



TEN QUESTIONS TRIBAL COUNCIL
SHOULD ASK BEFORE BORROWING MONEY





Borrowing money for tribal projects can be confusing. It's a challenge to sort through the numbers and financial jargon and understand the fine print. But the task becomes more manageable if you stay focused on the basics. Following is a list of ten very fundamental questions that Tribal Council may want to think about as it embarks on the borrowing process.

10 KEY QUESTIONS BEFORE BORROWING

1. Why are we borrowing?
2. Does borrowing help us achieve our objectives?
3. How are we going to pay for it?
4. Have we considered all of our options?
5. How much does it cost?
6. What are the risks of borrowing?
7. What have we done to protect ourselves?
8. Has the deal been clearly explained?
9. Are we being asked to waive our sovereign immunity?
10. Have all legal requirements been met?

WHY ARE WE BORROWING?

Borrowing is not the only way to pay for things. There may be other options, such as using cash on hand, grant monies or federal funding. Most often, borrowing is something that tribal governments do when other sources aren't enough. However, financial need is not the only motivation. Borrowing may have economic or planning advantages. For example, it may be better to borrow instead of paying in cash (or depleting tribal investments) if the interest you pay over time is less than the earnings you would sacrifice by spending current assets. In some cases, borrowing may help existing programs continue without budget cuts even as new tribal projects arise. In other cases, it may simply be more practical to pay for long-term capital improvements, such as an administration building, over the expected useful life rather than paying entirely up front.

DOES BORROWING HELP US ACHIEVE OUR OBJECTIVES?

Tribal governments have a long list of governmental and business objectives: housing, health care, education, cultural preservation, infrastructure, economic development and so on. All are important, and prioritizing among them is never easy. A borrowing should help meet one or more of these objectives while fitting within a tribe's debt management plan. Occasionally, there may be social purposes indirectly served by a borrowing. For example, a tribe may promote the economic advancement of its members through per capita payments. It may be hard to maintain these payments, though, if most of the tribe's revenue is being used to fund a casino expansion. By borrowing, it may be possible to simultaneously fund the expansion project *and* stabilize per capita payments at current levels.

HOW ARE WE GOING TO PAY FOR IT?

Borrowings come in different forms. Some are called general obligations, meaning a promise to pay from any and all available sources. Other borrowings are referred to as limited obligations, meaning that the promise to pay is limited to certain sources (such as a particular revenue stream or other assets). Often, these limited sources are then pledged as collateral. Selecting which structure works best depends upon a variety of credit factors and the tribe's objectives. Governmental borrowings may be more easily accomplished through an unsecured general obligation structure, while business enterprise borrowings often work better as limited obligations. There is no one-size-fits-all rule. However, clearly defining the sources of payment which are available (and unavailable) for servicing a debt is an essential part of any borrowing.

HAVE WE CONSIDERED ALL OF OUR OPTIONS?

Tribal leaders must understand not only the size, scope and cost of a particular project, but also what their options are for financing the project. For example, would a bank loan, a bond issue, or a high-yield offering make the most sense? Should the tribe think about credit enhancement—that is, a letter of credit, bond insurance, BIA or HUD guarantee, or other form of credit support as a means of reducing interest rate? Would a credit rating from one of the Wall Street rating agencies be helpful? Does any part of the borrowing qualify for cheaper tax-exempt financing? If so, has the tribe taken the steps necessary to pursue that option, such as passing a reimbursement resolution? To answer these questions, Tribal Council must examine the facts and circumstances of the project and the borrowing and determine which path leads to the best overall result for the tribe.

HOW MUCH DOES IT COST?

The cost of a borrowing is determined by the total amount of interest paid over the life of the loan or the bond issue, plus the various fees and expenses involved. An interest rate may be “fixed” (meaning it doesn’t change) or it may “float” (it changes). Fixed interest rates are more common with bond issues. Floating interest rates are more common with loans and usually are tied to some reference point, such as a prime rate or LIBOR index. Interest rate risk can be managed through swap agreements and similar products, which add another layer of cost. In addition to interest paid, there may be various fees—commitment fees, placement fees, underwriting discounts, fees of credit enhancement providers, etc. Expenses would include the cost of professionals involved, such as lawyers, accountants and others. Some costs are incurred only if certain conditions happen, such as a prepayment premium, a default rate of interest, or a requirement to provide additional collateral. Needless to say, understanding the total cost is a primary consideration.

WHAT ARE THE RISKS OF BORROWING?

Perhaps the most obvious risk is being unable to pay a debt as it comes due. This risk is particularly high with borrowings where the entire principal amount is due at maturity rather than paid down gradually over time. Before approving any borrowing, Tribal Council should be convinced of the tribe’s ability to repay (or refinance). Other risks include contractual covenants that may be too burdensome and impair operating flexibility. Restrictions on enterprise revenue distributions, limitations on additional debt, and various types of performance ratios (such as coverage or leverage tests) are examples of covenants that are quite common but problematic if not properly tailored to a tribe’s own situation. Another risk often overlooked is the risk of exposing confidential information, such as financial statements and operating data, to third parties. In general, it’s wise to think ahead about what can happen to upset a deal, and what can be done to cure defaults and correct problems.

WHAT HAVE WE DONE TO PROTECT OURSELVES?

Perhaps the best way to prevent a problem when borrowing is to know your limits and protect what is off-limits. Knowing your limits means more than just using caution in how much you borrow. It means being informed enough about the market to assess your own relative strengths and weaknesses and what your options are. This knowledge will help you negotiate terms and conditions that are commercially reasonable, serve the tribe’s purposes and allow for sufficient flexibility. Assembling a strong team of tribal representatives and advisors to look out for the tribe’s interests will help ensure adequate protections. Examples of protective measures might include a firewall between property that is pledged as collateral and assets that are not (such as assets held in trust or which are otherwise restricted). Or, if tribal government requires a certain level of funding to maintain basic functions, that need should be taken into account when structuring the various debt covenants. In short, protection means anticipating problems before they happen.

HAS THE DEAL BEEN CLEARLY EXPLAINED?

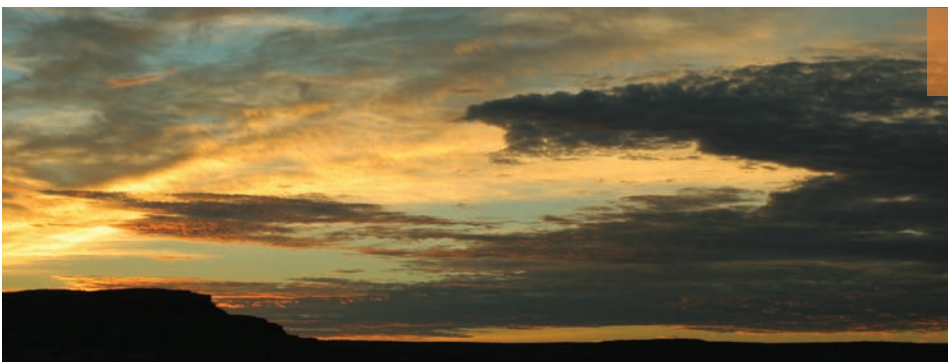
The financing team, including staff and professionals involved, should make sure that the terms of a proposed borrowing are adequately explained to Tribal Council in plain English so that Council can make an informed business decision. A clear explanation usually requires balancing substance and detail. The point is not to bury Tribal Council in information. Rather, the goal is to make sure that Tribal Council sees the big picture and is given enough detail on the business and legal issues to make a confident decision. The explanation process may take time, so it is often a good idea to conduct an informal work session with Council to review the documents and discuss the deal *before* it is placed on the agenda for vote. This gives Council an opportunity to ask questions, challenge assumptions and determine whether it is the right deal for the tribe.

ARE WE BEING ASKED TO WAIVE OUR SOVEREIGN IMMUNITY?

Most borrowings include some kind of waiver of sovereign immunity by the tribe. That’s because lenders and investors generally are not willing to provide money under an unenforceable agreement. At the same time, tribes generally are not willing to provide an open-ended, blanket waiver of immunity. It is usually possible, though, to find an acceptable middle ground in the form of a *limited* waiver of sovereign immunity. The waiver can be limited in a number of respects. For instance, it may be limited in recourse only to particular assets, limited as to specific courts (or to the arbitration of disputes), limited as to types of claims and the amount of any recovery, limited in time for bringing claims, and so forth. There is probably nothing more important and more unique to each tribe in a business context than a waiver of sovereign immunity. Therefore, the scope of any waiver should be carefully reviewed and clearly understood.

HAVE ALL LEGAL REQUIREMENTS BEEN MET?

Tribal Council should confer with the Tribal Attorney about whether the terms of a borrowing are consistent with tribal law. Among other things, tribal law may dictate how much the tribe can borrow, procedures for entering into contracts, restrictions on pledging tribal assets, limitations on waivers of sovereign immunity, special licensing requirements that may apply to third parties, and what effect (if any) a borrowing may have on the tribe’s gaming revenue allocation plan, investment policies, or other laws. Tribal Council should also confirm that the borrowing is consistent with the terms of existing obligations, such as the tribe’s gaming compact or other borrowing agreements that may already be in place.





ABOUT ORRICK

Orrick has been the nation's top-ranked bond counsel firm for more than a decade and is listed in Band 1 (highest category) in the field of Native American Law by *Chambers USA—America's Leading Lawyers for Business*.

We have been privileged to represent tribal governments in more than a dozen states on a variety of projects, including land acquisitions, health clinics, tribal housing, schools, government administration buildings, cultural centers, tribal utilities, parks and recreation facilities, and so on. In addition, we have represented tribal business enterprises in gaming, hotel and entertainment facilities, manufacturing plants and other commercial activities. Our Indian Tribal Finance Group is nationwide and comprises lawyers from our Public Finance, Corporate, Banking, Tax and Securities practices.

For more information or assistance, please contact Townsend Hyatt, Chair of Orrick's Tribal Finance Practice, at (503) 943-4820 or thyatt@orrick.com.

Orrick, Herrington & Sutcliffe LLP | 666 Fifth Avenue | New York, NY 10103-0001 | United States | tel +1-212-506-5000
Attorney advertising. As required by New York law, we hereby advise you that prior results do not guarantee a similar outcome.

NORTH AMERICA

LOS ANGELES NEW YORK ORANGE COUNTY PACIFIC NORTHWEST
SACRAMENTO SAN FRANCISCO SILICON VALLEY WASHINGTON DC



ORRICK

WWW.ORRICK.COM