

Outline for April 29, 2005 ABA Seminar “Developing a Multi-Use Gaming Project on Native American Land”

Financing Opportunities Available for a Mixed-Use Gaming Project (Including Public Bonds and Traditional Bank Mortgages)

- Lenders are drawn to Indian casinos like flies are drawn to, um, oatmeal. Lenders are often much less enthusiastic about financing other Indian needs. But those who see the non-gaming business potential in Indian country understand that it remains a largely untapped market.
- There are several Federal (and a few state) programs designed to help lenders overcome their fears about lending in Indian country. On the Federal level, HUD, SBA, Commerce, FSA and others all have programs designed to reduce a lender's risk of loss, improve the terms under which an Indian borrower can obtain financing, or both. Some of these programs might be used to help finance a multi-use gaming project.
- The Bureau of Indian Affairs, within the Department of the Interior, has a particularly active Loan Guaranty, Insurance and Interest Subsidy Program. It can be used by lenders to significantly reduce potential loan losses, and qualified borrowers can even enjoy a temporary reduction in the effective interest rate they pay. This Program usually cannot be used to help fund gaming operations, but it can be used to help fund ancillary projects like hotels, restaurants, theaters, and other business enterprises. It is an extremely flexible Program.
- The guaranty portion of BIA's program even allows lenders the choice of whether to liquidate a defaulted loan's collateral themselves, or have BIA do so.
- Flexibility and creativity are essential to any sustained effort to finance projects in Indian country. You would not expect to structure a deal exactly the same way in Latvia and in Argentina; don't expect to do so when you deal with different tribes.
- Consider that the casino portion of the project might be on tribal trust property, but the hotel you want to fund next door may be on individually-owned trust property. Or allotted land with restrictions on alienation. Or fee land. Or something else. “Checkerboard” reservations are common. You have already heard that you may have to settle for a leasehold deed of trust or leasehold mortgage to secure the loan. Make sure that the lease term exceeds the loan term by at least a few years.

- Remember, too, that the nature of title ownership may affect who exactly has civil and criminal jurisdiction over the property, and that can drastically affect how you enforce any rights that the lender has in the real estate. Where legal procedures or jurisdiction are unclear, you may even want to consider an altogether different source of collateral.
- If the tribe itself is the intended borrower, and you need to obtain a leasehold deed of trust, recognize the inherent problem early on. A tribe cannot lease property from itself, and therefore give you a valid leasehold deed of trust. But the tribe **can** lease the property to another tribal entity that it creates, and then sublease the property back. Viola! A valid leasehold interest.
- Inexperienced lenders are prone to grab more security than they need, sometimes snuffing out prospects for fresh financing and stifling economic growth. When this happens, the lender can actually help turn a good loan into a bad one. This practice is particularly common in Indian country. Good lawyers understand this dynamic and do not encourage their lender clients to over-secure. (The practice also annoys tribes, who may just turn out to be the lender's next biggest customer.)
- There are instances where commercial lender financing may not be the best available choice. Sometimes a bond issuance allows the borrower to access better interest rates, or a longer repayment term. This option is still fairly new for Indian borrowers, but as Jeff will describe in more detail, it is becoming more common as the markets warm up to the potential of Indian bonds.

Financing Opportunities for a Mixed-Use Gaming Project

April 29, 2005 ABA Seminar
“Developing a Multi-Use Gaming Project on Native American Land”

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Tribal leaders marvel at the different reception they get from lenders, depending on the project under consideration. Ask about financing a casino, and the meeting is always upbeat and unhurried. Try to finance a cultural center, or a truck stop, or an electronics factory, and somehow the banker’s clock ticks louder.

It should come as no surprise that lenders like to make money. Compared with other business ventures, casinos seem like a sure thing. They seem to have little risk of failure, and then there is that enormous cash flow that has to wash through one or more accounts at some lucky bank. Given how well a casino might do, it is perhaps understandable that banks trip all over themselves to finance Indian casinos. But this emphasis on casinos demonstrates more about perceptions in the lending community than financial realities. Casino deals are not always worthwhile, and at the same time, many other worthy projects are getting ignored.

Casinos are no sure thing. There is a good deal of regulation to fret over, and they require the existence of a valid compact with the host state before they can lawfully operate. There is typically a complex management agreement involved, and that agreement alone can significantly impact a tribe’s “take” of casino operations. Casinos also have to be the right kind and size for their market, or they can fail. In fact, some regions of the country appear already to be at or beyond their gaming saturation point, so that casino operators are competing for a more-or-less finite number of customers. In a recent example, we have seen a formerly successful casino near a metropolitan area forced to contract in size to turn around was quickly becoming an *unsuccessful* business. The tribe had to return over 100 largely unused slot machines to the company from which they were leased, redesign its entire gaming floor to attract more customers, and go through a costly refinancing to make the tribe’s revised earnings match up better with its debt load. In short, any of a large number of problems can cause a casino to falter or even fail, which is usually a very awkward moment for the bank official who put the loan transaction together.

Still, when a casino successfully comes on line, it is usually the cornucopia that lenders dream of having for a customer. The lender can usually dismiss worries about loan repayment, and instead start fretting over how to keep the customer’s business when the tribe pays off its loan early. A few successes like that can cause a stampede of lenders to follow the development of the next tribe’s gaming aspirations.

Lender's do sometimes have that sort of experience outside of gaming loans, but when they do there is usually no readily reproducible formula for predicting another, similar success. It seems sometimes to be little more than luck when Ben & Jerry walk through the door. But in Indian country, that is where most of the need is — in non-gaming commercial loans. Further, that is almost certainly where most of the real lender opportunities lie. The problem is that lenders remain unfamiliar with what it takes to successfully lend money in Indian country.¹

The two main complications that have held back lending to Indian tribes and Indian businesses have always concerned collateral and jurisdiction. What follows is a brief discussion of these issues, and what they mean in the context of lending for a mixed-use gaming project.

What Do We Use For Collateral?

A well-known problem with financing Indian deals is that Indian real property is often held by the United States in trust, or else (in the case of some land owned by Indian individuals) the land is subject to a restriction on alienation. A typical knee-jerk reaction from lenders is that they cannot finance any significant deal without real property as collateral. Thus ends a borrowing relationship before it begins.²

As a real estate attorney, you should know better than that. One need not have a mortgage or deed of trust on the fee interest in real property in order to have meaningful recourse in the event of default. Often a mortgage or deed of trust on a leasehold interest will suffice.

To consider a leasehold mortgage as collateral, a lender need only assure itself that the lease is of adequate duration, and that the terms are reasonable. Different tribes and individuals are subject to different laws that may limit the length of any lease involving their trust (or otherwise restricted) land. Lease term limitations run from 5 to 99 years, so obviously it is important at the outset to look for, and find out about, the nature of the borrower's title to the property and the laws that relate to that particular kind of land. The borrower will probably be able to guide you toward this basic information, but of course it is up to the lender to complete the due diligence necessary to confirm what is legally permissible. Doing most of this work toward the beginning of the deal will simplify matters, because you will still have time to alter the structure of the transaction

¹ Indian borrowers can also share some of the blame for the relative lack of commercial financing in Indian country. There is a certain level of borrower education that has to exist, and sometimes that financial savvy is not present. That matter is beyond the scope of this paper, except to mention that various governmental and private programs attempt to address the problem.

² It is assumed at this point that the lender has already determined the nature of the borrower's rights in the real property offered as collateral, and found it problematic. Ownership of real property on and around Indian reservations is often of a "checkerboard" nature; *i.e.*, fee property may be adjacent to allotted property belonging to an individual Indian, which may be next to property held in trust by the United States for the benefit of a tribe. If the property offered as collateral is owned in fee, there is no problem of the sort that often troubles Indian deals. It does not matter that Indians own the fee property; it matters only when the property in question is subject to restrictions on its alienation, either by a statutory trust responsibility or otherwise.

in case some unforeseen limitation makes the initial idea of a leasehold mortgage impractical.

Supposing that the lease term is not a problem for your transaction, you will next want to consider whether any lease provisions or other applicable laws limit the right of the borrower to pledge the lease as collateral. Naturally, if you run across a lease provision, tribal ordinance, or federal law that says that the leasehold interest under consideration cannot be used as collateral for a loan, it will be necessary to think up a new loan strategy.

If there is no limitation on pledging the lease — or at least, no limitation that cannot be removed by a lease amendment or tribal resolution — the next task is to make sure that the property subject to the lease is sufficiently well-defined to be of use in the event of foreclosure. Commercial leases in Indian country often adhere to ancient BIA forms, designed in a far simpler day, and do not contain the level of detail and specificity that one expects to see in a current day commercial lease. That casual approach to leasing unfortunately extends to the definition of the leasehold property itself. Most commercial leases (of raw land, anyway) contain a metes and bounds description of the leased property, written by a surveyor and adopted by a title company. They also contain provisions regarding access, utilities, and other matters that are essential to the effective use of the property after a forced liquidation. In contrast, some Indian leases contain little of this detail. In fact, it is not uncommon to learn that two adjacent leases of tribal property inadvertently overlap. Clearly, it is in the best interests of both parties to get this sort of detail straightened out long before closing.

One thing that can make a leasehold interest on Indian land attractive as collateral is an extremely modest rental rate, or other generous terms. Unlike some collateral, a lease with a particularly low rate can be expected to actually attract bidders, if a loan default ever brings the parties to foreclosure. And it is not at all uncommon for a tribe or other Indian owner of trust or restricted property to offer Indian business start-ups, or businesses to be run by a tribal enterprise, a ridiculously low rental rate or other favorable terms, just to help launch the business. The value of these leases as collateral, however, is only preserved if the favorable terms do not disappear should someone else occupy the land during the lease term.

To put the point another way, let us say that a lease offers a tribal enterprise a five acre parcel, improved with a three story office building, for an annual rental of just \$500. As a piece of loan collateral, that lease would most likely attract several serious bidders in the event of default and commencement of foreclosure proceedings. Bidders would happily offer a significant premium to purchase a lease with such wonderful terms, provided of course that the lease still had several years to go. The premium paid for the lease at the foreclosure sale would be part of the lender's recovery on its bad loan. But if a provision in the lease were to require any party but the original lessee to pay an annual rental of \$650,000 or fair market value, whichever is greater, the value of the leasehold mortgage has probably just dropped to zero. A lender clearly needs to understand as

early as possible whether the lease in question contains this sort of lease provision, so that it can have the borrower get the lease amended to change the offensive provision.

Another wrinkle to consider is the case where the borrower is the tribe itself, and the property to be mortgaged is owned by the United States in trust for the tribe. The tribe cannot lease property (in which it owns a beneficial interest) to itself, and thereby give the lender a leasehold mortgage for purposes of security. Or can it?

One option is for the tribe to create a legally distinct tribal corporation or tribal enterprise, and cause a master lease of the property to be made to that entity. The tribe can then sublease that property from that entity, and in so doing, create a legal interest that a lender could use as collateral.

Would this same procedure work for securing the sticks, bricks and grass of a casino (as opposed to an ancillary, non-gaming business)? Yes and, maybe, no. Yes, one could provide for a leasehold mortgage that would allow the lender to foreclose on the leasehold interest, and occupy and use the building and land. But finding a way to transfer the right to operate the property *as a casino* is far more complicated than that, and would require a *very* inventive attorney. Among other problems, the Indian Gaming Regulatory Act, 25 U.S.C. 2701 *et seq.*, anticipates that the profits and operation of an Indian casino will go to a specific tribe, in strict accordance with a detailed agreement (a compact) with the host state. Transferring to another party the right to operate and receive the proceeds from an Indian casino is beyond the scope of this paper, and probably on a par with designing a manned mission to Pluto.³

What Court Are We In?

In traditional bank-financed commercial lending, one expects the loan to be secured by assets, a revenue stream, or both. In the day-to-day work of most attorneys, the procedure for securing this sort of collateral is so well-worn that most of the paperwork required to record the lien initially, and a good deal of the foreclosure work (when necessary) can be done by an experienced paralegal, law clerk, or legal secretary. That is because it is clear what forms to use, where to file them, and what procedures govern in the event of a forced liquidation.

That element of predictability is not often available to lawyers working on deals in Indian country. Indian tribes usually have complete civil jurisdiction over their lands,⁴ and that includes the ability to make up their own laws and to enforce them in their own courts. But tribes have not always experienced enough major financial deals to have in place

³ It is still meaningful to obtain a leasehold mortgage on the real property of a casino, however. In the case of an uncooperative borrower (as opposed to a failed business), the threat of shutting the casino's doors can bring about a remarkable change in the borrower's attitude.

⁴ What constitutes tribal lands is beyond the scope of this paper. Tribal jurisdiction can be a tricky subject, and can turn on whether the property in question is held in trust for the tribe or an individual Indian, or is subject to restrictions on alienation, or is held in fee. Even property held in fee can be subject to tribal jurisdiction, depending upon who owns it and where it is positioned in proximity to other trust or restricted properties owned by the tribe or individual Indians.

clear procedures to govern the next one. On top of that, many borrowers who are more-or-less associated with a tribal government can claim the privilege of sovereign immunity, meaning that unless the lender secures a partial waiver of that privilege, the lender cannot enforce the provisions of the loan in *any* court.

Not surprisingly, under these circumstances lawyers working on Indian loans often feel uncomfortable delegating even ministerial tasks to non-lawyers. Instead, they recognize that “standard” legal forms may require fresh thought and revision on such topics as choice of law, venue, and resolutions confirming the borrower’s authority. They must often add a provision on sovereign immunity, and think through the extent to which federal officials (particularly the Bureau of Indian Affairs) may have to approve various aspects of the financing, such as the encumbrance of certain assets. Aside from confirming whether the borrower’s collateral can be pledged at all, counsel for the lender must allow sufficient time to obtain those governmental approvals. These elements tend to make Indian transactions somewhat different than non-Indian transactions. In a typical non-Indian deal, the lender can usually assume with some safety that the borrower can pledge the assets it has offered, and can put off obtaining proof of authority to encumber the property and title information until the last minute before closing. In an Indian deal, however, that procedure may be unwise. The lender is often better advised to perform that part of its due diligence at a relatively early stage, since any indication that the right to pledge an asset is going to be complicated or impossible will necessitate re-thinking the entire structure of the transaction.

Another aspect of doing business in Indian country is that, to the extent the deal is governed by tribal law, it is by no means certain that that body of law will look anything like what the lender is used to seeing. Custom and tradition sometimes take the place of detailed written codes. Tribal governments are not always broken down into separate executive, legislative and judicial branches. And even when there is a constitution, a detailed set of tribal ordinances, and a tri-party government, sometimes there are other idiosyncrasies with respect to a tribe’s legal system that require study and understanding. So, when a lender asks to see the tribe’s version of the Uniform Commercial Code, or its laws concerning a borrower’s equitable right of redemption, the tribe might deliver a code book with the requested information. On the other hand, the tribe might explain that those kinds of laws have never been enacted, and that the tribe has been functioning just fine without them.

When a tribe’s legal system does not look like what the lender is used to seeing, it is common for the lender to require that the tribe adopt certain laws in order to do the deal. This is sometimes done without even first trying to understand if the laws are really necessary. Rather than try to explain a different system that has worked well for the tribe, needy borrowers often simply comply with the lenders’ requirements. Of course, some of this culture clash is unavoidable, since lenders are often subject to the requirements of federal or state laws, not to mention bank examiners. But sadly, there are some instances in which a lender’s requirements simply eclipse a tribe’s culture in the name of conformity. There are even cases when, by doing so, a lender has actually *given away* protections that the tribe’s legal system would have provided. For instance, one major

tribe in the southwest does not believe that a debtor can properly shield itself from collection efforts with a statute of limitations, and will often require the debtor to repay a debt long after state courts would dismiss the case.

Of course, not every tribe considers as culturally significant its laws and customs concerning lending practices. Many tribes are perfectly content to enact whatever laws a lender tells it to put in place in order to make a particular loan transaction occur. This observation leads to another discovery one can make when lending in Indian country.

Indian tribes are not all at the same stage of establishing their chosen governmental systems, much less the laws that they have enacted. As a practical matter, what that means is that a lender cannot always assume that the promulgation of adequate tribal laws will necessarily translate into an adequate remedy, should the lender need to resort to those laws.

Most tribes take their laws, and their judicial systems, very seriously. Apart from the pride inherent in doing anything well, tribes sometimes feel driven to justify themselves to non-Indians. The result is a very thoughtful and even-handed judiciary, which often operates much faster than its state counterparts.

On the other hand, there are instances where an Indian judicial branch has no permanent facilities where they can meet. If it is forced to hold court in the tribal council's chambers when that body is not in session, it may not be fair to expect the smooth administration of court paperwork, or a rapid and convenient trial. Worse still, there are occasions where a tribal government is in some disarray, and the judiciary suffers as a result — perhaps because a judicial post is unfilled, or because certain elected tribal officials tend to meddle in specific cases before the tribal court, or because a particular judge simply does not have the background necessary to adequately address the full range of matters that come up, etc. Local officials with the Bureau of Indian Affairs can often shed considerable light on how well a tribal court system works, and when the lender would do well to trust it.

In the final analysis, if a lender has perseverance, none of these concerns (or any others) has to stand in the way of completing a loan transaction.⁵ Accurately gauging the loan environment simply specifies the amount and kind of work that will be necessary to make the deal happen. If the tribe has a good judicial system, use it. If it has good laws, use them. If not, borrow from the host state's laws and/or judicial system.⁶ Flexibility and

⁵ I have written the bulk of this paper under the assumption that you, as a lawyer, will be representing a lender, particularly one that is largely unacquainted with Indian country. That of course may not be the case. Perhaps you will be asked to represent the borrower. If so, you must recognize that it is not productive to approach loan negotiations without bearing in mind that the lender will not loan your client any money unless you hand the lender a large stick to whack your client with in the event of default. But if your client intends to pay back the money, you should be able to find a way to structure the deal that gives the lender what it needs, and still saves your client from unnecessary affronts to its assets or sovereign rights.

⁶ When negotiating which judicial forum the parties will use to enforce loan provisions, the parties should select a court of general jurisdiction, *i.e.*, a state or tribal court. Absent a federal question or complete diversity of citizenship, the federal judicial system has no jurisdiction, and the parties cannot simply confer

creativity can open up a wide range of commercial financial opportunities in Indian country, far more than lenders are used to seeing outside of Indian country.

There are times, however, when the complications of securing a proposed loan with real property seem just too great in proportion to the potential value of the leasehold interest. In fact, even with a leasehold mortgage, and all the personal property the lender can obtain as collateral, the lender may remain unsatisfied with the prospects for repayment.⁷ In these cases, there may still be options that will make the deal worth the lender's while. There are several federal (and a few state) programs designed to help lenders overcome their fears about lending in Indian country, or their perception that available collateral is not quite sufficient to meet their normal underwriting standards. On the federal level, HUD, SBA, Commerce, FSA and others all have programs designed to reduce a lender's risk of loss, improve the terms under which an Indian borrower can obtain financing, or both. Some of these programs might be used to help finance a multi-use gaming project.

The BIA's Loan Guaranty, Insurance, and Interest Subsidy Program.

One particularly active program is operated by the Bureau of Indian Affairs, within the Department of the Interior. The Loan Guaranty, Insurance and Interest Subsidy Program, 25 U.S.C. 1481 *et seq.* and 25 CFR Part 103, can be used by lenders to significantly reduce their potential loan losses. This program can guarantee or insure the repayment of up to 90% of the principal and accrued interest due on a loan made by a lender to an Indian business. In the case of loan guarantees, moreover, the lender even has the option of whether or not to conduct asset liquidation before submitting a claim to BIA. If the lender does not want to bother with asset liquidation, it can apply for and accept BIA's payment in exchange for assigning all of its rights in the loan and collateral to BIA.

Another great feature of the Loan Guaranty, Insurance and Interest Subsidy Program is that certain qualified borrowers can get a temporary reduction in the effective interest rate they pay. For a period of up to five years, BIA will rebate a portion of the interest the borrower pays on the loan.

The Loan Guaranty, Insurance and Interest Subsidy Program usually cannot be used to help fund gaming operations, but it can be used to help fund ancillary projects like hotels, restaurants, theaters, and other business enterprises. It is extremely flexible, and has a long history of success.

jurisdiction on the federal courts by agreement. Most loan transactions do not involve federal questions, and tribes are not considered citizens of any state for diversity purposes.

⁷ Out of excessive caution, inexperienced lenders will sometimes attempt to grab more security than they really need, which is different from complaining of a legitimate shortage of collateral. Getting too much collateral can have the perverse effect of snuffing out prospects for fresh financing, and stifling economic growth. When this happens, the lender can actually help turn a good loan into a bad one. This practice is all too common in Indian country. Good lawyers understand this dynamic and do not encourage their lender clients to over-secure. (The practice also annoys tribes, who may just turn out to be the lender's next biggest customer.)

Summary.

In conclusion, if you take the time to work through all of the issues, the deal will happen. Flexibility and creativity are essential to any sustained effort to finance projects in Indian country. Remember, unlike most corporate borrowers, the tribe is not going anywhere. And it needs funding to make its plans turn into reality. Perhaps the nicest thing about completing one transaction in Indian country, is that it can form the basis for another loan, and another, and another.