**USO NORTHWEST**

FINANCIAL REPORT

DECEMBER 31, 2018

# C O N T E N T S

**Page**

**INDEPENDENT AUDITORS' REPORT ..... 1**

**FINANCIAL STATEMENTS**

STATEMENTS OF FINANCIAL POSITION ..... 2
STATEMENTS OF ACTIVITIES ..... 3
STATEMENTS OF FUNCTIONAL EXPENSES ..... 4
STATEMENTS OF CASH FLOWS ..... 5
NOTES TO FINANCIAL STATEMENTS ..... 6 - 11

petersonsullivan LLP
Certified Public Accountants
& Advisors

# INDEPENDENT AUDITORS' REPORT

To the Board of Directors
USO Northwest
Seattle, Washington

We have audited the accompanying financial statements of USO Northwest, which comprise the statements of financial position as of December 31, 2018 and 2017, and the related statements of activities, functional expenses, and cash flows for the years then ended, and the related notes to the financial statements.

**Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of 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 financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the 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 entity'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 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 financial statements referred to above present fairly, in all material respects, the financial position of USO Northwest as of December 31, 2018 and 2017, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States.

Petersm Sullin L.L.P.

June 27, 2019

601 Union Street
Suite 2300
Seattle, WA 98101

(206) 382-7777 MAIN
(206) 382-7700 FAX

pscpa.com

**USO NORTHWEST**

STATEMENTS OF FINANCIAL POSITION

December 31, 2018 and 2017

| ASSETS | 2018 | 2017 |
|---|---|---|
| Current Assets | | |
| Cash and cash equivalents | $ 1,534,116 | $ 1,477,372 |
| Investments | | 59,820 |
| Contributions receivable, net | 27,365 | 121,585 |
| Contribution receivable - related party | | 48,511 |
| Rent receivable, current portion | 1,073,162 | 1,073,162 |
| Other current assets | 10,619 | 4,491 |
| Total current assets | 2,645,262 | 2,784,941 |
| Contributions Receivable, net of current portion | 10,000 | 20,000 |
| Rent Receivable, long-term portion | 3,988,664 | 4,935,466 |
| Property and Equipment | | |
| Furniture and equipment | 216,924 | 200,854 |
| Vehicles | 158,761 | 154,511 |
| Leasehold improvements | 2,351,295 | 1,934,236 |
| Assets not placed in service | | 258,537 |
| Construction in progress | 11,508 | 4,986 |
| | 2,738,488 | 2,553,124 |
| Less: accumulated depreciation | (852,850) | (657,720) |
| | 1,885,638 | 1,895,404 |
| Total assets | $ 8,529,564 | $ 9,635,811 |

| LIABILITIES AND NET ASSETS | | |
|---|---|---|
| Current Liabilities | | |
| Accounts payable | $ 86,533 | $ 33,445 |
| Accrued payroll and related liabilities | 49,760 | 45,151 |
| Total current liabilities | 136,293 | 78,596 |
| Net Assets | | |
| Without donor restrictions | 3,209,652 | 3,250,992 |
| With donor restrictions | 5,183,619 | 6,306,223 |
| Total net assets | 8,393,271 | 9,557,215 |
| Total liabilities and net assets | $ 8,529,564 | $ 9,635,811 |

See Notes to Financial Statements

**USO NORTHWEST**

STATEMENTS OF ACTIVITIES

For the Years Ended December 31, 2018 and 2017

| | 2018 | | | 2017 | | |
|---|---|---|---|---|---|---|
| | Without Donor Restrictions | With Donor Restrictions | Total | Without Donor Restrictions | With Donor Restrictions | Total |
| Support and Revenue | | | | | | |
| Public contributions | $ 887,539 | $ 3,980 | $ 891,519 | $ 1,186,887 | $ 192,349 | $ 1,379,236 |
| Public contributions - in-kind | | | | | | |
| Rent | 264,310 | | 264,310 | 65,487 | 140,150 | 205,637 |
| Materials | 3,014,301 | | 3,014,301 | 3,013,620 | | 3,013,620 |
| United Way contributions | 8,113 | | 8,113 | 5,432 | | 5,432 |
| Individual contributions through United Way | 59,951 | | 59,951 | 42,988 | | 42,988 |
| Special event revenues | 1,066,906 | | 1,066,906 | 911,121 | | 911,121 |
| Special event direct expenses | (436,850) | | (436,850) | (280,031) | | (280,031) |
| Investment income | 2,930 | | 2,930 | 4,882 | | 4,882 |
| Other income | 7,898 | | 7,898 | 2,057 | | 2,057 |
| Loss on disposal of assets | | | | (17,970) | | (17,970) |
| Net assets released from restrictions | 1,126,584 | (1,126,584) | | 922,100 | (922,100) | |
| Total support and revenue | 6,001,682 | (1,122,604) | 4,879,078 | 5,856,573 | (589,601) | 5,266,972 |
| Expenses | | | | | | |
| Program services | 5,544,267 | | 5,544,267 | 4,882,379 | | 4,882,379 |
| Management and general | 229,209 | | 229,209 | 184,742 | | 184,742 |
| Fundraising | 269,546 | | 269,546 | 288,617 | | 288,617 |
| Total expenses | 6,043,022 | | 6,043,022 | 5,355,738 | | 5,355,738 |
| **Change in net assets** | **(41,340)** | **(1,122,604)** | **(1,163,944)** | **500,835** | **(589,601)** | **(88,766)** |
| Net Assets, beginning of year | 3,250,992 | 6,306,223 | 9,557,215 | 2,750,157 | 6,895,824 | 9,645,981 |
| Net Assets, end of year | $ 3,209,652 | $ 5,183,619 | $ 8,393,271 | $ 3,250,992 | $ 6,306,223 | $ 9,557,215 |

See Notes to Financial Statements

**USO NORTHWEST**

STATEMENTS OF FUNCTIONAL EXPENSES

For the Years Ended December 31, 2018 and 2017

| | 2018 | | | | 2017 | | | |
|---|---|---|---|---|---|---|---|---|
| | Program Services | Management and General | Fundraising | Total | Program Services | Management and General | Fundraising | Total |
| Salaries, related taxes, and benefits | $ 576,593 | $ 131,516 | $ 193,372 | $ 901,481 | $ 495,815 | $ 123,189 | $ 186,031 | $ 805,035 |
| In-kind materials | 2,966,733 | 19,450 | 18,118 | 3,004,301 | 2,682,250 | 14,380 | 33,357 | 2,729,987 |
| Rent | 1,337,472 | | | 1,337,472 | 1,103,486 | | | 1,103,486 |
| Event rental and catering | | | 434,537 | 434,537 | | | 287,624 | 287,624 |
| Food expenses | 219,632 | | | 219,632 | 202,956 | | | 202,956 |
| Depreciation | 203,151 | | | 203,151 | 177,395 | | | 177,395 |
| Program expenses | 148,112 | | | 148,112 | 133,768 | | | 133,768 |
| Insurance | 18,040 | 30,380 | 15,635 | 64,055 | 15,846 | 2,526 | 4,593 | 22,965 |
| Telephone and internet | 13,430 | 4,100 | 6,237 | 23,767 | 23,586 | 5,547 | 6,653 | 35,786 |
| Consulting and marketing | 1,374 | | 19,628 | 21,002 | 11,965 | 2,042 | 8,559 | 22,566 |
| Professional fees | | 15,488 | | 15,488 | 10,100 | 13,300 | | 23,400 |
| Other operating expenses | 59,730 | 28,275 | 18,869 | 106,874 | 25,212 | 23,758 | 41,831 | 90,801 |
| Total expenses | 5,544,267 | 229,209 | 706,396 | 6,479,872 | 4,882,379 | 184,742 | 568,648 | 5,635,769 |
| Less: expenses netted with revenue on the statements of activities | | | (436,850) | (436,850) | | | (280,031) | (280,031) |
| Total expenses included in expense section of the statements of activities | $ 5,544,267 | $ 229,209 | $ 269,546 | $ 6,043,022 | $ 4,882,379 | $ 184,742 | $ 288,617 | $ 5,355,738 |

See Notes to Financial Statements

**USO NORTHWEST**

STATEMENTS OF CASH FLOWS

For the Years Ended December 31, 2018 and 2017

| | 2018 | 2017 |
|---|---|---|
| Cash Flows from Operating Activities | | |
| Change in net assets | $ (1,163,944) | $ (88,766) |
| Adjustments to reconcile change in net assets to net cash flows from operating activities | | |
| Depreciation expense | 203,151 | 177,395 |
| Donated property and equipment | (10,000) | (283,637) |
| Donated rent received | | (172,556) |
| Use of donated rent | 946,802 | 923,280 |
| Gain on investments | | (2,625) |
| Loss on disposal of property and equipment | | 17,970 |
| Changes in operating assets and liabilities | | |
| Contributions receivable | 152,731 | (115,676) |
| Prepaid expenses | | 21,528 |
| Other assets | (6,128) | 14,959 |
| Accounts payable | 53,088 | 1,200 |
| Accrued payroll and related liabilities | 4,609 | 796 |
| Net cash flows from operating activities | 180,309 | 493,868 |
| Cash Flows from Investing Activities | | |
| Purchase of property and equipment | (183,385) | (4,982) |
| Proceeds from sale of investments | 59,820 | |
| Net cash flows from investing activities | (123,565) | (4,982) |
| **Net change in cash and cash equivalents** | **56,744** | **488,886** |
| Cash and Cash Equivalents, beginning of year | 1,477,372 | 988,486 |
| Cash and Cash Equivalents, end of year | $ 1,534,116 | $ 1,477,372 |

See Notes to Financial Statements

## NOTES TO FINANCIAL STATEMENTS

### Note 1. Organization and Significant Accounting Policies

**Organization**

USO Northwest ("USO") is a nonprofit organization with the mission to serve the social, welfare, educational, and entertainment needs of the members of the armed forces, and to participate in the USO policies and procedures to the extent authorized by USO, Inc. (the national headquarters).

The programs of USO consist of the operation at four airport centers – one at the Seattle-Tacoma International Airport ("SeaTac"), one at the Portland International Airport ("PDX"), and two at Joint Base Lewis McChord ("Shali" and "Ft. Lewis") – and two mobile units ("the Mobile Canteen Units"). Joint Base Lewis McChord is also referred to as JBLM. The SeaTac facilities are provided to USO at no cost by the Port of Seattle, and the PDX facilities are provided to USO at no cost by the Port of Portland. The McChord facilities are provided at no cost by the Army Corps of Engineers and by a credit union (the CEO of the credit union is a USO board member).

Each airport center provides beverages and snacks, as well as facilities for resting, watching television, reading, and other activities. The equipment at each center is provided by donation and purchase. The SeaTac facilities operate 24 hours a day, 7 days a week based on volunteer staffing availability. The PDX facilities operate 16 hours a day, 7 days a week with the support of volunteer staff, and the JBLM facilities operate 12 hours a day, 6 days a week, also with the support of volunteer staff. The Mobile Canteen units were provided by donation and provide entertainment and food preparation for troops and their families during deployments and homecomings at locations other than the airport centers.

**Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from the estimates that were used.

**Fair Value Measurements**

Fair value is a market-based measurement determined based on assumptions that market participants would use in pricing an asset or liability. There are three levels that prioritize the inputs used in measuring fair value as follows:

- Level 1: Observable market inputs such as quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: Observable market inputs, other than quoted prices in active markets, that are observable either directly or indirectly; and
- Level 3: Unobservable inputs where there is little or no market data, which require the reporting entity to develop its own assumptions.

Investments are recorded at fair value on a recurring basis in these financial statements.

**Financial Statement Presentation**

USO is required to report information regarding its financial position and activities according to two classes of net assets: without donor restrictions and with donor restrictions. The classes of net assets are described as follows:

- Net assets without donor restrictions are those currently available at the discretion of the Board of Directors for use in USO's operations.

- Net assets with donor restrictions are those that are stipulated by donors for specific operating purposes or time periods. If restricted contributions are used for their restricted purpose in the same year they are received, they are classified under net assets without donor restrictions. Net assets with donor restrictions consist of the following as of December 31:

| | 2018 | 2017 |
|---|---|---|
| Rent (time-restricted) | $ 5,061,826 | $ 6,008,628 |
| SeaTac security improvements | 48,670 | 57,685 |
| Fort Lewis site improvements | 40,382 | 116,690 |
| PDX site improvements | | 69,000 |
| Mobile Unit | | 22,431 |
| Restricted for other programs | 32,741 | 31,789 |
| | $ 5,183,619 | $ 6,306,223 |

**Cash and Cash Equivalents**

Money market funds and highly liquid investments with original maturities of three months or less are considered to be cash equivalents. Cash and cash equivalents consist of the following at December 31:

| | 2018 | 2017 |
|---|---|---|
| Cash - checking | $ 1,073,665 | $ 1,079,496 |
| Money market funds | 460,451 | 397,876 |
| | $ 1,534,116 | $ 1,477,372 |

At times, USO has cash in financial institutions in excess of federally insured limits.

**Investments**

Investments are recorded at their fair values in the statements of financial position using Level 1 inputs (quoted prices on national exchanges). At December 31, 2017, investments consisted of stock held in corporations (Starbucks and Weyerhauser). These stocks were sold during 2018, and proceeds were transferred to the money market account. Gains/losses on investment sales are recognized using the specific identification method.

**Contribution Revenue**

USO recognizes revenue from contributions (including in-kind contributions) when the award is made. Contributions are recognized depending on the existence and/or nature of any donor restrictions. Special event revenue is recognized when the event takes place.

**Contributions Receivable**

Contributions receivable consist of pledged donations and are stated at the pledged amount less an allowance for doubtful accounts. Short-term contributions are recognized at net realizable value. Long-term contributions receivable are recognized at fair value (at the time of donation) and are measured at the present value of their expected cash flow. In arriving at fair value, long-term contributions are discounted using an estimated risk-adjusted discount rate and an allowance for doubtful accounts. At December 31, 2018, management has not discounted long-term contributions, as management has determined the discount would be immaterial to these financial statements. Of the total gross contributions receivable at December 31, 2018 and 2017, 68% and 67% was due from two and three donors, respectively.

Management reviews the collectibility of contributions receivable on a periodic basis and determines the amount estimated to be uncollectible. A reserve for doubtful accounts is then established. USO charges off receivables against the allowance when management determines that a receivable is not collectible.

Contributions receivable consist of the following at December 31:

| | 2018 | 2017 |
|---|---|---|
| Amounts due in: | | |
| Less than one year | $ 34,250 | $ 129,095 |
| One to five years | 10,000 | 20,000 |
| Total gross contributions receivable | 44,250 | 149,095 |
| Less: allowance for doubtful accounts | (6,885) | (7,510) |
| Contributions receivable, net | $ 37,365 | $ 141,585 |

**Rent Receivable**

USO has a lease with SeaTac airport that expires in 2024, with yearly payments of $10. Because the lease is at a below-market rate, USO recognized an in-kind donation (in 2014) for the fair value of the rent in excess of the actual rent to be paid. The rent receivable represents the remaining contribution to be received over the remaining term of the lease, discounted at 2.6%. As of December 31, 2018 and 2017, management did not believe an allowance was necessary against this receivable.

USO has a lease with the Army Corps of Engineers at JBLM. The lease has a five-year term expiring in 2021, with no yearly payments. Because the lease is at a below-market rate, during 2016, USO recognized an in-kind donation of $238,321, which is the fair value of the rent in excess of the actual rent to be paid. The rent receivable represents the remaining contribution to be received over the remaining term of the lease, discounted at 1.41%. As of December 31, 2018 and 2017, management did not believe an allowance was necessary against this receivable.

USO has a lease with America's Credit Union (a related party) at JBLM. The lease has a five-year term expiring in 2022, with no yearly payments. Because the lease is at a below-market rate, during 2017, USO recognized an in-kind donation of $172,556, which is the fair value of the rent in excess of the actual rent to be paid. The rent receivable represents the remaining contribution to be received over the remaining term of the lease, discounted at 1.94%. As of December 31, 2018 and 2017, management did not believe an allowance was necessary against this receivable.

The amount of benefit for the three leases are due in the following years ending December 31:

| | Rent Receivable | Discount (Interest Portion) | Total |
|---|---|---|---|
| 2019 | $ 1,073,162 | $ - | $ 1,073,162 |
| 2020 | 1,073,162 | 26,416 | 1,046,746 |
| 2021 | 1,036,712 | 51,168 | 985,544 |
| 2022 | 992,156 | 73,478 | 918,678 |
| 2023 | 989,210 | 96,523 | 892,687 |
| Thereafter | 164,868 | 19,857 | 145,011 |
| | $ 5,329,270 | $ 267,444 | $ 5,061,826 |

Other facilities (PDX) have contributed to USO, but these relationships are on a month-to-month basis and are recognized in the month contributed.

**Property and Equipment**

Property and equipment are recorded at cost or, in the case of donated property, at the estimated fair value at the date of donation. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets. Amortization of leasehold improvements is also calculated using the straight-line method over the shorter of the improvement's useful life or the anticipated lease term (it is anticipated that USO has long-term relationships with its landlords). USO's policy is to capitalize an asset with a cost of at least $3,500 and an estimated useful life of at least two years.

**Functional Allocation of Expenses**

The costs of providing the various programs and other activities have been summarized on a functional basis in the statements of activities and functional expenses. The financial statements report certain categories of expenses that are attributed to more than one program or supporting function. Therefore, expenses require allocation on a reasonable basis that is consistently applied. Salaries, wages, payroll taxes, and employee benefits expenses are allocated among functional expenses on the basis of time and effort. Telephone and internet are allocated based on salary and wages allocations. All other major categories are allocated directly to the department charged.

**Income Taxes**

USO is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code.

**Recent Accounting Pronouncement Adopted**

During the year ended December 31, 2018, USO adopted the provisions of Accounting Standards Update ("ASU") No. 2016-14, Not-for-Profit Entities (Topic 958) – Presentation of Financial Statements of Not-for-Profit Entities. The update addresses the complexity and understandability of net asset classifications, deficiencies in information about liquidity and availability of resources, and the lack of consistency in the type of information provided about expenses and investment return. USO has adjusted the presentation of these statements accordingly.

**Reclassifications**

Certain amounts in the prior-year financial statements have been reclassified to conform to the current-year presentation.

**Subsequent Events**

Management of USO has evaluated subsequent events through the date these financial statements were available to be issued, which was June 27, 2019.

## Note 2. Liquidity and Availability of Resources

The USO strives to maintain liquid financial assets sufficient to cover six months of general expenditures. Financial assets in excess of daily cash requirements are invested in money market funds (included with cash and cash equivalents). The following table shows the total financial assets held by the USO and the amounts of those financial assets that could readily be made available within one year of the statement of financial position date to meet general expenditures as of December 31:

| | 2018 | 2017 |
|---|---|---|
| Financial assets at year-end | | |
| Cash and cash equivalents | $ 1,534,116 | $ 1,477,372 |
| Investments | | 59,820 |
| Current receivables, net of allowance | 27,365 | 121,585 |
| Financial assets available to meet cash needs for general expenditures within one year | $ 1,561,481 | $ 1,658,777 |

## Note 3. Support

**Contributions**

Contributions from individuals and corporations provide a majority of the contributions to support USO's programs. Contributions from one source (different each year) represented 12% and 25% of total revenue for the years ended December 31, 2018 and 2017, respectively.

The United Way agencies of King, Pierce, and other counties provide funding (or coordinate the collection of funding) for USO. USO makes annual budget presentations to the United Way agencies of King and Pierce Counties, and the budgets must be accepted by the United Way before support is provided.

**Bequests**

The USO recognizes revenue from bequests when (1) the bequest becomes an unconditional promise to give and (2) when the amount to be received can be estimated. This is usually when the will has gone through probate. During 2017, bequests of $313,057 were received from one donor and are included with public contributions on the statements of activities. There were no bequests received in 2018.

**In-Kind Contributions**

Food, supplies, entertainment items, materials, advertising, and other assets received as donations are recorded and reflected in the accompanying financial statements at their fair values at the date of receipt. Total in-kind contributions (non-rent) were $3,014,301 in 2018 and $3,013,620 in 2017. The most significant individual in-kind donation (non-rent) in 2018 and 2017 was for Girl Scout cookies valued at $919,820 and $1,000,755, respectively.

USO also receives support in the form of donated facilities at SeaTac, PDX, and JBLM (Ft. Lewis and Shali). For donated facilities associated with long-term leases, revenue is recognized when the lease is executed, but the expense is recognized ratably over the lease term. In total, the facilities expense recognized was valued at $1,337,472 and $1,103,486 in 2018 and 2017, respectively.

In addition, USO has an in-kind rent receivable from SeaTac, Ft. Lewis, and Shali of $5,061,826 and $6,008,628 as of December 31, 2018 and 2017, respectively. This receivable is related to donated facilities.

USO benefits from thousands of hours of volunteer effort at the SeaTac, PDX, and JBLM centers. Generally, these volunteer hours are not reflected in the financial statements because they do not meet the accounting requirements for recognition.

## Note 4. Related Party Transactions

In 2018 and 2017, USO received $104,904 and $180,590, respectively, in cash contributions from USO World Headquarters ("USO-WHQ"). USO is affiliated with USO-WHQ as a chartered member. At December 31, 2017, USO had a receivable of $48,511 related to these contributions, which is shown as contribution receivable – related party on the 2017 statement of financial position. No related party receivable existed at December 31, 2018.

## Note 5. Employee Retirement Plan

USO has a 401(k) retirement plan for the benefit of all eligible employees. USO matches employee contributions up to 4%. USO's contributions to the plan were $18,925 and $11,980 during the years ended December 31, 2018 and 2017, respectively.