7,385	6,494
Ending Net Assets, Unrestricted	**$36,358**	**$44,525**	**$45,711**	**$(8,339)**

(All figures shown in thousands. APAPO = APA Practice Organization; R & D = research and development.)

[a] Restated to reflect a change in accounting method to adopt the appropriate recording of an income tax provision for Ten G LLC.

[b] Prior period adjustment primarily represents tax refunds due to Ten G LLC resulting from net operating loss carry forwards not previously reported.

Street. Under negotiation are an additional 8,653 square feet of space in the Ten G Street building and potentially 10,000–14,000 square feet in APA's 750 First Street building. APA has consolidated over 7,000 square feet of its space at Ten G Street into existing space at 750 First Street. APA is reviewing alternatives to use its space more efficiently to create even more leasable square footage and reduce APA's occupancy expense.

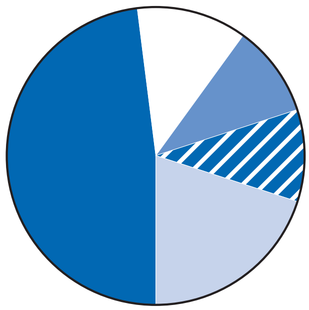
Effects of Noncash Items on the Balance Sheet

As mentioned previously, APA's long-term stock portfolio was not insulated from the significant market downturn in 2008. APA incurred realized losses of $3.4 million, unrealized losses of $28 million, and net management fees, dividend and interest earnings, and a transfer of dividend and interest earned during 2007 from the long-term portfolio to short-term working capital, which reduced our portfolio by $32.2 million—from $72 million as of January 1, 2008, to $39.8 million as of December 31, 2008. Although our 2008 year-to-date performance was down 44%, the performance since inception (March 31, 1988) net of fees was up 9.85% in spite of the challenging period experienced during 2008. From January 1, 2009, through May 31, 2009, the portfolio has recorded a return of 14% and has just reached a value of $45 million (see Long-Term Portfolio chart on p. 332; see also Table 2).

The market values of the interest rate swaps concerning APA and the APA 750 LLC declined by nearly $15.8 million as of year end due to the steep decline in the long-term interest rate market.

Because of the significant "paper" entries needed to adjust the long-term investments and interest rate swap valuations, as well as the other factors described previously,

LONG-TERM PORTFOLIO COMPOSTION



48% LARGE-CAP VALUE
12% INTERNATIONAL VALUE
10% SMALL-CAP VALUE
10% MID-CAP GROWTH
20% SMALL-CAP GROWTH

VALUE 58% GROWTH 30% INTERNATIONAL 12%

PERFORMANCE RETURNS[a]/MARKET VALUE

	2008	MARKET VALUE
Southeastern Asset Management	-49.2%	$ 19.1 M
Westfield Capital Management	-40.3%	7.9 M
Longleaf International Fund	-39.6%	4.8 M
Brandywine Mutual Fund	-43.4%	4.0 M
Advisory Research, Inc.	-26.3%	3.3 M
Lapides	-27.9%	0.6 M
Total	**-44.2%**	**$ 39.7 M**
Total Return Since Inception	**9.8%**	

[a] Returns are net of fees.

APA finds itself in uncharted territory, with negative net assets of $8.3 million as of December 31, 2008 (see Table 3). Negative net assets trigger (a) tighter scrutiny by our lenders (Bank of America) and credit rating agency (Standard & Poor's) and may result in (b) increased debt interest and more rigorous reporting requirements, (c) greater focus by third parties on our fiscal controls, and (d) debt covenant violations.

It is important to remember that our audited financial statements do not reflect the equity we have in our buildings—equity that is conservatively estimated to be in excess of $150 million. However, because that equity is not readily accessible to support operations, it is important that we maintain solid controls over our expenditures through 2009 and rebuild our net assets under the one arm of APA over which management has a great deal of control.

Debt Refinance

In May 2008, APA and the APA 750 LLC refinanced the long-term debt associated with the 750 First Street building. This action lowered interest costs, extended the bank's commitment for an unprecedented 10 years, extended amortization of principal, and simplified reporting requirements.

Total consolidated debt increased by $4.1 million to cover the cost of the prepayment penalty on the Series B Notes of approximately $3.5 million, closing costs, and accrued interest. Lower interest rates combined with the lower bank credit spread resulted in an average rate on the new debt of 5.24%, compared with 6.42% before the refinancing. This interest rate differential resulted in an annual interest savings of approximately $620,000.

Summary

To be sure, 2008 was a year to remember. On the positive side, the Council of Representatives, the Board of Directors, the Finance Committee, the members of APA governance, the CEO, senior management, and the entire staff have

APA'S PUBLIC CREDIT RATING

In spite of the challenging 2008 results, Standard & Poor's (S&P) reaffirmed APA's BBB+ rating with a stable outlook (upgraded from BBB in September 2006). S&P cited the following positive attributes of APA's operations:

- A long, positive operating history
- Diverse revenue streams
- Revenue flexibility supported by APA's ability to increase dues and subscription prices while reducing operating expenses
- An increase, albeit a modest 2%, in membership for the first time in at least 7 years
- Adequate financial resources

Offsetting credit factors include:

- Balance sheet exposure risk due to real estate holdings and the associated swaps and debt
- Substantial losses in fiscal 2008 due to investments and swap valuations
- High level of debt
- Subsequent operating challenges

The stable outlook reflects S&P's anticipation that APA will issue no new debt, continue to manage its current debt and derivative instruments, return to balanced operations, and stabilize its membership base.

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tackled this downturn in the economy on multiple fronts in an attempt to preserve APA's financial strength. There have been significant cost reductions at all levels as we position ourselves to deal with whatever comes our way in the future. These cost reductions, in concert with the development of our strategic plan, should set APA on a course that will preserve our resources and allow us to continue to deliver the products and services deserving of our membership. We have weathered many storms in years past, and we are prepared and ready to meet these current challenges as we look positively toward the future.

As always, if you have any questions about the association's finances, please feel free to e-mail your treasurer at *finances@apa.org.* ■