

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.

AUDITED FINANCIAL STATEMENTS

December 31, 2008

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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, 2008, 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, 2007 financial statements, and in our report dated April 21, 2008, 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, 2008, 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.

Drolet + Associates, P.L.L.C.

Washington, DC
March 9, 2009

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.
STATEMENT OF FINANCIAL POSITION
December 31, 2008
(With Summarized Financial Information for December 31, 2007)

	2008	2007
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 156,447	\$ 284,491
Investments	243,320	9,950
Bequests receivable	218,047	132,115
Foundation grants receivable	-0-	75,000
Contributions & pledges receivable	53,555	112,684
Prepaid expenses and other current assets	62,509	40,664
TOTAL CURRENT ASSETS	733,878	654,904
BEQUESTS RECEIVABLE, net of current portion	835,597	396,346
FIXED ASSETS		
Furniture and equipment	224,608	179,262
Less accumulated depreciation	(183,040)	(172,213)
TOTAL FIXED ASSETS	41,568	7,049
DEPOSITS	3,675	3,675
TOTAL ASSETS	\$ 1,614,718	\$ 1,061,974
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Accounts payable	\$ 14,484	\$ 23,938
Accrued expenses	63,661	111,004
Line of credit	150,000	-0-
Notes payable	12,942	7,049
Deferred revenue	500	19,220
TOTAL CURRENT LIABILITIES	241,587	161,211
NOTES PAYABLE, net of current portion	27,098	-0-
TOTAL LIABILITIES	268,685	161,211
NET ASSETS		
Unrestricted	292,389	297,302
Temporarily restricted, for subsequent years' activities	1,053,644	603,461
TOTAL NET ASSETS	1,346,033	900,763
TOTAL LIABILITIES AND NET ASSETS	\$ 1,614,718	\$ 1,061,974

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, 2008
(With Summarized Financial Information for the Year Ended December 31, 2007)

	Unrestricted	Temporarily Restricted	2008 Total	2007 Total
REVENUE				
Contributions	\$ 1,458,323		\$ 1,458,323	\$ 1,656,829
Charitable bequest	100,001	\$ 643,354	743,355	124,668
Grants	561,488		561,488	538,498
In-kind contributions	472,382		472,382	513,600
Other income	7,773		7,773	20,364
Interest income	2,961		2,961	4,254
Net assets released from restrictions, expiration of time restrictions	193,171	(193,171)	-0-	-0-
TOTAL REVENUE	2,796,099	450,183	3,246,282	2,858,213
EXPENSES				
Program services	2,081,898		2,081,898	2,378,861
Management and general	225,324		225,324	474,349
Fundraising	493,790		493,790	259,027
TOTAL EXPENSES	2,801,012		2,801,012	3,112,237
CHANGE IN NET ASSETS	(4,913)	450,183	445,270	(254,024)
NET ASSETS, BEGINNING OF YEAR	297,302	603,461	900,763	1,154,787
NET ASSETS, END OF YEAR	\$ 292,389	\$ 1,053,644	\$ 1,346,033	\$ 900,763

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, 2008
(With Summarized Financial Information for the Year Ended December 31, 2007)

	Program	Management & General	Fundraising	2008 Total	2007 Total
Advertising	\$ 15,564	\$ 214	\$ 1,478	\$ 17,256	\$ 17,495
Equipment rental and expense	9,991	1,732	5,531	17,254	26,776
Catering	118,301	29,391	26,387	174,079	137,025
Conference, meetings & events	581		2,334	2,915	6,375
Depreciation	4,230	478	6,119	10,827	8,618
Dues and subscriptions	4,698	133	1,828	6,659	6,777
Entertainment and other expenses	5,430	912	2,608	8,950	59,539
Insurance	16,842	986	2,658	20,486	12,171
Licenses and permits	154	2	3,935	4,091	10,126
Interest expense	2,300	1,245	1,245	4,790	2,172
Miscellaneous	5,413	1,811	20,277	27,501	27,329
Office supplies	23,826	4,926	3,143	31,895	60,420
Payroll and benefits expense	863,619	114,297	259,548	1,237,464	1,449,373
Postage and delivery	19,274	1,166	13,254	33,694	66,200
Printing and reproduction	46,194	1,383	17,980	65,557	143,891
Professional fees	734,222	18,231	65,439	817,892	688,496
Rent	55,812	6,305	30,870	92,987	89,656
Service contracts	29,139	23,834	3,730	56,703	52,835
Telephone, internet and fax	30,373	5,010	7,442	42,825	56,109
Travel and meals	95,935	13,268	17,984	127,187	148,854
Web-site hosting and licenses				-0-	42,000
TOTAL	\$ 2,081,898	\$ 225,324	\$ 493,790	\$ 2,801,012	\$ 3,112,237

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, 2008
(With Summarized Financial Information for the Year Ended December 31, 2007)

	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES:		
CHANGE IN NET ASSETS	\$ 445,270	\$ (254,024)
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Depreciation	10,827	8,618
(Increase) decrease in bequests receivable	(525,183)	7,447
Decrease in foundation grants receivables	75,000	110,000
Decrease (increase) in contributions & pledges receivable	59,129	(28,566)
Increase in prepaid expenses	(21,845)	(10,949)
Decrease in accounts payable	(9,454)	(5,833)
(Decrease) increase in deferred revenue	(18,720)	6,375
(Decrease) increase in accrued expenses	(47,343)	44,388
NET CASH USED IN OPERATING ACTIVITIES	(32,319)	(122,544)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of investments	(243,320)	(9,950)
Proceeds from the sales of investments	249,610	175,537
Donated investments	(239,660)	(175,537)
NET CASH USED IN INVESTING ACTIVITIES	(233,370)	(9,950)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from line of credit	250,000	180,000
Repayments on line of credit	(100,000)	(180,000)
Repayment of note payable	(12,355)	(7,048)
NET CASH PROVIDED BY (USED) IN FINANCING ACTIVITIES	137,645	(7,048)
NET DECREASE IN CASH AND CASH EQUIVALENTS	(128,044)	(139,542)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	284,491	424,033
CASH AND CASH EQUIVALENTS, END OF YEAR	\$ 156,447	\$ 284,491
Supplemental disclosure of non-cash investing and financing activities:		
Obligation incurred for the purchase of software	\$ 45,346	\$ -0-
Supplemental disclosure:		
Cash paid during the year for interest	\$ 4,790	\$ 2,172

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

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2008

NOTE A – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization	<p>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.</p> <p>SLDN is supported primarily by contributions, bequests, grants and special events.</p>
Income Taxes	<p>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.</p>
Fixed Assets	<p>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.</p>
Cash and Cash Equivalents	<p>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.</p>
Contributions	<p>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.</p>
Donated Services	<p>Donated services are recognized as contributions in accordance with SFAS No. 116, Accounting for Contributions Received and Contributions Made, 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. Volunteers also provided fundraising services throughout the year that are not recognized as contributions in the financial statements since the recognition criteria under SFAS No. 116 were not met.</p>
Investments	<p>Investments are recorded at fair market value.</p>

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.
NOTES TO FINANCIAL STATEMENTS (Continued)
December 31, 2008

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.

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 2007 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 the Organization's financial statements for the year ended December 31, 2007 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.

The following is a schedule of future minimum lease payments as of December 31, 2008:

<i>Year Ending December 31,</i>	<i>Amount</i>
2009	\$ 96,540
2010	100,890
2011	87,200
Total future minimum lease payments	\$ 284,630

For the years ended December 31, 2008 and 2007, rent expense was approximately \$93,000 and \$90,000, respectively.

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.
NOTES TO FINANCIAL STATEMENTS (Continued)
December 31, 2008

NOTE C – RETIREMENT PLAN

SLDN sponsors a defined contribution plan (the Plan) that operates under section 403(b) of the Internal Revenue Code (IRC). 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, 2008 and 2007, SLDN made contributions of approximately \$18,000 and \$23,000, 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 year ended December 31, 2008, the estimated future receipt of the bequest was decreased by approximately \$55,000 to reflect the change in value of the trust assets. For the year ended December 31, 2007, the estimated future receipt of the bequest increased approximately \$125,000. Cash payments will be received once each year for the next three years. The amounts will vary depending on investment results over those intervening years. The potential amount to be received over the next three years has been estimated, for financial statement purposes, at approximately \$356,000.

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, 2008, the value is estimated to be \$699,000.

Bequests receivable as of December 31, 2008 and 2007 are as follows:

Description	2008	2007
Bequest receivable in less than one year	\$ 218,047	\$ 132,115
Bequests receivable in one to five years	835,597	396,346
Total bequests receivable	\$ 1,053,644	\$ 528,461

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, 2007 approximately \$75,000 or 100% of foundation grants receivable was from two donors.

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.
NOTES TO FINANCIAL STATEMENTS (Continued)
December 31, 2008

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.

The future scheduled maturities of the note payable are as follows:

<i>Year Ending December 31,</i>	Amount
2009	\$ 12,942
2010	15,667
2011	11,431
Total payments	\$ 40,040

On August 18, 2005, SLDN entered into a financing agreement to purchase software with CitiCapital Technology Finance, Inc. in the amount of \$21,145. The term of this agreement was 39 months with a maturity date of December 31, 2008.

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%. Subsequent to year end, the line of credit was renewed through January 17, 2010. It is secured by substantially all assets of SLDN.

NOTE H – DONATED SERVICES

For the years ended December 31, 2008 and 2007, in-kind contributions consisted of the following program expenses.

Description	2008	2007
Legal services	\$ 466,950	\$ 460,583
Advertising	5,432	10,066
Web-site hosting and licenses	-0-	42,000
Other materials and services	-0-	951
Total In-Kind	\$ 472,382	\$ 513,600

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.
NOTES TO FINANCIAL STATEMENTS (Continued)
December 31, 2008

NOTE I – FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair Value Measurements

Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* (SFAS 157) defines fair value, establishes a framework for measuring fair value, establishes a fair value hierarchy based on the quality of inputs used to measure fair value, and enhances disclosure requirements for fair value measurements. SLDN accounts for its investments at fair value or considers fair value in their measurement. SLDN accounts for certain financial assets and liabilities at fair value under various accounting literature, including SFAS No. 124.

Fair Value Hierarchy

In accordance with SFAS No. 157, SLDN has categorized its financial instruments, based on the priority of the inputs to the valuation technique, into a three-level fair value hierarchy. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). If the inputs used to measure the financial instruments fall within different levels of the hierarchy, the categorization is based on the lowest level input that is significant to the fair value measurement of the instrument.

Financial assets and liabilities recorded on the Statement of Financial Position are categorized based on the inputs to the valuation techniques as follows:

Level 1

Financial assets and liabilities whose values are based on unadjusted quoted prices for identical assets or liabilities in an active market that SLDN has the ability to access (examples include active exchange-traded equity securities, listed derivatives, and most U.S. Government and agency securities).

Level 2

Financial assets and liabilities whose values are based on quoted prices in markets that are not active or model inputs that are observable either directly or indirectly for substantially the full term of the asset or liability. Level 2 inputs include the following:

- Quoted prices for similar assets or liabilities in active markets (for example, restricted stock);
- Quoted prices for identical or similar assets or liabilities in non-active markets (examples include corporate and municipal bonds, which trade infrequently);
- Pricing models whose inputs are observable for substantially the full term of the asset or liability (examples include most over-the-counter derivatives, including interest rate and currency swaps); and

SERVICEMEMBERS LEGAL DEFENSE NETWORK, INC.
NOTES TO FINANCIAL STATEMENTS (Continued)
December 31, 2008

NOTE I – FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

- Pricing models whose inputs are derived principally from or corroborated by observable market data through correlation or other means for substantially the full term of the asset or liability (examples include certain residential and commercial mortgage related assets, including loans, securities and derivatives).

Level 3

Financial assets and liabilities whose values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. These inputs reflect management's own assumptions about the assumptions a market participant would use in pricing the asset or liability (examples include certain private equity investments, long-term promises to give, split interest agreements, and long-term grants payable).

As of December 31, 2008, SLDN's investments valued at fair market value are considered Level 1 investments.

The market value of the investments as of December 31, 2008 and 2007 are as follows:

Description	2008	2007
Certificates of deposits	\$ 243,320	\$ -0-
Bank of America corporate bond	-0-	9,950
Total investments	\$ 243,320	\$ 9,950