Road Trip: Pearl River Resort
Current Perspectives on Class II Gaming
Financing Alternatives for Tribal Gaming Facilities

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In the early years of tribal gaming, financing for gaming operations was often difficult, or impossible to obtain. Management contracts under IGRA sometimes served primarily as financing vehicles, with the management company providing the financial backing for what was then perceived as a high-risk enterprise. The proven success of tribal gaming operations, and the demonstrated institutional stability of tribal governments, has now opened most of the traditional financing markets to tribes.

The three most common types of financing for larger gaming projects are commercial bank loans, investment banked (or brokered) financings placed with banks or other institutional investors, and syndicated bank financings. These are by no means the only methods of financing a large gaming project, but they are by far the most common.

Commercial and Investment Banks

Commercial and investment banks are not the same. A commercial bank is the type of bank that we all grew up with. It takes deposits, it offers checking and savings accounts, it makes loans. There are large commercial banks with offices across the country, as well as small commercial banks with only one office.

Investment banks do not take deposits, they do not offer checking accounts, and, in general, they do not make loans. They are brokers that have contacts with people or businesses with money who want to make loans or investments and, for a fee, they match borrowers with those lenders.

Many large commercial banks have a division, or affiliate, that is an investment bank. That way the same institutional “family” can provide both commercial banking and investment banking services.

Commercial Bank Loans

A commercial bank loan is probably the most straightforward of the three financing transactions considered in this article. In a commercial bank loan, the tribe deals with one bank that makes the loan to the tribe from the bank’s own funds. The basic features of a commercial bank loan include:

Nature of negotiations: The tribe negotiates directly with the institution that is lending it the money. The loan term, interest rate, collateral and security, and any covenants and restrictions, are negotiated directly with the commercial bank.

Nature of compensation: A commercial bank is compensated by the interest it charges on the loan, and sometimes by an additional, relatively small, non-use fee for any credit capacity made available to the tribe but not actually used. It often also charges an up-front (commitment or origination) fee, payable at the time the financing is done.

Nature of business covenants: Because the bank expects to have an ongoing, direct relationship with the tribe, covenants tend to be both objective (e.g., minimum levels of net income, minimum ratios of net income to debt service and maximum levels of debt to net income) and discretionary (e.g., requiring the bank’s consent for the incurrence of additional debt). Financial reporting obligations are usually more inclusive (e.g., annual, quarterly and perhaps monthly financial statements and annual financial projections).

Distribution of financial information: The tribe provides relevant financial information directly to the bank and can insist on confidentiality.

Nature of relationship: A commercial bank will stay in close contact with the tribe, reviewing the financial statements, keeping abreast of the tribe’s economic activity, and often calling on the tribal leadership. It will look for other products and services that it can offer. As the tribe needs additional financial accommodations (e.g., changes in covenants, additional financing), it is able to talk directly with its lender and the lender should be familiar with the tribe’s economic situation. If the relationship develops well, this should mean that changes to the financing terms or covenants will be easier to negotiate. If the relationship does not develop well, the tribe may find itself locked in with an uncooperative bank.

Investment Banked, or Brokered, Bonds or Loans

An investment bank does not lend its own money. It acts as an intermediary, matching up a borrower with one or more lenders (who may be individuals, financial institutions or both). The basic features of financing through an investment bank include:

Nature of negotiations: The tribe first negotiates with the investment bank, which proposes financing terms (loan term, collateral and security, covenants and restrictions) that it anticipates will acceptable to lenders. When that negotiation is concluded, the investment bank prepares an “offering document,” which is material describing the tribe, the use of the financing proceeds, the negotiated terms of the financing and the financial information relevant to the tribe’s ability to repay. The investment banker then distributes copies of that offering document to potential lenders to see if lenders are willing to lend money on that basis and, if so, at what interest rate. Lenders may accept the financing on the terms worked out between the tribe and the investment bank, or they may require changes, which would then go back to the tribe for it to
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consider. As a result, in some situations there can be two sets of negotiations— one between the tribe and the investment bank and a second when the actual lenders are identified. A good investment bank anticipates the positions of the lenders with the result that the second set of negotiations is minimal.

Nature of compensation: An investment bank is compensated by a one-time charge it collects at the time the financing is done. This fee is usually calculated as a percentage of the amount borrowed. The tribe will also pay interest on the loan, and perhaps commitment and/or non-use fees, to the actual lenders.

Nature of business covenants: Because the lenders do not generally have an ongoing, direct relationship with the tribe (the relationship that the tribe has is usually with the investment bank itself), these tend to be objective rather than discretionary (e.g., required ratios of net income to debt service; permission to incur additional debt payable from the same revenues so long as a required coverage ratio is maintained), with fewer provisions for obtaining lender consent for any action. Financial reporting obligations may be less demanding (e.g., annual financial statements).

Distribution of financial information: The tribe initially provides relevant financial information to the investment bank. That information is included in the offering document that goes to prospective lenders. While the tribe and the investment bank can request that the recipients keep that information confidential, the ability to do so will depend on how widely the document is distributed (fewer recipients makes it easier) and the nature of those recipients (institutional investors and banks are often easier to work with than individual investors).

Nature of relationship: The tribe may not know who its actual lenders are. In any event, the lenders will have little or no direct contact, and little continuing contact, with the tribe. They will deal with the tribe through the investment bank or through a trustee (which is why the financial covenants and tests to incur additional debt tend to be objective, not discretionary). Changes to the financing terms or covenants will be more difficult to make because of the need to identify the lenders and the possibility that there may be a significant number of them. The investment bank itself will usually stay in contact with the tribe and will look for other products and services that it can offer. If the tribe needs additional financing, and if it can be incurred within the terms of the financing documents, the investment banker will find new lenders (who may include some of the first lenders) to provide additional loans.

Syndicated Bank Financings

These financings are a hybrid of the two discussed above and are often used on the largest loans. In a syndicated bank financing, the bank with whom the tribe deals (the "agent") brings in a number of other lenders to form a lending syndicate. Each member of the lending syndicate, including the agent, is a party to the financing agreement with the tribe and makes a separate loan to the tribe under the financing agreement. The agent acts as the servicer for all of the syndicate members, transmitting loan advances from the lenders to the tribe and receiving loan payments from the tribe and distributing them to the members. In the event of a default, the agent, as secured party, will exercise remedies on behalf of all members.

The syndicate structure reflects the fact that, as a financing gets larger, individual banks begin to reach lending limits applicable to individual borrowers or to specific industries, and they look for ways to manage their risk exposure by "sharing" that risk with other lenders. Because it has attributes of both a commercial bank loan and an investment bank financing, the basic features of a syndicated bank financing come from both of the foregoing summaries. In the areas of the nature of the negotiations, the nature of the compensation and the distribution of financial information, a syndicated bank financing is more like an investment bank financing. In the areas of the nature of the business covenants and the nature of the relationship, it is more like a commercial bank loan. In short, in a syndicated bank financing the tribe is dealing with a bank that will be lending it some—but not all—of the amount the tribe needs from that bank's own funds, and at the same time will be looking for other banks to join in to the loan on the same terms.

The growth and success of tribal gaming operations, and the successful history of tribal lending, will continue to open these financial markets to tribes. As a tribe's gaming operations increase, it may become common for the tribe to be involved in all three of these financial markets. Tribes can now choose from among these markets and, with preparation and an understanding of the nature and expectations of the markets that are available to it, can select the financing structure that best meets its economic and relationship needs.

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