



Consolidated Financial Statements and Report of
Independent Certified Public Accountants

United Service Organizations, Inc.

December 31, 2016

(with summarized comparative information for December 31, 2015)

United Service Organizations, Inc.

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Board of Governors
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Report On the Financial Statements

We have audited the accompanying consolidated financial statements of United Service Organizations, Inc. (USO), which comprise the consolidated statement of financial position as of December 31, 2016, and the related consolidated statements of activities and changes in net assets and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management’s Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor’s Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor’s judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the USO’s preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the USO’s internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of United Service Organizations, Inc. as of December 31, 2016, and the changes in their net assets and their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidated schedule of functional expenses for the year ended December 31, 2016 is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures. These additional procedures included comparing and reconciling the information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplementary information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Report On 2015 Summarized Comparative Information

We have previously audited the USO's 2015 consolidated financial statements (not presented herein), and we expressed an unmodified audit opinion on those audited consolidated financial statements in our report dated April 11, 2016. In our opinion, the accompanying summarized comparative information as of and for the year ended December 31, 2015 is consistent, in all material respects, with the audited financial statements from which it has been derived.

Other Reporting Required By Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report, dated April 5, 2017 on our consideration of 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering USO's internal control over financial reporting and compliance.



Baltimore, Maryland
April 5, 2017

United Service Organizations, Inc.

Consolidated Statements of Financial Position

<i>December 31,</i>	2016	2015
Assets		
Cash and cash equivalents	\$ 28,292,556	\$ 29,573,566
Contributions receivable, net	15,164,633	7,323,076
Grants receivable	7,120,795	5,124,101
Other receivables, net	500,568	627,664
Prepaid expenses and other assets	2,084,216	2,249,556
Inventory	3,178,561	3,762,059
Investments	112,496,402	100,885,931
Fixed assets, net	5,668,650	4,914,736
Total Assets	\$ 174,506,381	\$ 154,460,689
Liabilities and Net Assets		
Liabilities		
Accounts payable and accrued expenses	\$ 12,918,568	\$ 10,451,942
Deferred rent	67,553	151,624
Total Liabilities	12,986,121	10,603,566
Net Assets		
Unrestricted	98,329,022	89,777,385
Temporarily restricted	36,943,315	28,481,815
Permanently restricted	26,247,923	25,597,923
Total Net Assets	161,520,260	143,857,123
Total Liabilities and Net Assets	\$ 174,506,381	\$ 154,460,689

The accompanying notes are an integral part of these consolidated financial statements.

United Service Organizations, Inc.

Consolidated Statement of Activities and Changes in Net Assets

Year ended December 31, 2016 (with summarized comparative information for December 31, 2015)

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total 2016	Total 2015
Revenue and Support					
Contributions:					
Corporate, foundation and individual giving	\$ 18,431,185	\$ 16,918,226	\$ 650,000	\$ 35,999,411	\$ 22,695,245
Direct response	70,300,967	43,068	—	70,344,035	70,426,637
United way and CFC	1,200,924	—	—	1,200,924	1,186,836
Contributed materials, facilities and services	75,445,025	978,488	—	76,423,513	85,132,227
Grants	21,996,694	—	—	21,996,694	20,370,582
USO center revenue	5,238,723	—	—	5,238,723	4,735,723
Investment income (loss)	2,884,166	3,459,265	—	6,343,431	(1,741,239)
Other income	274,363	—	—	274,363	134,705
Total Revenue and Support	195,772,047	21,399,047	650,000	217,821,094	202,940,716
Net Assets Released from Restrictions	12,937,547	(12,937,547)	—	—	—
Total Revenue and Other Support	208,709,594	8,461,500	650,000	217,821,094	202,940,716
Operating Expenses					
Program services:					
USO centers	44,483,567	—	—	44,483,567	36,708,379
Programs	13,846,645	—	—	13,846,645	12,517,791
Contributed materials, facilities and services	76,809,031	—	—	76,809,031	84,678,705
Entertainment	6,129,596	—	—	6,129,596	8,345,598
Communications and public awareness outreach	20,324,927	—	—	20,324,927	17,483,138
Total program expenses	161,593,766	—	—	161,593,766	159,733,611
Supporting Services					
Fundraising	23,725,134	—	—	23,725,134	23,070,908
Management and general	14,383,057	—	—	14,383,057	15,472,933
Contributed materials, facilities and services	456,000	—	—	456,000	215,743
Total Supporting Services	38,564,191	—	—	38,564,191	38,759,584
Total Operating Expenses	200,157,957	—	—	200,157,957	198,493,195
Changes in Net Assets	8,551,637	8,461,500	650,000	17,663,137	4,447,521
Net Assets, beginning of year	89,777,385	28,481,815	25,597,923	143,857,123	139,409,602
Net Assets, end of year	\$ 98,329,022	\$ 36,943,315	\$ 26,247,923	\$ 161,520,260	\$ 143,857,123

The accompanying notes are an integral part of this consolidated financial statement.

United Service Organizations, Inc.

Consolidated Statements of Cash Flows

<i>Years ended December 31,</i>	2016	2015
Cash Flows from Operating Activities		
Change in net assets	\$ 17,663,137	\$ 4,447,521
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	2,119,558	2,187,262
Contributed investments	(148,819)	(758,251)
Change in discount and allowance on contributions and other receivable, net	284,517	(24,756)
Change in allowance for inventory obsolescence	—	(24,800)
Realized/unrealized (gain) loss on investments	(4,585,337)	3,281,272
Contributions restricted for permanent endowment	(250,000)	—
Revenue from contributed inventory, construction materials, equipment	(1,061,027)	(1,215,974)
Contributed inventory used	879,544	1,304,086
Gain on disposal of fixed assets	(35,187)	(8,400)
Changes in assets and liabilities		
Contributions receivable	(8,202,617)	4,394,482
Grants and other receivables	(1,848,566)	566,600
Prepaid expenses and other assets	165,340	(686,903)
Inventory	782,117	207,177
Accounts payable and accrued expenses	2,466,198	(888,390)
Deferred rent	(84,071)	(109,159)
Net Cash Provided by Operating Activities	8,144,787	12,671,767
Cash Flows from Financing Activities		
Contributions restricted for permanent endowment	250,000	—
Net Cash Provided by Financing Activities	250,000	—
Cash Flows from Investing Activities		
Purchase of fixed assets	(2,837,849)	(1,631,612)
Proceeds from the sale of fixed assets	37,939	15,801
Purchase of investments	(132,248,688)	(148,489,638)
Sales of investments	125,372,801	127,232,104
Net Cash Used in Investing Activities	(9,675,797)	(22,873,345)
Net Decrease in Cash and Cash Equivalents	(1,281,010)	(10,201,578)
Cash and Cash Equivalents, beginning of year	29,573,566	39,775,144
Cash and Cash Equivalents, end of year	\$ 28,292,556	\$ 29,573,566

The accompanying notes are an integral part of these consolidated financial statements.

United Service Organizations, Inc.

Notes to Consolidated Financial Statements

December 31, 2016 (with summarized comparative information for December 31, 2015)

NOTE A—ORGANIZATION

United Service Organizations, Inc. (USO) is a not-for-profit, congressionally chartered, private organization devoted exclusively to strengthening America's military service members by keeping them connected to family, home and country, throughout their service to the nation. The USO is not part of the United States Government, but is recognized by the Department of Defense, Congress and President of the United States, who serves as Honorary Chairman of USO. The USO relies on the generosity of individuals, organizations and corporations to support its activities. For over 75 years, the USO has been the nation's leading organization to serve the men and women in the U.S. military, and their families, throughout their time in uniform. From the moment they join, through their assignments and deployments, and as they transition back to their communities, the USO is always by their side.

Today's USO continuously adapts to the needs of our men and women in uniform and their families, so they can focus on their very important mission. We operate USO centers at or near military installations across the United States and throughout the world, including in combat zones, and even un-staffed USO service sites in places too dangerous for anyone but combat troops to occupy.

USO airport centers throughout the country offer around-the clock hospitality for traveling service members and their families. Our trademark USO tours bring America and its celebrities to service members who are assigned far from home, to entertain them and convey the support of the nation. Our many specialized programs offer a continuum support to service members throughout their journey of service, from the first time they don the uniform until they last time they take it off.

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying consolidated financial statements reflect the accounts of United Service Organizations, Inc. and the USO Foundation. All intercompany accounts and transactions have been eliminated.

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

Use of Estimates

The presentation of consolidated 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 consolidated 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 Consolidated Financial Statements—Continued

December 31, 2016 (with summarized comparative information for December 31, 2015)

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

Net Assets

Net assets are classified and reported as follow:

Unrestricted: Net assets that are not subject to donor-imposed stipulations. Included in unrestricted net assets are amounts that have been designed by the Board of Governors for a specific purpose.

Temporarily Restricted: Temporarily restricted net assets represent those resources that are subject to donor-imposed stipulations that will be met either by the actions of the USO and/or by the passage of time.

Permanently Restricted: Permanently restricted net assets represent those resources that are subject to donor-imposed stipulations that they be maintained permanently by the USO. Revenues and gains on permanently restricted net assets are reported as increases in unrestricted or temporarily restricted net assets dependent on the donor-imposed stipulations.

Foreign Currency

The USO operates centers at 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

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

Investments

Investment income is presented net of investment advisory/management fees in the accompanying consolidated statement of activities.

Inventory

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

Contributed product inventory is recorded at the fair value on the date received. Management periodically reviews inventory levels for slow-moving or obsolete inventory and adjusts the fair value, if necessary.

United Service Organizations, Inc.

Notes to Consolidated Financial Statements—Continued

December 31, 2016 (with summarized comparative information for December 31, 2015)

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

Investments and Fair Value Measurements

The USO values its financial assets and liabilities based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. A fair value hierarchy that prioritizes the inputs to valuation techniques is used to measure fair value. The hierarchy maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. The hierarchy is broken down into the follow three levels, based on the reliability of inputs:

Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities that are observable at the measurement date;

Level 2 – Significant observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data; and

Level 3 – Significant unobservable inputs for the asset or liability that reflect the reporting entity's own estimates about the assumptions that market participants would use in pricing the asset or liability.

The following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at December 31, 2016 and 2015.

Money market funds: The carrying value of money market funds held as investments approximate the fair value due to the short maturity of these instruments.

Corporate bonds and government obligations: When quoted prices are available in an active market, they are classified within Level 1 of the fair value hierarchy. Quoted prices in inactive markets are classified within Level 2. If quoted market prices are not available or accessible, then fair values are estimated using pricing models, matrix pricing, or discounted cash flow models. The most significant inputs to the discounted cash flow model are the coupon, yield and expected maturity date. The fair values of corporate bonds, international bonds or government obligations that are estimated using pricing models or matrix pricing based on observable prices of the investments that trade in inactive markets are generally classified within Level 2 of the fair value hierarchy. Securities are classified within Level 3 when there is limited activity or less transparency concerning inputs to the valuation.

Equity securities and mutual funds: Valued at the closing share price reported on the active market on which the individual securities are traded.

Alternative investments: Alternative investments consist of investments in funds of funds based on their underlying investments. The funds in this class of investments invest primarily in managed futures, foreign exchange and private investment companies to achieve diversification to provide for increased return and/or reduced volatility. The fair values of such investments are determined using the net asset value (NAV) per share as a practical expedient. Investments, classified within Level 2 of the fair value hierarchy are redeemable monthly.

United Service Organizations, Inc.

Notes to Consolidated Financial Statements—Continued

December 31, 2016 (with summarized comparative information for December 31, 2015)

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

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.

Contributed Materials and Facilities

Donated facilities, equipment use, materials and supplies received from the United States Government and other donors are reflected in the accompanying consolidated 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

The 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.

The 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. The USO also receives contributions of media air time to promote its Public Service Announcements. These contributions of services are reflected in the accompanying consolidated 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 consolidated financial statements.

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

Contributions

Contributions, including unconditional promises to give, are recognized as revenues in the period received or pledged. Conditional promises to give are not recognized until the conditions on which they depend are substantially met. 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 consolidated 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.

United Service Organizations, Inc.

Notes to Consolidated Financial Statements—Continued

December 31, 2016 (with summarized comparative information for December 31, 2015)

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

Contributions—Continued

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 credit-adjusted interest rates determined at the time the promise to give is made by a donor. Amortization of the discounts is included in contribution revenue in the accompanying consolidated statement of activities. Allowances are recorded for estimated uncollectible contributions based upon management's judgment and analysis of the creditworthiness of the donors, past collection experience, and other relevant factors.

Unconditional promises to give product inventory that are expected to be received within three months or less are recorded at their net realizable value which is the estimated fair value based on a minimal timeframe between promise to give and receipt of goods. Inventory receivables are recorded at wholesale value. Wholesale value of the items donated is determined based on management's best estimate using information provided by donors and other third parties. The USO does not accept or record inventory receivables that are expected to be collected in greater than one year. Management considers all promises to give of product inventory to be fully collectible, therefore no allowance is recorded. Contributions receivable included \$129,208 and \$170,119 of unconditional promises to give product inventory as of December 31, 2016 and 2015, respectively.

Grant Revenue

Grant revenue on cost-reimbursement grants or contracts is recognized when 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 consolidated statement of financial position. Such grant programs are subject to independent audit under the Office of Management and Budget Uniform Guidance 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 consolidated 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 around the world. Revenue is recorded when earned. Amounts received in advance for tours and other activities are recorded as deferred revenue and included in accounts payable and accrued expenses in the accompanying consolidated statements of financial position.

United Service Organizations, Inc.

Notes to Consolidated Financial Statements—Continued

December 31, 2016 (with summarized comparative information for December 31, 2015)

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

Other Receivables

The carrying value of the USO's other receivables represents their estimated net realizable value. As of December 31, 2016 and 2015, the USO has recorded an allowance for doubtful accounts against other receivables of \$150,000 and \$171,032, respectively. The USO estimates an allowance for doubtful accounts based on historical collection rates. In addition, the USO records specific allowances based on facts that become known after revenue is earned.

Concentration of Credit Risk

Financial instruments that potentially subject the USO to a concentration of credit risk include cash deposits with commercial banks. The 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 limits at times throughout the year due to anticipated large expenses under various projects. As of December 31, 2016, balances held in accounts in excess of the FDIC insurable limit were \$26,231,993. Management does not consider this to be a significant credit risk. Amounts in foreign bank accounts total \$721,185 and \$739,269 at December 31, 2016 and 2015, respectively.

Functional Allocation of Expenses

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

Income Taxes

The USO and Foundation are exempt from federal income tax under Section 501(a) of the Internal Revenue Code (IRC) of 1986, as amended, as organizations described in IRC Section 501(c)(3). However, income generated from activities unrelated to the exempt purposes of the organizations are subject to tax under IRC Section 511. USO and Foundation have processes presently in place to ensure the maintenance of tax-exempt status; to identify and report unrelated income; to determine filing and tax obligations in jurisdictions for which the organization has nexus; and to identify and evaluate other matters that may be considered income tax positions. Neither the USO nor Foundation had any material unrelated business income tax liability for the years ended December 31, 2016 and 2015. Therefore, no income tax liability has been provided in the accompanying consolidated financial statements.

United Service Organizations, Inc.

Notes to Consolidated Financial Statements—Continued

December 31, 2016 (with summarized comparative information for December 31, 2015)

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

Income Taxes—Continued

US GAAP requires that an income tax position be recognized or derecognized based on a “more likely than not” threshold. USO and Foundation follow guidance that clarifies the accounting for uncertainty in tax positions taken or expected to be taken in a tax return, including issues relating to financial statement recognition and measurement. This guidance provides that the tax effects from an uncertain tax position can only be recognized in the financial statements if the position is “more-likely-than-not” to be sustained if the position were to be challenged by a taxing authority. The assessment of the tax position is based solely on the technical merits of the position, without regard to the likelihood that the tax position may be challenged. The tax years ending December 31, 2016, 2015, 2014 and 2013 are still open to audit for both federal and state purposes. USO and Foundation have determined that there are no material uncertain tax positions that require recognition or disclosure in the financial statements.

Prior Year Summarized Information

The consolidated financial statements include certain prior year summarized comparative information in total but not by asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the USO's consolidated financial statements for the year ended December 31, 2015, from which the summarized information was derived.

USO Foundation

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. The Foundation's accounts are included in the consolidated financial statements.

New Accounting Pronouncements

In February 2016, the FASB issued Accounting Standards Update (“ASU”) 2016-02 “Leases (Topic 842),” which supersedes the guidance in former ASC Topic 840 “Leases.” The most significant change will result in the recognition of lease assets for the right to use the underlying asset, and lease liabilities for the obligation to make lease payments by lessees, for those leases classified as operating leases under current guidance. The new guidance will also require significant additional disclosures about the amount, timing and uncertainty of cash flows from leases. This standard is effective for the fiscal year ending December 31, 2020, with early adoption permitted. Upon adoption of ASU 2016-02, entities are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. The USO believes adoption of this standard will have a significant impact on the statements of financial position and is evaluating the impact this ASU will have on the statements of activities and cash flows.

United Service Organizations, Inc.

Notes to Consolidated Financial Statements—Continued

December 31, 2016 (with summarized comparative information for December 31, 2015)

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

New Accounting Pronouncements—Continued

In August 2016, the FASB issued ASU 2016-14 to Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities. The ASU amends several requirements for financial statements and notes, including net asset classifications in the statements of financial position and statements of activities and enhanced disclosures in numerous areas. This standard is effective for the fiscal year ending December 31, 2018, with early adoption permitted. The USO is evaluating the impact this ASU will have on the financial statement presentation.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments, which clarifies how companies present and classify certain cash receipts and cash payments in the statement of cash flows. This standard is effective for the fiscal year ending December 31, 2018, with early adoption permitted. The USO is evaluating the impact this ASU will have on the financial statements.

NOTE C—CONTRIBUTIONS RECEIVABLE, NET

Contributions receivable, net consist of the following unconditional promises to give as of December 31:

	2016	2015
Less than one year	\$ 10,649,942	\$ 7,156,402
One to five years	5,003,966	340,185
More than five years	61,288	71,503
	15,715,196	7,568,090
Discount	(265,288)	(63,464)
Allowance for doubtful accounts	(285,275)	(181,550)
	\$ 15,164,633	\$ 7,323,076

Amounts presented above have been discounted to present value using various discount rates ranging between 1% to 4%.

United Service Organizations, Inc.

Notes to Consolidated Financial Statements—Continued

December 31, 2016 (with summarized comparative information for December 31, 2015)

NOTE D—INVESTMENTS

At December 31, investments consists of the following:

	2016	2015
Corporate and commercial obligations	\$ 12,113,173	\$ 12,316,846
U.S. Treasury securities and other government obligations	37,998,037	30,537,259
Corporate equity securities	35,039,833	31,981,931
Mutual funds	20,509,545	18,703,056
Money market holdings	5,501,254	6,073,658
Alternative investments	1,334,560	1,273,181
	<u>\$ 112,496,402</u>	<u>\$ 100,885,931</u>

The following schedule summarizes investment return for the year ending December 31:

	2016	2015
Interest and dividends	\$ 2,311,091	\$ 1,946,661
Net unrealized gains (losses)	3,421,460	(4,305,966)
Net realized gains	1,163,877	1,024,694
Less: investment expenses	(552,997)	(406,628)
	<u>\$ 6,343,431</u>	<u>\$ (1,741,239)</u>

United Service Organizations, Inc.

Notes to Consolidated Financial Statements—Continued

December 31, 2016 (with summarized comparative information for December 31, 2015)

NOTE D—INVESTMENTS—Continued

Investments were recorded at fair value as of December 31, 2016 based on the following level of hierarchy:

	Total	Level 1	Level 2	Level 3
Corporate and commercial obligations	\$ 12,113,173	\$ 12,113,173	\$ —	\$ —
U.S. Treasury securities and other government obligations	37,998,037	37,998,037	—	—
Corporate equity securities	35,039,833	35,039,833	—	—
Mutual funds	20,509,545	20,509,545	—	—
Money market holdings	5,501,254	5,501,254	—	—
Alternative investments	1,334,560	—	1,334,560	—
	<u>\$ 112,496,402</u>	<u>\$ 111,161,842</u>	<u>\$ 1,334,560</u>	<u>\$ —</u>

Investments were recorded at fair value as of December 31, 2015 based on the following level of hierarchy:

	Total	Level 1	Level 2	Level 3
Corporate and commercial obligations	\$ 12,316,846	\$ 12,316,846	\$ —	\$ —
U.S. Treasury securities and other government obligations	30,537,259	30,537,259	—	—
Corporate equity securities	31,981,931	31,981,931	—	—
Mutual funds	18,703,056	18,703,056	—	—
Money market holdings	6,073,658	6,073,658	—	—
Alternative investments	1,273,181	—	1,273,181	—
	<u>\$ 100,885,931</u>	<u>\$ 99,612,750</u>	<u>\$ 1,273,181</u>	<u>\$ —</u>

United Service Organizations, Inc.

Notes to Consolidated Financial Statements—Continued

December 31, 2016 (with summarized comparative information for December 31, 2015)

NOTE E—COMMITMENTS AND CONTINGENCIES

Operating Leases

The USO leases office space and equipment under various long-term lease agreements expiring 2017 through 2027. Lease incentives are amortized and recognized as expense over the term of the lease on a straight-line basis. Unamortized amounts are recorded as deferred rent in the accompanying consolidated statements of financial position.

Future minimum payments under operating leases with terms of one year or more, including the lease assumed subsequent to December 31, 2016, are as follows:

2017	\$	1,440,527
2018		1,528,580
2019		1,519,161
2020		1,549,017
2021		1,587,502
2022 and thereafter		8,703,021
		<hr/>
	\$	16,327,808

For the years ended December 31, 2016 and 2015, total rental expense under all operating leases was \$1,411,628 and \$1,246,235, respectively (excluding related in-kind support).

Other

The 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 outstanding legal proceedings will not have a material effect on the USO's financial position, change in net assets, or cash flows.

United Service Organizations, Inc.

Notes to Consolidated Financial Statements—Continued

December 31, 2016 (with summarized comparative information for December 31, 2015)

NOTE F—FIXED ASSETS

At December 31, fixed assets consist of the following:

	2016	2015
Furniture, fixtures, and equipment	\$ 13,011,755	\$ 12,864,841
Leasehold improvements	11,163,739	9,882,297
	24,175,494	22,747,138
Less: accumulated depreciation and amortization	(18,506,844)	(17,832,402)
	\$ 5,668,650	\$ 4,914,736

For the years ending December 31, 2016 and 2015, depreciation expense totaled \$2,119,558 and \$2,187,262, respectively.

NOTE G—NET ASSETS

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, 2016 and 2015 as follows:

	2016	2015
Education fund	\$ 13,273	\$ 17,773
Military families and expeditionary programs	6,193,470	3,391,799
USO centers	1,706,009	2,006,703
Transition programs	2,213,140	2,386,872
Other programs	867,821	432,719
Passage of time	1,943,834	1,168,857
	\$ 12,937,547	\$ 9,404,723

United Service Organizations, Inc.

Notes to Consolidated Financial Statements—Continued

December 31, 2016 (with summarized comparative information for December 31, 2015)

NOTE G—NET ASSETS—Continued

At December 31, 2016 and 2015, net assets consisted of the following:

	2016	2015
Unrestricted		
Operating	\$ 58,989,534	\$ 53,321,983
Board designated	39,339,488	36,455,402
Total unrestricted	98,329,022	89,777,385
Temporarily restricted		
Education fund	644,100	617,793
Military families and expeditionary programs	6,067,448	5,965,951
USO centers	2,179,072	579,065
Transition programs	460,000	750,000
Other programs	786,752	700,000
Time restricted	5,858,774	2,341,522
Unappropriated endowment earnings	20,947,169	17,527,484
Total temporarily restricted	36,943,315	28,481,815
Permanently restricted		
Spirit of Hope endowment	25,572,923	25,572,923
Other endowments	275,000	25,000
Other	400,000	—
Total permanently restricted	26,247,923	25,597,923
Total net assets	\$ 161,520,260	\$ 143,857,123

United Service Organizations, Inc.

Notes to Consolidated Financial Statements—Continued

December 31, 2016 (with summarized comparative information for December 31, 2015)

NOTE H—ALLOCATION OF JOINT COSTS

The USO conducts activities that include appeals for contributions. These activities primarily include direct-response campaigns. The costs of conducting those joint activities were allocated as follows in 2016 and 2015:

	2016	2015
Programs	\$ 11,260,470	\$ 10,509,974
Management and general	6,653,452	7,038,532
Fundraising	13,744,950	14,851,231
	<u>\$ 31,658,872</u>	<u>\$ 32,399,737</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:

	2016	2015
Celebrity entertainment	\$ 35,267,483	\$ 37,118,498
Center facilities	8,896,917	8,111,243
Public Service Announcements	21,969,998	29,574,636
Materials and other	10,289,115	10,327,850
	<u>\$ 76,423,513</u>	<u>\$ 85,132,227</u>

United Service Organizations, Inc.

Notes to Consolidated Financial Statements—Continued

December 31, 2016 (with summarized comparative information for December 31, 2015)

NOTE J—RETIREMENT PLAN

The USO maintains a 401(a) with a 401(k) component plan named the United Service Organizations Retirement Savings Plan (RSP). The RSP allows eligible participants to contribute both pre-tax and Roth contributions to the RSP, as well as, allows the USO to contribute both employer matching contributions and safe harbor non-elective contributions. Employer matching contributions vest 100 percent over a period of five years; whereas, safe harbor non-elective contributions vest 100 percent over a period of 2 years. In 2016 and 2015, the USO contributed a safe harbor non-elective contribution on behalf of each eligible employee in an amount equal to 4 percent of the employee's compensation without regard to whether the employee makes any employee contributions, subject to federal limitations. Additionally, in 2016 and 2015, the USO contributed a discretionary employer matching contribution equal to 100% of the employee's salary deferral contributions, up to a maximum of 5 percent of the employee's compensation.

The USO's policy is to fund retirement plan costs as accrued. Retirement plan expense was \$2,184,761 and \$2,131,827 for the years ended December 31, 2016 and 2015, respectively.

NOTE K—ENDOWMENT

The USO's endowment consists of the Spirit of Hope endowment and other individual funds established for a variety of purposes. 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.

The District of Columbia Uniform Prudent Management of Institutional Funds Act (DC-UPMIFA) imposes guidelines on the management and investment of endowment funds. Management of the USO has interpreted DC-UPMIFA 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, the 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 organization in a manner consistent with the standard of prudence prescribed by UPMIFA. As of December 31, 2016, there are no immediate plans for the earnings of the endowment to be spent as the expressed purpose of the Endowment is to ensure the availability of funds for the long-term sustainability of the USO and its programs and services.

United Service Organizations, Inc.

Notes to Consolidated Financial Statements—Continued

December 31, 2016 (with summarized comparative information for December 31, 2015)

NOTE K—ENDOWMENT—Continued

The USO has adopted an investment policy for the endowment fund. This investment policy is based on growing the endowment fund to provide financial stability for the USO in perpetuity with no short term plans for withdraws 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.

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

2016	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ —	\$ 20,947,169	\$ 25,847,923	\$ 46,795,092
Board-designated endowment funds	39,339,488	—	—	39,339,488
Total funds	\$ 39,339,488	\$ 20,947,169	\$ 25,847,923	\$ 86,134,580

2016	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	\$ 36,455,402	\$ 17,527,484	\$ 25,597,923	\$ 79,580,809
Contributions	—	—	250,000	250,000
Investment return:				
Investment income	2,249,062	2,658,419	—	4,907,481
Net appreciation	635,024	761,266	—	1,396,290
Total additions	2,884,086	3,419,685	250,000	6,553,771
Endowment net assets, end of year	\$ 39,339,488	\$ 20,947,169	\$ 25,847,923	\$ 86,134,580

United Service Organizations, Inc.

Notes to Consolidated Financial Statements—Continued

December 31, 2016 (with summarized comparative information for December 31, 2015)

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:

<u>2015</u>	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted endowment funds	\$ —	\$ 17,527,484	\$ 25,597,923	\$ 43,125,407
Board-designated endowment funds	36,455,402	—	—	36,455,402
Total funds	\$ 36,455,402	\$ 17,527,484	\$ 25,597,923	\$ 79,580,809

<u>2015</u>	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ 37,262,089	\$ 18,469,436	\$ 25,597,923	\$ 81,329,448
Investment return:				
Investment income	547,320	646,939	—	1,194,259
Net depreciation	(1,354,007)	(1,588,891)	—	(2,942,898)
Total investment return	(806,687)	(941,952)	—	(1,748,639)
Endowment net assets, end of year	\$ 36,455,402	\$ 17,527,484	\$ 25,597,923	\$ 79,580,809

NOTE L—SUBSEQUENT EVENTS

The USO executed an assets acquisition agreement to acquire the assets of RP/6, Inc. (RP/6), a nonprofit corporation, and assume agreed upon liabilities of RP/6 effective January 1, 2017. The purpose of this acquisition is to enhance and further expand the transition support services currently provided by the USO to reach more military service members and their families. There was no cash consideration associated with the acquisition agreement.

United Service Organizations, Inc.

Notes to Consolidated Financial Statements—Continued

December 31, 2016 (with summarized comparative information for December 31, 2015)

NOTE L—SUBSEQUENT EVENTS—Continued

The accounting for this acquisition will be included in the consolidated financial statements on the effective date of acquisition as follows:

Fair value of assets acquired	\$ 2,230,988
Liabilities assumed	(23,082)
	<hr/>
Contribution received in acquisition of RP/6	\$ 2,207,906
	<hr/>

The USO executed a loan repayment agreement to satisfy the debt of USO Central Florida, a nonprofit corporation chartered by the USO, effective February 28, 2017. Under this agreement, the USO has agreed to pay the debtor two installments of \$85,349 plus interest at a rate of 0.71% per year. The final payment is due on or before March 1, 2018.

The USO evaluated its December 31, 2016 consolidated financial statements for subsequent events through, April 5, 2017, the date the consolidated financial statements were available to be issued, and concluded that no additional disclosures are required.

Supplemental Information



United Service Organizations, Inc.

Consolidated Schedule of Functional Expenses

December 31,

2016

	Program Services					Fund-raising	Management and General	Total Operating Expenses
	USO Centers	Programs	Entertainment	Communications and Public Awareness Outreach	Total			
Salaries	\$ 20,241,868	\$ 1,192,683	\$ 855,043	\$ 3,325,701	\$ 25,615,295	\$ 3,745,844	\$ 4,231,770	\$ 33,592,909
Payroll taxes	1,572,037	88,869	57,072	239,456	1,957,434	257,252	271,053	2,485,739
Retirement plan	1,243,680	87,538	60,427	237,448	1,629,093	259,526	296,142	2,184,761
Employee benefits	1,879,414	123,320	70,655	302,050	2,375,439	311,303	447,539	3,134,281
Total salaries and related expenses	24,936,999	1,492,410	1,043,197	4,104,655	31,577,261	4,573,925	5,246,504	41,397,690
Program supplies and services	16,707,156	10,708,212	35,506,876	—	62,922,244	—	—	62,922,244
Office expenses	1,586,156	188,962	2,654	41,839	1,819,611	143,129	176,183	2,138,923
Information Technology	1,000,138	2,175,115	33,949	201,298	3,410,500	198,824	121,006	3,730,330
Printing and production	43,063	2,483	1,519,763	4,808,079	6,373,388	10,438,233	3,241,224	20,052,845
Marketing and promotion	—	—	—	23,906,113	23,906,113	612,203	—	24,518,316
Awards and grants	2,014,810	—	—	—	2,014,810	—	—	2,014,810
Professional fees	1,016,268	63,071	971,854	4,109,780	6,160,973	2,392,006	2,399,728	10,952,707
Subscriptions, dues, and staff training	109,537	79,582	4,197	24,118	217,434	145,139	73,101	435,674
Travel	1,434,320	716,249	2,147,664	294,459	4,592,692	668,931	191,236	5,452,859
General insurance	192,012	21,734	9,813	38,218	261,777	46,912	54,370	363,059
Occupancy	9,220,646	191,416	70,805	278,892	9,761,759	338,319	342,169	10,442,247
Rental and maintenance of equipment	559,839	4,191	1,934	9,026	574,990	11,605	15,474	602,069
Postage and shipping	312,494	710,682	4,703	4,376,410	5,404,289	3,109,292	2,552,720	11,066,301
Meetings, conferences and events	304,077	3,995	42	104,031	412,145	681,437	66,076	1,159,658
Depreciation and amortization	1,993,798	12,480	5,760	26,880	2,038,918	34,560	46,080	2,119,558
Other expenses	40,698	25,241	78,920	3	144,862	524,844	118,961	788,667
Functional expenses, gross	\$ 61,472,011	\$ 16,395,823	\$ 41,402,131	\$ 42,323,801	\$ 161,593,766	\$ 23,919,359	\$ 14,644,832	\$ 200,157,957
Note: In-kind expenses included in expenses listed above	\$ 16,988,444	\$ 2,549,178	\$ 35,272,535	\$ 21,998,874	\$ 76,809,031	\$ 194,225	\$ 261,775	\$ 77,265,031
Functional expenses, net	\$ 44,483,567	\$ 13,846,645	\$ 6,129,596	\$ 20,324,927	\$ 84,784,735	\$ 23,725,134	\$ 14,383,057	\$ 122,892,926

The accompanying notes are an integral part of this consolidated financial statement.

United Service Organizations, Inc.

Consolidated Schedule of Functional Expenses

December 31,

2015

	Program Services					Fund-raising	Management and General	Total Operating Expenses
	USO Centers	Programs	Entertainment	Communications and Public Awareness Outreach	Total			
Salaries	\$ 17,044,004	\$ 1,274,793	\$ 1,020,954	\$ 2,836,983	\$ 22,176,734	\$ 3,076,198	\$ 4,565,998	\$ 29,818,930
Payroll taxes	1,270,722	94,147	71,577	211,196	1,647,642	218,092	329,047	2,194,781
Retirement plan	1,117,672	96,492	85,183	230,376	1,529,723	233,105	368,999	2,131,827
Employee benefits	1,562,188	133,461	101,114	295,260	2,092,023	297,700	501,331	2,891,054
Total salaries and related expenses	20,994,586	1,598,893	1,278,828	3,573,815	27,446,122	3,825,095	5,765,375	37,036,592
Program supplies and services	14,704,142	8,226,335	37,362,960	—	60,293,437	—	—	60,293,437
Office expenses	882,783	65,608	2,216	7,885	958,492	142,289	116,090	1,216,871
Information Technology	1,174,691	2,118,074	56,920	269,484	3,619,169	285,806	360,159	4,265,134
Printing and production	18,799	—	2,492,989	4,645,398	7,157,186	10,956,693	3,379,774	21,493,653
Marketing and promotion	—	12,218	—	30,061,270	30,073,488	708,399	—	30,781,887
Awards and grants	1,109,814	—	—	—	1,109,814	—	—	1,109,814
Professional fees	827,146	418,473	712,635	3,343,462	5,301,716	2,207,898	1,989,762	9,499,376
Subscriptions, dues, and staff training	102,032	30,739	9,520	25,709	168,000	125,188	68,885	362,073
Travel	1,271,061	967,091	3,150,178	227,787	5,616,117	403,765	324,352	6,344,234
General insurance	154,937	21,067	11,557	44,749	232,310	42,539	63,768	338,617
Occupancy	8,297,952	195,771	71,054	251,752	8,816,529	257,808	394,680	9,469,017
Rental and maintenance of equipment	425,794	5,096	3,528	11,759	446,177	14,895	16,854	477,926
Postage and shipping	274,152	611,019	3,621	4,596,046	5,484,838	3,413,057	2,783,021	11,680,916
Meetings, conferences and events	365,741	2,375	9,864	6,685	384,665	463,770	59,462	907,897
Depreciation and amortization	2,067,346	23,983	23,983	23,983	2,139,295	23,983	23,984	2,187,262
Other expenses	20,256	123,947	342,053	—	486,256	374,988	167,245	1,028,489
Functional expenses, gross	\$ 52,691,232	\$ 14,420,689	\$ 45,531,906	\$ 47,089,784	\$ 159,733,611	\$ 23,246,173	\$ 15,513,411	\$ 198,493,195
Note: In-kind expenses included in expenses listed above	\$ 15,982,853	\$ 1,902,898	\$ 37,186,308	\$ 29,606,646	\$ 84,678,705	\$ 175,265	\$ 40,478	\$ 84,894,448
Functional expenses, net	\$ 36,708,379	\$ 12,517,791	\$ 8,345,598	\$ 17,483,138	\$ 75,054,906	\$ 23,070,908	\$ 15,472,933	\$ 113,598,747

The accompanying notes are an integral part of this consolidated financial statement.