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TFA Monthly Newsletter

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IN THE NEWS

Priority Distributions: Good, Bad, or Indifferent?

by David Howard

As we walk through gaming debt agreements with Tribal leadership, some are surprised and also a bit concerned when they realize that upon a default, the lender may stop any and all distributions to the Tribe. This provision is standard in all Tribal gaming loans and is the lenders' primary way to protect their loan. This is a scary thought for any Tribe – particularly those that depend on gaming revenues to fund their governmental operations, programs and per capita distributions.

One way to protect a certain amount of distributions to the Tribe is to include a provision called a Priority Distribution. These distributions are allowed to be made even in the event of default and are paid even before the lenders' are paid their principal and interest payments. The size of a Priority Distribution depends upon the total level of cash flow that supports the related financing; however, priority distributions typically range from $500,000 to $2 million per month, or $6 million to $24 million annually.

Important to note, the amount of Priority Distributions is not meant to fully fund government operations; rather, it provides for a baseline of protection that can be counted upon even in a

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Casino Revenue Sharing Bill Moves Forward after New York State Senate Approval

04/12/16 – WorldCasinoDirectory.com

Washington Gambling Commission Reconsiders New 'Skill' Games

04/13/16 – BellinghamHerald.com

Chumash Enterprises CEO Named Executive of the Year

04/23/16 – Independent.com

Oglala Sioux Tribe Approved for New Class III Gaming Compact

04/26/16 – WorldCasinoDirectory.com

Backers of Brockton Casino Denied Massachusetts License

04/29/16 – ProvidenceJournal.com

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default situation.

In a gaming-related financing, Priority Distributions are effectively treated like an operating expense of the casino. Therefore, lenders will deduct the amount of Priority Distributions from the casino EBITDA. The total amount of outstanding gaming debt is then divided by this "adjusted" EBITDA to calculate the primary financial loan covenant ratio – Total Leverage. Like all good things, the Priority Distribution comes with a cost, as the Total Leverage Ratio is a key metric in determining the interest rate on the loan… the higher the leverage, the more expensive the interest costs. While it may be important, having the safety of a Priority Distribution could cost a Tribe millions of dollars over the life of the loan.

Is it worth it? The answer, as you might expect, is that it depends. For Tribes with slightly higher Total Leverage (greater than 2.5x) and a high dependence on gaming revenues to fund governmental operations, it often is a good idea to negotiate a Priority Distribution into the debt agreements. For Tribes with lower Total Leverage and strong cash flow from their gaming operations that generate well in excess of $12 to $24 million in tribal distributions anyway, the incremental interest cost is like buying insurance that you will never need. That said, political factors may come into play and some Tribes may want to insure a "default proof" distribution to protect government bond obligations or per capita payments.

Each situation is unique, but it's good to know there is mechanism available to Tribes to protect a certain amount of distributions.

TFA CAPITAL PARTNERS

TFA
400 Continental Boulevard
Suite 320
El Segundo, CA 90245
tfacp.com

KRISTI JACKSON
CHAIRMAN
310.341.2335
kjackson@tfacp.com

DAVID HOWARD
CEO
310.341.2795
dhoward@tfacp.com

JEFF HEIMANN
MANAGING DIRECTOR
310.341.2518
jheimann@tfacp.com

WILLIAM CRADER
MANAGING DIRECTOR
310.341.2336
wcrader@tfacp.com

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