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IN THE NEWS

**Tribal M&A—What You Should Know**

by Mack Rossoff

Tribes confront a familiar issue: how do I invest this excess cash flow to build value for my Tribe in the future? How do I grow? Increasingly, Indian gaming is looking to the commercial gaming M&A market for growth and we believe this trend will continue.

Until fairly recently, the vast majority of Tribes with excess cash flow from gaming operations invested in one of three ways: 1) expansion of their existing operations; 2) additional gaming operations on Tribal lands or other in-state territory taken into trust; and 3) other businesses unrelated to gaming in order to diversify the sources of their revenue. The gaming expertise and franchise value created by successful tribal gaming operations was exploited mainly in nearby expansions. In other words, the Tribes stayed close to home.

There were a couple of notable exceptions, however. Mohegan Sun of Connecticut, one of the country's largest Indian gaming operators, began to venture off reservation over ten years ago. In 2005, Mohegan purchased the Pocono Downs – a commercial racetrack that was slated to receive a slot license – from Penn National Gaming Corporation. Mohegan paid \$240 million to acquire

the facility and hundreds of millions more to build a slots casino in 2006, a table games addition in 2010 and a hotel in 2013. Mohegan's strategic logic was pretty clear: as one of the premier names in gaming in the Northeastern United States, Mohegan would leverage its expertise and highly respected reputation and become a regional gaming powerhouse. Mohegan continues to operate Pocono Downs to this day and generates approximately \$50 million of cash flow annually from the operation – a respectable, although not spectacular return on a substantial investment. Mohegan's other regional forays have been more uneven. Attempts to secure gaming licenses in Palmer and Boston Massachusetts and in the Catskills in New York have not panned out, while a management contract at the Resorts Casino Hotel in Atlantic City has been fruitful. (Mohegan has also sponsored the Cowlitz resort casino in Washington State, now under construction, and a new casino resort mega-complex at the Incheon International Airport in South Korea.)

The other notable exception to the "stay close to home" rule is provided by The Seminole Tribe of Florida. The Sem-

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inoles, operators of the Hard Rock gaming resorts in Hollywood and Tampa Florida and other gaming facilities in Florida, are also the owner of the Hard Rock International Corporation. A purely commercial operation, Hard Rock was purchased by the Seminoles in 2007 from its then-owner, Rank PLC, for nearly \$1 billion. The company, wholly-owned by the Seminoles, now operates 164 cafes, 22 hotels (with 15 more under development), 11 casinos and five concert venues.

On the few occasions in which other Tribes that attempted to leverage their gaming expertise in off-reservation commercial gaming and resort operations, the results have, historically, not been pretty. But in recent months, a corner, of sorts, has been turned, as demonstrated by two announcements of Tribes purchasing commercial casino operations. In June of 2016, the Poarch Creek Indian Gaming Authority announced its acquisition of the Margaritaville Resort Casino in Bossier City, Louisiana for an undisclosed amount. Poarch Creek, sounding much like any large, successful and growing business, declared: "This acquisition will further our goal of building a great company...." Two months later, in August of 2016, the Laguna Development Corporation, an arm of the Laguna Pueblo Tribe of New Mexico, announced it was acquiring the Isle of Capri Casino Hotel in Lake Charles, Louisiana for \$134.5 million, or roughly 8.5 times the target's cash flow. Laguna's press release stated: "This reflects our aggressive strategy for growth." Tribes have proved they are now financially and operationally capable of competing for and winning commercial gaming properties outside their traditional service areas.

This move by Tribes into the commercial M&A market on a broader scale

was likely inevitable. Large, successful companies are driven financially and managerially to grow aggressively and become great – witness the statements above. In addition, Tribes with excess cash flow are confronting the same challenges as other investors to find lucrative non-gaming opportunities in a world with very low interest rates and slow corporate growth. The benefits to a Tribal gaming company of the acquisition of a commercial casino are manifold:

- The Tribe is purchasing a known quantity and can have confidence in its due diligence;
- Operating management can be inserted into the target and performance improved;
- Tribal capital is often patient – the Tribe can take the time needed to make the acquisition successful;
- Financial returns will likely be in the range of 8% to 10% cash on cash in the early years of the acquisition, an adequate return and one that compares well with investments in marketable securities;
- A number of synergies with existing operations may be available, even if the target is geographically remote, such as benefits in purchasing, marketing and management development;
- As the off-reservation gaming company grows, its cost of debt capital will tend to fall since larger credits tend to be granted lower rates than smaller credits.

These transactions are not without their pitfalls. First, most gaming acquisitions are competitive and Tribes must be careful not to be outmaneuvered by rivals who are more experienced in the acquisitions business. Tribes must be prepared to pay a market price (7.5X to 8.5X EBITDA for large facilities) and pro-

vide a compelling case that they can secure a state gaming license, raise financing and close quickly. Second, Tribes must be prepared to pay a small premium when conducting their first commercial acquisition. Sellers will require the additional compensation when dealing with an entity that has never been granted a state gaming license for a commercial property. And third, Tribes must be confident that they have the management talent to handle the new entity and be prepared, particularly in a highly competitive jurisdiction, to add to the team with non-Tribal professionals, if necessary.

In the next five years, the gaming industry in the United States will face continuing challenges and considerable change. The industry will need to deal with the reality of a slow-growth economy, demographic shifts and changing fashions. Numerous gaming entities will be swapping out of assets as they emerge from bankruptcy (eg; Caesar's) or cash-out financial investors (eg: Affinity or Twin Rivers). Tribal governments would do well to follow the example of the Poarch Creek and Laguna nations – set their sights on commercial gaming assets they can afford and manage. It is likely that more than one Tribal nation will build a great gaming company and benefit their members for years to come.

*Mack Rossoff is Managing Director and founder of Rossoff & Company LLC, an independent investment banking and advisory firm, providing advice on mergers and acquisitions, corporate strategy and restructuring. Since 2008, Rossoff & Co. has successfully executed challenging assignments for clients across a wide spectrum of industries. Over their careers, Rossoff & Co professionals have executed a combined \$200 billion in transactions.*



**TFA**  
400 Continental Boulevard  
Suite 320  
El Segundo, CA 90245  
[tfacp.com](http://tfacp.com)

#### KRISTI JACKSON

CHAIRMAN  
310.341.2335  
[kjackson@tfacp.com](mailto:kjackson@tfacp.com)

#### JEFF HEIMANN

MANAGING DIRECTOR  
310.341.2518  
[jheimann@tfacp.com](mailto:jheimann@tfacp.com)

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