

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.

AUDITED FINANCIAL STATEMENTS

December 31, 2010

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Report of Independent Auditors.....	1
Statement of Financial Position.....	2
Statement of Activities	3
Statement of Functional Expenses	4
Statement of Cash Flows.....	5
Notes to Financial Statements	6-11



Board of Directors
Servicemembers Legal Defense Network, Inc.
Washington, DC

Report of Independent Auditors

We have audited the accompanying statement of financial position of Servicemembers Legal Defense Network, Inc. (SLDN) as of December 31, 2010, and the related statements of activities, functional expenses, and cash flows for the year then ended. These financial statements are the responsibility of SLDN'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 SLDN's December 31, 2009 financial statements, and in our report dated February 19, 2010, 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. 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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes 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 Servicemembers Legal Defense Network, Inc. as of December 31, 2010, and the changes in its net assets and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Washington, DC
February 15, 2011

Drolet + Associates, PLLC

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.
STATEMENT OF FINANCIAL POSITION
December 31, 2010
(With Summarized Financial Information for December 31, 2009)

	2010	2009
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 525,067	\$ 732,445
Investments	3,605	-0-
Bequests receivable	229,883	222,120
Foundation grants receivable	85,000	20,000
Contributions & pledges receivable	77,355	30,260
Due from SLDN Freedom to Serve	5,560	-0-
Prepaid expenses and other current assets	48,112	51,040
TOTAL CURRENT ASSETS	974,582	1,055,865
FIXED ASSETS		
Furniture and equipment	224,608	224,608
Less accumulated depreciation	(213,270)	(198,155)
TOTAL FIXED ASSETS	11,338	26,453
BEQUESTS RECEIVABLE, net of current portion	413,792	635,912
FOUNDATION GRANTS RECEIVABLE, net of current portion	-0-	10,000
DEPOSITS	3,675	3,675
TOTAL ASSETS	\$ 1,403,387	\$ 1,731,905
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Accounts payable	\$ 11,072	\$ 23,401
Accrued expenses	74,120	62,793
Line of credit	-0-	150,000
Notes payable	11,431	15,667
Deferred revenue	76,800	66,625
TOTAL CURRENT LIABILITIES	173,423	318,486
NOTES PAYABLE, net of current portion	-0-	11,431
TOTAL LIABILITIES	173,423	329,917
NET ASSETS		
Unrestricted	501,289	513,956
Temporarily restricted, for subsequent years' activities	728,675	888,032
TOTAL NET ASSETS	1,229,964	1,401,988
TOTAL LIABILITIES AND NET ASSETS	\$ 1,403,387	\$ 1,731,905

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

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.
STATEMENT OF ACTIVITIES
For The Year Ended December 31, 2010
(With Summarized Financial Information for the Year Ended December 31, 2009)

	Unrestricted	Temporarily Restricted	2010 Total	2009 Total
REVENUE				
Contributions	\$ 1,299,862		\$ 1,299,862	\$ 1,545,580
Charitable bequest	7,763	\$ 7,763	15,526	30,080
Grants	854,820	75,000	929,820	839,103
In-kind contributions	1,399,845		1,399,845	803,813
Other income	2,481		2,481	3,316
Interest income	45		45	3,920
Net assets released from restrictions, expiration of time restrictions	242,120	(242,120)	-0-	-0-
TOTAL REVENUE	3,806,936	(159,357)	3,647,579	3,225,812
EXPENSES				
Program services	3,152,238		3,152,238	2,389,826
Management and general	232,950		232,950	226,335
Fundraising	434,415		434,415	553,696
TOTAL EXPENSES	3,819,603		3,819,603	3,169,857
CHANGE IN NET ASSETS	(12,667)	(159,357)	(172,024)	55,955
NET ASSETS, BEGINNING OF YEAR	513,956	888,032	1,401,988	1,346,033
NET ASSETS, END OF YEAR	\$ 501,289	\$ 728,675	\$ 1,229,964	\$ 1,401,988

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

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.
STATEMENT OF FUNCTIONAL EXPENSES
For The Year Ended December 31, 2010
(With Summarized Financial Information for the Year Ended December 31, 2009)

	Program	Management & General	Fundraising	2010 Total	2009 Total
Advertising	\$ 32,154	\$ 627	\$ 4,883	\$ 37,664	\$ 30,645
Equipment rental and expense	8,405	2,958	3,220	14,583	14,636
Catering	119,666	41,924	23,459	185,049	150,819
Conference, meetings & events	1,385		1,110	2,495	2,801
Depreciation			15,115	15,115	15,115
Dues and subscriptions	10,270	26	2,363	12,659	10,790
Entertainment and other expenses	6,602	262	1,255	8,119	8,126
Grant expense	1,240	130	1,630	3,000	2,000
Insurance	11,569	368	2,134	14,071	14,890
Licenses and permits	595	293	4,648	5,536	4,373
Interest expense	1,318	714	714	2,746	7,075
Miscellaneous	7,716	3,218	21,671	32,605	31,625
Office supplies	20,895	3,754	1,558	26,207	26,331
Payroll and benefits expense	984,001	94,072	251,161	1,329,234	1,253,016
Postage and delivery	7,436	667	6,032	14,135	32,512
Printing and reproduction	17,877	1,477	11,211	30,565	52,073
Professional fees	1,735,500	23,497	43,993	1,802,990	1,233,952
Rent	68,667	4,823	27,998	101,488	97,143
Service contracts	21,203	27,791	689	49,683	56,959
Telephone, internet and fax	13,024	7,068	3,725	23,817	16,282
Travel and meals	82,715	19,281	5,846	107,842	108,694
TOTAL	\$ 3,152,238	\$ 232,950	\$ 434,415	\$ 3,819,603	\$ 3,169,857

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

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.
STATEMENT OF CASH FLOWS
For The Year Ended December 31, 2010
(With Summarized Financial Information for the Year Ended December 31, 2009)

	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES:		
CHANGE IN NET ASSETS	\$ (172,024)	\$ 55,955
Adjustments to reconcile change in net assets to net cash (used in) provided by operating activities:		
Depreciation	15,115	15,115
Decrease in bequests receivable	214,357	195,612
Increase in foundation grants receivables	(55,000)	(30,000)
(Increase) decrease in contributions & pledges receivable	(47,095)	23,295
Increase in due from SLDN Freedom to Serve	(5,560)	-0-
Decrease in prepaid expenses	2,928	11,469
(Decrease) increase in accounts payable	(12,329)	8,917
Increase in deferred revenue	10,175	66,125
Increase (decrease) in accrued expenses	11,327	(868)
NET CASH (USED IN) PROVIDED BY OPERATING ACTIVITIES	(38,106)	345,620
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from the sales of investments	51,405	360,042
Donated investments	(55,010)	(116,722)
NET CASH (USED IN) PROVIDED BY INVESTING ACTIVITIES	(3,605)	243,320
CASH FLOWS FROM FINANCING ACTIVITIES:		
Repayments on line of credit	(150,000)	-0-
Repayment of note payable	(15,667)	(12,942)
NET CASH USED IN FINANCING ACTIVITIES	(165,667)	(12,942)
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(207,378)	575,998
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	732,445	156,447
CASH AND CASH EQUIVALENTS, END OF YEAR	\$ 525,067	\$ 732,445
Supplemental disclosure:		
Cash paid during the year for interest	\$ 2,746	\$ 7,075

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

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2010

NOTE A – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization Servicemembers Legal Defense Network, Inc. (SLDN) is a not-for-profit corporation incorporated in the State of Delaware on August 17, 1993. SLDN is a national, nonprofit legal services, watchdog and policy organization dedicated to ending discrimination against and harassment of military personnel affected by “Don’t Ask, Don’t Tell, Don’t Pursue, Don’t Harass” and related forms of intolerance.

SLDN is supported primarily by contributions, bequests, grants and special events.

Income Taxes SLDN is exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code (the Code) and did not conduct unrelated business activities. In addition, SLDN has been determined by the Internal Revenue Service not to be a “private foundation” within the meaning of Section 509(a) of the Code.

Fixed Assets SLDN capitalizes all fixed assets acquisitions in excess of \$5,000. Fixed assets are recorded at cost, if purchased, or fair market value at date of donation, if contributed. Depreciation is provided on a straight-line basis over the estimated useful lives of the assets.

**Cash and Cash
Equivalents** For the purposes of the statement of cash flows, SLDN considers all highly liquid investments with an initial maturity of three months or less to be cash equivalents.

Contributions SLDN reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. Restricted contributions for which the restrictions are met in the year received are considered unrestricted for financial statement purposes. When a donor restriction expires, that is, when a stipulated time restriction ends or the purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

**Donated
Services** Donated services are recognized as contributions in accordance with Financial Accounting Standards Board (FASB), *Accounting Standards Codification 958, Accounting for Contributions* (ASC 958), if the services (a) create or enhance nonfinancial assets or (b) require specialized skills, are performed by people with those skills, and would otherwise be purchased by SLDN.

Investments Investments are recorded at fair market value.

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.
NOTES TO FINANCIAL STATEMENTS (Continued)
December 31, 2010

NOTE A – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
(Continued)

Functional Expense
Allocation

The costs of providing the various programs and other activities have been summarized on a functional basis in the statement of activities. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

Accounting for
Uncertain Tax
Positions

The provision of Financial Standards Board (FASB) Accounting Standards Codification 740, *Income Taxes* (ASC 740) requires that a tax position be recognized or derecognized based on a “more-likely-than-not” threshold. This applies to positions taken or expected to be taken in a tax return. SLDN believes that it has appropriate support for any tax positions taken, and as such, does not have any uncertain tax positions that are material to the financial statements.

Estimates

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

Reclassification

Certain 2009 amounts have been reclassified for comparative purposes.

Prior Year
Information

The financial statements include certain prior year summarized comparative information in total but not by net 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 SLDN's financial statements for the year ended December 31, 2009 from which the summarized information was derived.

NOTE B – LEASING ARRANGEMENTS

In August 1997, SLDN entered into a lease for office space at 1612 K Street NW, Washington, DC. The annual minimum rental is subject to annual increases payable in monthly installments on the first day of each month. The original lease has been amended to include additional space and extend the lease term to October 31, 2011. In the normal course of business, the lease will be renewed or replaced by another lease.

For the years ended December 31, 2010 and 2009, rent expense was approximately \$101,000 and \$97,000, respectively.

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.
NOTES TO FINANCIAL STATEMENTS (Continued)
December 31, 2010

NOTE C – RETIREMENT PLAN

SLDN sponsors a defined contribution plan (the Plan) that operates under section 403(b) of the Internal Revenue Code. The purpose of the Plan is to provide retirement benefits for participating employees. SLDN contributes up to 2% of each participant's annual salary to the Plan on a one-to-one matching basis. For the years ended December 31, 2010 and 2009, SLDN made contributions of approximately \$22,000 and \$17,000, respectively.

NOTE D – BEQUESTS

In 2002, SLDN was the recipient of a bequest which will be paid in ten annual installments. The assets are held in a trust established by the decedent's estate. The first annual payment of \$85,785 was received in July 2002. Generally accepted accounting principles require that management estimate the potential future receipts from this bequest and record its entire value in the financial statements in the year the bequest is made. For the years ended December 31, 2010 and 2009, the estimated future receipt of the bequest were increased by approximately \$15,000 and \$1,500, respectively to reflect the change in value of the trust assets. The final cash payment will be received in June, 2011. The expected amount will vary depending on investment results over the next six months. The potential amount to be received over the next six months has been estimated, for financial statement purposes, at approximately \$126,000.

In 2008, SLDN was also the recipient of another bequest which will be paid in thirty-two quarterly installments until the fund is exhausted. The assets are held in a donor designated fund established by the decedent's estate. As of December 31, 2010, the value is estimated to be approximately \$517,000.

Bequests receivable as of December 31, 2010 and 2009 are as follows:

Description	2010	2009
Bequest receivable in less than one year	\$ 229,883	\$ 222,120
Bequests receivable in one to five years	413,792	635,912
Total bequests receivable	\$ 643,675	\$ 858,032

NOTE E – CONCENTRATIONS

SLDN maintains cash balances at several financial institutions in the Washington, DC metropolitan area. Accounts at each institution are insured by the Federal Deposit Insurance Corporation (FDIC). At times during the year, SLDN's cash balances exceeded the FDIC insurance amount. Management believes the risk in these situations to be minimal.

As of December 31, 2010 and 2009 approximately \$75,000 and \$30,000 or 88% and 100% of foundation grants receivable was from one donor.

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.
NOTES TO FINANCIAL STATEMENTS (Continued)
December 31, 2010

NOTE F – NOTE PAYABLE

During the year ended December 31, 2008, SLDN entered into a financing arrangement to purchase software for approximately \$46,000 at an interest rate of 10.9%. Payments are due in equal monthly installments of approximately \$1,500.

NOTE G – LINE OF CREDIT

On January 17, 2006, SLDN entered into a revolving line of credit agreement with Bank of America for \$150,000. This line of credit bears a variable interest rate equal to Bank of America's Prime Rate plus .5%. Prior to year end, the line of credit was renewed through July 1, 2011. It is secured by substantially all assets of SLDN. For the years ended December 31, 2010 and 2009, SLDN had a balance of \$0 and \$150,000, respectively.

NOTE H – DONATED SERVICES

For the years ended December 31, 2010 and 2009, in-kind contributions consisted of the following program expenses.

Description	2010	2009
Legal services	\$ 1,395,015	\$ 793,746
Advertising	4,830	5,087
Other materials and services	-0-	4,980
Total In-Kind	\$ 1,399,845	\$ 803,813

NOTE I – TEMPORARILY RESTRICTED NET ASSETS

As of December 31, 2010 and 2009, temporarily restricted net assets consisted of the following:

Restriction	2010	2009
Time restricted bequest receivable	\$ 643,675	\$ 858,032
Time restricted foundation grants	85,000	30,000
Total temporarily restricted net assets	\$ 728,675	\$ 888,032

For the years ended December 31, 2010 and 2009, releases from temporarily restricted net assets consisted of the following:

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.
NOTES TO FINANCIAL STATEMENTS (Continued)
December 31, 2010

NOTE I – TEMPORARILY RESTRICTED NET ASSETS (Continued)

Restriction	2010	2009
Time restricted bequest receivable	\$ 222,120	\$ 225,692
Time restricted foundation grants	20,000	-0-
Total temporarily restricted net assets	\$ 242,120	\$ 225,692

NOTE J – FAIR VALUE MEASUREMENTS

Financial Accounting Standards Board (FASB) *Accounting Standards Codification 820, Fair Value Measurements and Disclosures* (ASC 820) defines fair value, establishes a frame work for measuring fair value and expands disclosures about fair value measurements. Fair value is 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 measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability, or in the absence of a principal market, the most advantageous market. Valuation techniques that are consistent with the market, income or cost approach, as specified by ASC 820, are used to measure fair value.

The fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value into three broad levels as follows:

Level 1 - inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets (examples include equity securities);

Level 2 - inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability other than quoted prices, either directly or indirectly, including inputs in markets that are not considered to be active (examples include corporate or municipal bonds);

Level 3 - inputs to the valuation methodology are unobservable and significant to the fair value measurement. The inputs to the determination of fair value require significant management judgment (examples include certain private equity securities and split interest agreements).

An investment's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

Fair values of assets measured on a recurring basis at December 31, 2010 and 2009 are as follows:

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.
NOTES TO FINANCIAL STATEMENTS (Continued)
December 31, 2010

NOTE J – FAIR VALUE MEASUREMENTS

	Fair Value	Fair Value Measurements at Reporting Date Using		
		Quoted Prices In Active Market for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
December 31, 2010				
Money market funds	\$ 485,680	\$ 485,680		
Bequest receivable	643,675		\$ 643,675	
Foundation grant receivable	85,000		85,000	
Marketable equity securities	3,605	3,605		
Total	\$ 1,217,960	\$ 489,285	\$ 728,675	\$ -0-
December 31, 2009				
Money market funds	\$ 686,091	\$ 686,091		
Bequest receivable	858,032		\$ 858,032	
Foundation grant receivable	30,000		30,000	
Total	\$ 1,574,123	\$ 686,091	\$ 888,032	\$ -0-

NOTE K – RELATED PARTY

On January 26, 2010, SLDN formed Servicemembers Legal Defense Network Freedom to Serve (SLDNFS), a nonprofit organization exempt under Section 501(C) (4) of the Internal Revenue Code. The purpose of SLDNFS is to promote the social welfare of all servicemembers affected by any type of discrimination based on their real or perceived sexual orientation, gender identity, or gender expression. SLDN and SLDNFS have officers and directors in common.

SLDN shares office space and other related expenses with the newly formed SLDNFS. Total shared expenses for the year ended December 31, 2010 were approximately, \$5,600 which was subsequently reimbursed to SLDN by SLDNSF.

NOTE L – SUBSEQUENT EVENTS

Subsequent events were evaluated through February 15, 2011, which is the date the financial statements were available to be issued.