

Financial Statements and Report of Independent
Certified Public Accountants

United Service Organizations, Inc.

December 31, 2009 and 2008

United Service Organizations, Inc.

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Report of Independent Certified Public Accountants

Board of Governors
United Service Organizations, Inc.

We have audited the accompanying statement of financial position of United Service Organizations, Inc. (USO) as of December 31, 2009, and the related statements of activities and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of USO's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from USO's 2008 financial statements and, in our report dated March 23, 2009, we expressed an unqualified opinion on those financial statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America as established by the American Institute of Certified Public Accountants. 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 USO'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 audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of United Service Organizations, Inc. as of December 31, 2009, and the change in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 5, 2010 on our consideration of the USO's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the USO's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

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

Grant Thornton LLP

McLean, Virginia
March 5, 2010

United Service Organizations, Inc.

Statement of Financial Position

| <i>December 31,</i> | 2009 | 2008 |
|---|----------------------|----------------------|
| Assets | | |
| Cash and cash equivalents | \$ 12,223,259 | \$ 17,974,344 |
| Contributions receivable, net | 5,022,507 | 3,518,644 |
| Grants receivable | 5,493,207 | 5,949,605 |
| Other receivables | 472,293 | 716,827 |
| Prepaid expenses and other assets | 1,421,188 | 810,907 |
| Inventory | 2,517,113 | 450,316 |
| Investments | 57,524,642 | 48,233,158 |
| Fixed assets—net | 7,243,070 | 4,644,961 |
| Total Assets | \$ 91,917,279 | \$ 82,298,762 |
| Liabilities and Net Assets | | |
| Liabilities | | |
| Accounts payable and accrued expenses | \$ 8,528,460 | \$ 8,555,162 |
| Deferred rent | 588,843 | 660,014 |
| Total Liabilities | 9,117,303 | 9,215,176 |
| Net Assets | | |
| Unrestricted | | |
| Operating | 21,313,717 | 22,196,896 |
| Board-designated | | |
| Spirit of Hope | 26,064,567 | 21,622,448 |
| Total unrestricted | 47,378,284 | 43,819,344 |
| Temporarily restricted | | |
| Desert Storm Education Fund | 635,880 | 594,066 |
| Spirit of Hope | 5,235,710 | — |
| Time Restriction | 85,000 | 298,356 |
| Ongoing Program Activities | 3,186,188 | 1,571,330 |
| Capital Projects | 572,818 | 1,147,358 |
| USO Councils and Others | 108,173 | 55,209 |
| Total temporarily restricted | 9,823,769 | 3,666,319 |
| Permanently restricted | | |
| Camp Casey | 25,000 | 25,000 |
| Spirit of Hope | 25,572,923 | 25,572,923 |
| Total permanently restricted | 25,597,923 | 25,597,923 |
| Total Net Assets | 82,799,976 | 73,083,586 |
| Total Liabilities and Net Assets | \$ 91,917,279 | \$ 82,298,762 |

The accompanying notes are an integral part of this statement.

United Service Organizations, Inc.

Statement of Activities and Changes in Net Assets

| | 2009 | | | 2008 |
|--|-------------------------|------------------------|------------------------|----------------------|
| | Year ended December 31, | | | |
| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
| Revenue and Support | | | | |
| Programs | | | | |
| USO center revenue | \$ 8,046,772 | \$ — | \$ — | \$ 8,046,772 |
| Contributed materials, facilities and services | 142,256,897 | 6,199,717 | — | 148,456,614 |
| Grants and sponsorships | 15,771,793 | 419,160 | — | 16,190,953 |
| Public support | | | | |
| Corporate, foundation and individual giving | 7,513,039 | 5,582,425 | — | 13,095,464 |
| Direct response | 53,499,646 | 1,941,351 | — | 55,440,997 |
| United way, CFC and other federated | 1,988,080 | — | — | 1,988,080 |
| Investment income (loss) | 4,513,340 | 5,390,923 | — | 9,904,263 |
| Rental and other income | 187,980 | — | — | 187,980 |
| Total Revenue and Support | 233,777,547 | 19,533,576 | — | 253,311,123 |
| Net Assets Released from Restrictions | 13,376,126 | (13,376,126) | — | — |
| Total Revenue and Other Support | 247,153,673 | 6,157,450 | — | 253,311,123 |
| Operating Expenses | | | | |
| Program services | | | | |
| USO operations | 46,480,212 | — | — | 46,480,212 |
| Contributed materials, facilities and services | 146,443,359 | — | — | 146,443,359 |
| Entertainment | 7,221,197 | — | — | 7,221,197 |
| Communications and public awareness outreach | 15,156,647 | — | — | 15,156,647 |
| Total program expenses | 215,301,415 | — | — | 215,301,415 |
| Supporting Services | | | | |
| Fundraising | 16,780,672 | — | — | 16,780,672 |
| Management and general | 11,512,646 | — | — | 11,512,646 |
| Total Supporting Services | 28,293,318 | — | — | 28,293,318 |
| Total Operating Expenses | 243,594,733 | — | — | 243,594,733 |
| Changes in Net Assets | 3,558,940 | 6,157,450 | — | 9,716,390 |
| Net Assets, beginning of year | 43,819,344 | 3,666,319 | 25,597,923 | 73,083,586 |
| Net Assets, end of year | \$ 47,378,284 | \$ 9,823,769 | \$ 25,597,923 | \$ 82,799,976 |

The accompanying notes are an integral part of this statement.

United Service Organizations, Inc.

Statement of Cash Flows

| <i>Year ended December 31,</i> | 2009 | 2008 |
|---|----------------------|----------------------|
| Change in Cash and Cash Equivalents | | |
| Cash Flows from Operating Activities | | |
| Change in net assets | \$ 9,716,390 | \$ (14,398,692) |
| Adjustments to reconcile change in net assets to net cash provided by operating activities: | | |
| Depreciation and amortization | 1,510,117 | 984,501 |
| Contributed investments | (1,110,646) | (523,598) |
| Realized/unrealized (gain) loss on investments | (8,633,278) | 13,116,974 |
| Revenue from contributed inventory | (6,084,277) | (3,385,972) |
| Contributed inventory used | 4,071,022 | 5,063,337 |
| Loss (gain) on disposal of fixed assets | 992 | (3,325) |
| Changes in assets and liabilities | | |
| Contributions receivable | (1,503,863) | 2,583,866 |
| Grants and other receivables | 700,932 | (6,085,825) |
| Prepaid expenses and other assets | (610,281) | (293,763) |
| Inventory | (53,542) | 159,927 |
| Accounts payable and accrued expenses | (26,702) | (228,890) |
| Deferred rent | (71,171) | (52,020) |
| Net Cash Used in Operating Activities | (2,094,307) | (3,063,480) |
| Cash Flows from Investing Activities | | |
| Purchase of fixed assets | (4,110,218) | (1,691,190) |
| Proceeds from the sale of fixed assets | 1,000 | 4,818 |
| Payments under note receivable | — | 46,699 |
| Purchase of investments | (40,643,345) | (32,680,943) |
| Sales of investments | 41,095,785 | 31,889,430 |
| Net Cash Used in Investing Activities | (3,656,778) | (2,431,186) |
| Net Decrease in Cash and Cash Equivalents | (5,751,085) | (5,494,666) |
| Cash and Cash Equivalents, beginning of year | 17,974,344 | 23,469,010 |
| Cash and Cash Equivalents, end of year | \$ 12,223,259 | \$ 17,974,344 |

The accompanying notes are an integral part of this statement.

United Service Organizations, Inc.

Notes to Financial Statements

December 31, 2009 and 2008

NOTE A—ORGANIZATION

United Service Organizations, Inc. (USO) is a Congressionally chartered, civilian, not-for-profit organization devoted exclusively to providing morale, welfare and recreation type services to military personnel and their families worldwide. USO is not part of the United States Government. It relies on the generosity of individuals and corporations to support its activities. For sixty-nine years its mission has been to enhance the quality of life for military personnel and their families by helping them adjust to the special rigors of a transient military lifestyle and by fostering a partnership between the military and civilian communities. To carry out this mission, USO operates Centers at major military installations and airports around the world, produces free celebrity entertainment tours for military personnel, and manages donor-restricted scholarship and crisis funds for the benefit of military personnel and their families.

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying financial statements reflect the accounts of USO Arlington and its domestic and overseas operating centers. All intercompany accounts and transactions have been eliminated.

Chartered stateside USO affiliates are financially autonomous of USO and are, therefore, excluded from USO financial statements.

Use of Estimates

The presentation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

United Service Organizations, Inc.

Notes to Financial Statements—Continued

December 31, 2009 and 2008

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

Net Assets

Net assets, which are composed of unrestricted, temporarily and permanently restricted funds, are described below:

Unrestricted Funds:

- *Operating*—Funds that are generated from general activities and are used to support day-to-day programs and operations.
- *Spirit of Hope*—Funds which have been designated by the Board of Governors to assist the USO in delivering its programs and services for many years into the future. These Board designated contributions and investment earnings are available to fund operations. The fund was established in 1998 with a transfer of funds from the Desert Storm Education Fund. In the event that the Desert Storm Education Fund does not have sufficient resources to meet its obligations as originally intended, the funds transferred from the Desert Storm Education Fund to the Spirit of Hope shall be available to satisfy any such remaining obligations.

Temporarily Restricted Funds:

- *Desert Storm Education Fund*—Contributions restricted to provide for academic or vocational scholarships to surviving family members of casualties of Desert Shield/Storm operations.
- *Time Restriction*—Certain contributions receivable result from multi-year pledges, and accordingly the amounts due in future years (at their discounted value) have been recorded as temporarily restricted until the year when the pledge becomes due.
- *Ongoing Program Activities*—Contributions restricted for various worldwide USO programs, such as Operation USO Care Package, Operation Phone Home, Operation Mail Call, Operation Enduring Care, and United Through Reading.
- *Capital Projects*—Contributions restricted for the establishment, expansion or capital improvements of various USO Centers worldwide.
- *USO Councils and Others*—Donor funds restricted for use in certain regional localities.
- *Spirit of Hope*—Earning on donor-restricted endowment funds classified as temporarily restricted net assets until those amounts are appropriated for expenditure.

United Service Organizations, Inc.

Notes to Financial Statements—Continued

December 31, 2009 and 2008

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

Permanently Restricted Funds:

- *Camp Casey Endowment*—A contribution which has been restricted by the donor to be held in perpetuity, with stipulations on a portion of the earnings to be used for Camp Casey and the remaining to be used for on-going programs and services.
- *Spirit of Hope Endowment Fund*—Funds to be held in perpetuity, with the earnings available to assist the USO in delivering its programs and services for many years into the future. These contributions are from Congressional appropriations and from corporate and individual contributions.

Foreign Currency

USO operates Centers at major military installations around the world. The United States dollar is the functional currency of the USO; however, the USO maintains financial assets and liabilities in foreign currencies to meet the local obligations of the Centers. The financial assets and liabilities in foreign currencies are translated using exchange rates in effect at the end of the period and revenue and costs are translated using weighted average exchange rates for the period.

Cash and Cash Equivalents

USO considers all highly liquid investments purchased with an initial maturity of three months or less to be cash equivalents.

Investments

Investments are reported at fair value. Investment income is presented net of investment advisory/management fees in the accompanying statement of activities. All investment income is reported as a change in unrestricted net assets unless otherwise restricted by the donor.

Fixed Assets

Furniture, fixtures, equipment, and other capitalized assets are recorded at cost and are depreciated using the straight-line method over the estimated useful lives of the respective assets, which range from three to seven years. Leasehold improvements are amortized using the straight-line method over the lesser of the terms of the lease or the expected useful lives of the improvements.

Inventory

Inventories are stated at the lower of cost or market determined on a first-in, first-out basis and average cost methods.

United Service Organizations, Inc.

Notes to Financial Statements—Continued

December 31, 2009 and 2008

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

Contributed Materials and Facilities

Donated facilities, equipment use, supplies and materials received from the United States Government and other donors are reflected in the accompanying financial statements as support to the USO at the estimated fair value when received or when an unconditional pledge to contribute has been made.

Contributed Services

USO recognizes contributions of services received if such services (a) create or enhance non-financial assets or (b) require specialized skills, are provided by individuals possessing those skills and would typically need to be purchased if not contributed.

USO receives contributions of services from celebrities in order to carry out its program of providing free celebrity entertainment tours for military personnel around the world. USO also receives contributions of media air time to promote its Public Service Announcements. These contributions of services are reflected in the accompanying financial statements as support to the USO at the estimated fair value when received. As these contributions of services are expended in the year that the services are provided, a corresponding expense equal to the estimated fair market value of the services provided is recognized in the accompanying financial statements.

In addition, USO receives services from a large number of volunteers who give significant amounts of time to USO's programs. No amounts have been reflected for these types of donated services, as they do not meet the criteria outlined above.

Contributions

All contributions are considered to be available for unrestricted use, unless specifically restricted by the donor. Contributions with temporary, donor-imposed time or purpose restrictions are recorded as temporarily restricted support. A donor restriction expires when a stipulated time restriction ends or when a purpose restriction is accomplished. Upon expiration, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions. Restricted contributions received in the same year in which the restrictions are met are recorded as an increase to temporarily restricted support at the time of receipt and as net assets released from restrictions. The principal and any donor restricted income from permanently restricted contributions are classified as permanently restricted net assets. Income on those assets, not permanently restricted by the donor, is classified as temporarily restricted (if purpose restricted by the donor) or unrestricted net assets.

Unconditional promises to give that are expected to be collected within one year are recorded at their net realizable value. Unconditional promises to give that are expected to be collected in future years are recorded at the present value of their estimated future cash flows. The discounts on those amounts are computed using risk-free interest rates applicable to the years in which the promises are received. The discount rate used in 2008 was 3.4 percent. Amortization of the discounts is included in contribution revenue in the accompanying statement of activities.

United Service Organizations, Inc.

Notes to Financial Statements—Continued

December 31, 2009 and 2008

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

Grants and Sponsorships

Grant revenue on cost-reimbursement grants or contracts is recognized when the USO requests reimbursement from granting agencies after the program expenditures have been incurred. Billed and unbilled receivables of the government grants are expected to be collected within one year and are recorded at net realizable value as grant receivables in the statement of financial position. Such grant programs are subject to independent audit under the Office of Management and Budget Circular A-133 and review by grantor agencies. Such review could result in the disallowance of expenditures under the terms of the grant or reductions of future grant funds. Based on prior experience, the USO's management believes that costs ultimately disallowed, if any, would not materially affect the financial position of the USO.

USO Center Revenue

USO Center Revenue represents amounts collected for cultural tours, canteen operations, gift shops and a variety of other activities of USO Centers located at military installations worldwide. Revenue is recorded when earned.

Concentration of Credit Risk

Financial instruments that potentially subject USO to a concentration of credit risk include cash deposits with commercial banks. USO's cash management policies limit its exposure to a concentration of credit risk by maintaining cash accounts at financial institutions whose deposits are insured by the Federal Deposit Insurance Corporation (FDIC). Cash deposits may exceed the FDIC insurable limit of \$250,000 at times throughout the year due to anticipated large expenses under various projects. As of December 31, 2009, the amount in excess of the FDIC insurable limit was approximately \$9,360,000. Management does not consider this to be a significant credit risk. Amounts in foreign bank accounts total approximately \$867,000 at December 31, 2009.

Functional Allocation of Expenses

The costs of providing various programs and supporting services have been summarized on a functional basis in the accompanying statement of functional expenses. Certain costs have been allocated among the program and supporting services benefited.

Income Taxes

USO is exempt from federal income tax under Section 501(a) of the Internal Revenue Code (IRC) of 1986, as amended, as an organization described in IRC Section 501(c)(3). However, income generated from activities unrelated to the USO's exempt purpose is subject to tax under IRC Section 511. USO did not have any material unrelated business income tax liability for the years ended December 31, 2009 and 2008. Therefore, no tax liability has been provided in the accompanying financial statements.

United Service Organizations, Inc.

Notes to Financial Statements—Continued

December 31, 2009 and 2008

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

Effective in 2009, the USO adopted guidance issued by the Financial Accounting Standards Board (FASB) which creates a single model to address uncertainty in tax positions and clarifies the accounting for income taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in its financial statements. Under the requirements of this guidance, organizations could now be required to record an obligation as the result of tax positions they have historically taken on various tax exposure items. Prior to this pronouncement, the determination of when to record a liability for a tax exposure was based on whether a liability was considered probable and reasonably estimable. The impact of the adoption did not have a material effect on the financial statements of the USO.

New Accounting Pronouncements

In June 2009, the FASB issued new guidance to establish the FASB Accounting Standards Codification (the “Codification”) as the single source of authoritative nongovernmental U.S. generally accepted accounting principles (GAAP). The Codification is effective for interim and annual periods ending after September 15, 2009. The adoption of this standard has not had a material impact on the USO’s financial statements.

Reclassifications

Certain reclassifications have been made to December 31, 2008 amounts to conform to the December 31, 2009 presentation.

NOTE C—CONTRIBUTIONS RECEIVABLE, NET

Unconditional, unrestricted promises to give at December 31, 2009 amounted to \$3,939,005 which was due in less than one year. Temporarily restricted promises to give at December 31, 2009 amounted to \$1,083,502 which was due in less than one year. There was no allowance for uncollectable accounts at December 31, 2009.

Unconditional, unrestricted promises to give at December 31, 2008 amounted to \$3,338,644, of which \$3,290,288 was due in less than one year and \$48,356 was due in less than two years. Temporarily restricted promises to give at December 31, 2008 amounted to \$180,000 which was due in less than one year. An allowance for uncollectable accounts of \$13,128 was recorded at December 31, 2008.

United Service Organizations, Inc.

Notes to Financial Statements—Continued

December 31, 2009 and 2008

NOTE D—INVESTMENTS

At December 31, investments consist of the following:

| | 2009 | 2008 |
|--------------------------------------|----------------------|----------------------|
| Corporate and commercial obligations | \$ 8,787,564 | \$ 10,046,417 |
| U.S. Treasury securities | 618,516 | 1,026,830 |
| Corporate equity securities | 36,449,847 | 32,762,595 |
| Managed futures | 2,328,279 | 2,570,521 |
| Certificates of deposit | — | 260,927 |
| Money market holdings | 9,340,436 | 1,418,472 |
| Other | — | 147,396 |
| | <u>\$ 57,524,642</u> | <u>\$ 48,233,158</u> |

Effective January 1, 2008, the USO adopted new guidance that defines fair value, establishes a framework for measuring fair value, establishes a fair value hierarchy based on the inputs used to measure fair value and enhances disclosure requirements for fair value measurements. The guidance maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the observable inputs be used when available.

Observable inputs are inputs that market participants would use in pricing the asset or liability based on market data obtained from independent sources. Unobservable inputs reflect assumptions that market participants would use in pricing the asset or liability based on the best information available in the circumstances. The hierarchy is broken down into three levels based on the transparency of inputs as follows:

Level 1 – Quoted prices are available in active markets for identical assets or liabilities as of the report date. A quoted price for an identical asset or liability in an active market provides the most reliable fair value measurement because it is directly observable to the market.

Level 2 – Pricing inputs are other than quoted prices in active markets, which are either directly or indirectly observable as of the report date. The nature of these securities include investments for which quoted prices are available but traded less frequently and investments that are fair valued using other securities, the parameters of which can be directly observed.

Level 3 – Securities that have little to no pricing observability as of the report date. These securities are measured using management's best estimate of fair value, where the inputs into the determination of fair value are not observable and require significant management judgment or estimation.

Inputs are used in applying the various valuation techniques and broadly refer to the assumptions that market participants use to make valuation decisions, including assumptions about risk. Inputs may include price information, volatility statistics, specific and broad credit data, liquidity statistics, and other factors. A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. However, the determination of what constitutes "observable" requires significant judgment by the entity.

United Service Organizations, Inc.

Notes to Financial Statements—Continued

December 31, 2009 and 2008

NOTE D—INVESTMENTS—Continued

The USO considers observable data to be that market data that is readily available, regularly distributed or updated, reliable and verifiable, not proprietary, and provided by independent sources that are actively involved in the relevant market. The categorization of a financial instrument within the hierarchy is based upon the pricing transparency of the instrument and does not necessarily correspond to the entity's perceived risk of that instrument.

Investments were recorded at fair value as of December 31, 2009 based on the following level of hierarchy:

| | Amount | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
|--------------------------------------|----------------------|---|---|--|
| Corporate and commercial obligations | \$ 8,787,564 | \$ 6,001,857 | \$ 2,785,707 | \$ — |
| U.S. Treasury securities | 618,516 | 618,516 | — | — |
| Corporate equity securities | 36,449,847 | 36,449,847 | — | — |
| Managed futures | 2,328,279 | — | 2,328,279 | — |
| Money market holdings | 9,340,436 | 9,340,436 | — | — |
| | <u>\$ 57,524,642</u> | <u>\$ 52,410,656</u> | <u>\$ 5,113,986</u> | <u>\$ —</u> |

United Service Organizations, Inc.

Notes to Financial Statements—Continued

December 31, 2009 and 2008

NOTE D—INVESTMENTS—Continued

Investments were recorded at fair value as of December 31, 2008 based on the following level of hierarchy:

| | Amount | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
|--------------------------------------|----------------------|---|---|--|
| Corporate and commercial obligations | \$ 10,046,417 | \$ 4,287,692 | \$ 5,758,725 | \$ — |
| U.S. Treasury securities | 1,026,830 | 1,026,830 | — | — |
| Corporate equity securities | 32,762,595 | 32,762,595 | — | — |
| Managed futures | 2,570,521 | — | 2,570,521 | — |
| Certificates of deposit | 260,927 | 260,927 | — | — |
| Money market holdings | 1,418,472 | 453,914 | 964,558 | — |
| Other | 147,396 | 147,396 | — | \$ — |
| | <u>\$ 48,233,158</u> | <u>\$ 38,939,354</u> | <u>\$ 9,293,804</u> | <u>\$ —</u> |

The following schedule summarizes investment return:

| | 2009 | 2008 |
|-------------------------------|---------------------|------------------------|
| Interest and dividends | \$ 1,469,437 | \$ 1,702,896 |
| Net unrealized gains (losses) | 11,630,960 | (11,853,853) |
| Net realized losses | (2,997,682) | (1,263,121) |
| Less: investment expenses | (198,452) | (249,080) |
| | <u>\$ 9,904,263</u> | <u>\$ (11,663,158)</u> |

United Service Organizations, Inc.

Notes to Financial Statements—Continued

December 31, 2009 and 2008

NOTE E—COMMITMENTS AND CONTINGENCIES

The USO leases various office spaces under long-term lease agreements which expire between 2010 and 2014. The office leases provide for scheduled rent increases and increases in operating expenses and real estate taxes attributable to the leased property. As part of a lease agreement, USO received eight months of free rent on a portion of the space and reimbursement for certain leasehold improvements as lease incentives, which are recorded as deferred rent in the accompanying statement of financial position. Scheduled rent increases and these incentives are being recognized over the term of the lease on a straight-line basis. Future minimum payments under this operating lease and other equipment operating leases are as follows:

| | | |
|------|----|-----------|
| 2010 | \$ | 885,940 |
| 2011 | | 908,357 |
| 2012 | | 925,521 |
| 2013 | | 944,723 |
| 2014 | | 478,091 |
| | | <hr/> |
| | \$ | 4,142,632 |
| | | <hr/> |

For the years ended December 31, 2009 and 2008, total rental expense under all operating leases was \$786,624 and \$738,121, respectively (excluding related in-kind support).

USO is subject to claims and suits arising in the ordinary course of its operations. In the opinion of management, the ultimate resolution of any legal proceedings will not have a material effect on USO's financial position, change in net assets, or cash flows.

United Service Organizations, Inc.

Notes to Financial Statements—Continued

December 31, 2009 and 2008

NOTE F—FIXED ASSETS

At December 31, fixed assets consist of the following:

| | 2009 | 2008 |
|---|----------------------|---------------------|
| Furniture, fixtures, and equipment | \$ 6,333,931 | \$ 4,631,156 |
| Leasehold improvements | 5,138,487 | 3,278,664 |
| Construction in progress | 650,884 | 156,005 |
| | <u>\$ 12,123,302</u> | <u>\$ 8,065,825</u> |
| Less: accumulated depreciation and amortization | (4,880,232) | (3,420,864) |
| | <u>\$ 7,243,070</u> | <u>\$ 4,644,961</u> |

NOTE G—NET ASSETS RELEASED FROM RESTRICTIONS

Net assets were released from temporary donor restrictions by incurring expenses satisfying the restricted purposes specified by the donors or by the passage of time during the years ended December 31, 2009 and 2008, as follows:

| | 2009 | 2008 |
|-----------------------------|----------------------|----------------------|
| Desert Storm Education Fund | \$ 113,400 | \$ 168,987 |
| Time Restricted | 248,356 | 498,374 |
| Ongoing Program Activities | 12,978,892 | 13,326,462 |
| USO Councils and others | 35,478 | 75,925 |
| | <u>\$ 13,376,126</u> | <u>\$ 14,069,748</u> |

United Service Organizations, Inc.

Notes to Financial Statements—Continued

December 31, 2009 and 2008

NOTE H—ALLOCATION OF JOINT COSTS

The USO conducts direct response campaigns that include fund-raising appeals, as well as program and management and general components. The costs of conducting those joint activities were allocated as follows in 2009 and 2008:

| | 2009 | 2008 |
|------------------------|----------------------|----------------------|
| Programs | \$ 8,575,956 | \$ 7,257,420 |
| Management and general | 4,922,818 | 3,855,991 |
| Fund-raising | 10,532,273 | 9,686,529 |
| | <u>\$ 24,031,047</u> | <u>\$ 20,799,940</u> |

NOTE I—CONTRIBUTED MATERIALS, FACILITIES AND SERVICES

A summary by category of in-kind support donated for the years ended December 31, is as follows:

| | 2009 | 2008 |
|------------------------------|-----------------------|-----------------------|
| Materials and facilities | \$ 18,887,384 | \$ 18,222,646 |
| Public Service Announcements | 80,732,724 | 70,026,939 |
| Celebrity entertainment | 48,836,506 | 44,702,003 |
| | <u>\$ 148,456,614</u> | <u>\$ 132,951,588</u> |

NOTE J—RETIREMENT PLAN

USO maintains a defined contribution retirement plan which provides for the purchase of annuity contracts for participants upon their retirement. USO contributes 7.8 percent of each covered employee's annual salary. Employees are 100 percent vested upon five years of service once eligible.

USO's policy is to fund retirement plan costs as accrued. Retirement plan expense was \$1,299,079 and \$887,603 for the years ended December 31, 2009 and 2008, respectively.

United Service Organizations, Inc.

Notes to Financial Statements—Continued

December 31, 2009 and 2008

NOTE K—ENDOWMENT

The Spirit of Hope endowment includes both donor-restricted endowment funds and funds designated by the Board of Governors to function as endowments. As required by GAAP, net assets associated with endowment funds, including funds designated by the Board of Governors to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

During 2008, the District of Columbia enacted into law the Uniform Prudent Management of Institutional Funds Act (UPMIFA). Management of USO has interpreted the District of Columbia law as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, USO classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the organizations in a manner consistent with the standard of prudence prescribed by UPMIFA. As of December 31, 2009, there are no plans for the earnings of the endowment to be spent.

The fair value of assets associated with donor-restricted endowment funds may fall below the level that UPMIFA requires to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature that are reported in unrestricted net assets were \$14,928 as of December 31, 2008. There were no deficiencies of this nature as of December 31, 2009.

USO has adopted an investment policy for the endowment fund. This investment program is based on growing the endowment fund to provide financial stability for the USO in perpetuity with no short term plans for withdrawals from the fund. The USO's ability to tolerate risk and volatility should be consistent with that of a conservative growth portfolio, with investments made in companies that demonstrate consistent growth over time. Asset allocations are developed in accordance with this long-term, conservative growth strategy.

United Service Organizations, Inc.

Notes to Financial Statements—Continued

December 31, 2009 and 2008

NOTE K—ENDOWMENT—Continued

The following illustrates endowment net asset composition by type of fund and the changes in endowment net assets for the year ended December 31:

| 2009 | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|----------------------------------|---------------|---------------------------|---------------------------|---------------|
| Donor-restricted endowment funds | \$ — | \$ 5,235,710 | \$ 25,597,923 | \$ 30,833,633 |
| Board-designated endowment funds | 26,064,567 | — | — | 26,064,567 |
| Total funds | \$ 26,064,567 | \$ 5,235,710 | \$ 25,597,923 | \$ 56,898,200 |

| 2009 | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|--|---------------|---------------------------|---------------------------|---------------|
| Endowment net assets, beginning of year | \$ 21,607,520 | \$ — | \$ 25,597,923 | \$ 47,205,443 |
| Investment return: | | | | |
| Investment income | 570,365 | 674,178 | — | 1,244,543 |
| Net appreciation | 3,871,754 | 4,576,460 | — | 8,448,214 |
| Total investment return | 4,442,119 | 5,250,638 | — | 9,692,757 |
| Adjustment from (to) Unrestricted net assets | 14,928 | (14,928) | — | — |
| Endowment net assets, end of year | \$ 26,064,567 | \$ 5,235,710 | \$ 25,597,923 | \$ 56,898,200 |

United Service Organizations, Inc.

Notes to Financial Statements—Continued

December 31, 2009 and 2008

NOTE K—ENDOWMENT—Continued

The following illustrates endowment net asset composition by type of fund and the changes in endowment net assets for the year ended December 31:

| 2008 | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|----------------------------------|---------------|---------------------------|---------------------------|---------------|
| Donor-restricted endowment funds | \$ (14,928) | \$ — | \$ 25,597,923 | \$ 25,582,995 |
| Board-designated endowment funds | 21,622,448 | — | — | 21,622,448 |
| Total funds | \$ 21,607,520 | \$ — | \$ 25,597,923 | \$ 47,205,443 |

| 2008 | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|---|---------------|---------------------------|---------------------------|---------------|
| Endowment net assets, beginning of year | \$ 32,870,241 | \$ — | \$ 25,597,923 | \$ 58,468,164 |
| Net asset reclassification based on change in law | (6,086,171) | 6,086,171 | — | — |
| Endowment net assets after reclassification | 26,784,070 | 6,086,171 | 25,597,923 | 58,468,164 |
| Investment return: | | | | |
| Investment income | 648,255 | 766,246 | — | 1,414,501 |
| Net appreciation | (5,809,877) | (6,867,345) | — | (12,677,222) |
| Total investment return | (5,161,622) | (6,101,099) | — | (11,262,721) |
| Adjustment from (to) Unrestricted net assets | (14,928) | 14,928 | — | — |
| Endowment net assets, end of year | \$ 21,607,520 | \$ — | \$ 25,597,923 | \$ 47,205,443 |

United Service Organizations, Inc.

Notes to Financial Statements—Continued

December 31, 2009 and 2008

NOTE L—SUBSEQUENT EVENTS

In May 2009, the FASB issued new guidance to incorporate the accounting and disclosure requirements for subsequent events into U.S. GAAP. The guidance introduces new terminology, defines a date through which management must evaluate subsequent events, and lists the circumstances under which an entity must recognize and disclose events or transactions occurring after the balance-sheet date. The USO adopted this guidance as of December 31, 2009.

The USO evaluated its December 31, 2009 financial statements for subsequent events through March 5, 2010, the date the financial statements were available to be issued. The following subsequent event requires disclosure in the financial statements.

The USO Foundation (Foundation) was incorporated as a supporting organization on March 22, 2007 to carry out and support the general charitable purposes of the USO. On January 20, 2010 and February 2, 2010, the funds constituting the corpus of the “Spirit of Hope Endowment,” which amounted to \$47.2 million in aggregate, was transferred to the Foundation.

The USO is not aware of any additional subsequent events which would require disclosure in the financial statements.

Supplemental Information



United Service Organizations, Inc.

Schedule of Functional Expenses

December 31,

2009

| | Program Services | | | | | Fund-raising | Management and General | Total Operating Expenses |
|---|------------------|---------------|--|----------------|---------------|---------------|------------------------|--------------------------|
| | USO Operations | Entertainment | Communications and Public Awareness Outreach | Total | | | | |
| Salaries | \$ 13,937,775 | \$ 761,205 | \$ 1,048,186 | \$ 15,747,166 | \$ 1,775,119 | \$ 3,044,786 | \$ 20,567,071 | |
| Payroll taxes | 1,077,828 | 58,998 | 74,674 | 1,211,500 | 126,012 | 196,060 | 1,533,572 | |
| Employee benefits | 1,678,726 | 107,447 | 159,822 | 1,945,995 | 274,324 | 552,419 | 2,772,738 | |
| Total salaries and related expenses | 16,694,329 | 927,650 | 1,282,682 | 18,904,661 | 2,175,455 | 3,793,265 | 24,873,381 | |
| Supplies and services | 36,960,299 | 49,060,431 | 25,906 | 86,046,636 | 329,130 | 257,649 | 86,633,415 | |
| Printing and production | 65,127 | 2,072,004 | 5,933,200 | 8,070,331 | 7,576,405 | 2,868,886 | 18,515,622 | |
| Marketing and promotion | — | 221,308 | 82,543,405 | 82,764,713 | 637,254 | — | 83,401,967 | |
| Awards and grants | 615,957 | — | — | 615,957 | — | — | 615,957 | |
| Professional fees | 696,900 | 552,203 | 2,570,687 | 3,819,790 | 2,691,962 | 1,757,568 | 8,269,320 | |
| Subscriptions, dues, and staff training | 170,736 | 1,586 | 22,459 | 194,781 | 105,857 | 26,329 | 326,967 | |
| Travel | 2,116,563 | 2,943,704 | 397,927 | 5,458,194 | 407,843 | 270,571 | 6,136,608 | |
| General insurance | 280,535 | 22,982 | 30,667 | 334,184 | 44,466 | 104,301 | 482,951 | |
| Occupancy | 222,676 | 81,749 | 110,393 | 414,818 | 173,521 | 326,370 | 914,709 | |
| Rental and maintenance of equipment | 335,291 | — | — | 335,291 | — | 137,003 | 472,294 | |
| Communication | 2,967,209 | 40,383 | 218,171 | 3,225,763 | 43,032 | 218,084 | 3,486,879 | |
| Postage and shipping | 557,921 | 15,393 | 2,705,833 | 3,279,147 | 1,986,824 | 1,404,151 | 6,670,122 | |
| Conferences and meetings | 16,445 | 7,752 | 7,784 | 31,981 | 41,133 | 107,918 | 181,032 | |
| Depreciation and amortization | 1,349,089 | 40,257 | 40,257 | 1,429,603 | 40,257 | 40,257 | 1,510,117 | |
| Donation | 27,750 | — | — | 27,750 | — | — | 27,750 | |
| Other expenses | 277,514 | 70,301 | — | 347,815 | 527,533 | 200,294 | 1,075,642 | |
| Total | \$ 63,354,341 | \$ 56,057,703 | \$ 95,889,371 | \$ 215,301,415 | \$ 16,780,672 | \$ 11,512,646 | \$ 243,594,733 | |

Note: In-kind expenses included in supplies and services and marketing and promotion

| | | | | | | | |
|---------------|---------------|---------------|----------------|------|------|------|----------------|
| \$ 16,874,129 | \$ 48,836,506 | \$ 80,732,724 | \$ 146,443,359 | \$ — | \$ — | \$ — | \$ 146,443,359 |
|---------------|---------------|---------------|----------------|------|------|------|----------------|

The accompanying notes are an integral part of this statement.

United Service Organizations, Inc.

Schedule of Functional Expenses

December 31,

2008

| | Program Services | | | | | | Total | Fund-raising | Management and General | Total Operating Expenses |
|---|------------------|---------------|-------------------------------------|----------------|---------------|--------------|----------------|--------------|------------------------|--------------------------|
| | USO Operations | Entertainment | Communications and Public Awareness | | Outreach | | | | | |
| Salaries | \$ 9,477,843 | \$ 551,088 | | 718,684 | \$ | 10,747,615 | \$ | 1,151,025 | \$ | 14,164,198 |
| Payroll taxes | 775,045 | 43,323 | | 50,722 | | 869,090 | | 87,368 | | 1,122,734 |
| Employee benefits | 1,073,328 | 85,762 | | 111,340 | | 1,270,430 | | 181,391 | | 1,836,679 |
| Total salaries and related expenses | 11,326,216 | 680,173 | | 880,746 | | 12,887,135 | | 1,419,784 | | 17,123,611 |
| Supplies and services | 36,723,409 | 44,984,767 | | 44,230 | | 81,752,406 | | 398,488 | | 82,317,404 |
| Printing and production | 366,217 | 1,157,155 | | 4,335,893 | | 5,859,265 | | 5,982,827 | | 13,856,719 |
| Marketing and promotion | 62,279 | 169,661 | | 70,806,687 | | 71,038,627 | | 875,141 | | 71,913,768 |
| Awards and grants | 326,387 | — | | — | | 326,387 | | — | | 326,387 |
| Professional fees | 536,395 | 559,483 | | 1,947,759 | | 3,043,637 | | 2,827,600 | | 7,250,927 |
| Subscriptions, dues, and staff training | 62,223 | 1,358 | | 23,062 | | 86,643 | | 46,705 | | 171,872 |
| Travel | 1,707,915 | 3,549,860 | | 202,436 | | 5,460,211 | | 238,018 | | 5,900,697 |
| General insurance | 360,395 | 38,445 | | 33,502 | | 432,342 | | 50,254 | | 550,560 |
| Occupancy | 224,107 | 93,788 | | 92,965 | | 410,860 | | 185,964 | | 865,586 |
| Rental and maintenance of equipment | 262,581 | — | | — | | 262,581 | | — | | 349,883 |
| Communication | 317,135 | 30,709 | | 154,992 | | 502,836 | | 28,574 | | 612,082 |
| Postage and shipping | 237,606 | 20,551 | | 2,133,822 | | 2,391,979 | | 2,278,001 | | 5,834,440 |
| Conferences and meetings | 135,293 | 2,768 | | 11,784 | | 149,845 | | 40,446 | | 377,779 |
| Depreciation and amortization | 883,661 | 25,210 | | 25,210 | | 934,081 | | 25,210 | | 984,501 |
| Donation | 1,095,640 | — | | — | | 1,095,640 | | — | | 1,095,640 |
| Other expenses | 229,296 | 59,774 | | — | | 289,070 | | 343,629 | | 1,109,440 |
| Total | \$ 54,856,755 | \$ 51,373,702 | \$ 80,693,088 | \$ 186,923,545 | \$ 14,740,641 | \$ 8,977,110 | \$ 210,641,296 | | | |

Note: In-kind expenses included in supplies and services and marketing and promotion

| | | | | | | |
|---------------|---------------|---------------|----------------|------|------|----------------|
| \$ 19,900,011 | \$ 44,702,003 | \$ 70,026,939 | \$ 134,628,953 | \$ — | \$ — | \$ 134,628,953 |
|---------------|---------------|---------------|----------------|------|------|----------------|

The accompanying notes are an integral part of this statement.