

# TRIBAL ECONOMIC DIVERSIFICATION: EXPANDING BEYOND GAMING

By Valerie Red-Horse and Derril Jordan

The Indian country press is filled with articles and stories extolling the virtues of tribal economic development, with many of those articles focusing on the need for, and benefits of, diversification of the tribal economic base. It is hard to argue with the wisdom of such advice, and few, if any, tribal leaders or tribal sovereignty advocates would take exception to anything that has been said in favor of economic development generally, and diversification specifically.

Gaming has become the primary economic engine for substantial economic growth throughout Indian country. If a tribe is located in an area where gaming can make a meaningful contribution to the tribal economy, both in terms of generating tribal governmental revenues and creating job opportunities for members, gaming typically can provide a substantial form of economic development. However, many tribes are located in areas where gaming is not an immediately available practical choice for significant and sustained economic development. (According to *Casino City's Indian Gaming Industry Report, 2011 Edition*, in 2009, 237 tribes operated gaming facilities, which is only 42 percent of the 564 federally recognized tribes in the United States.) Those non-gaming tribes must consider other ventures and activities for economic development. There are also many gaming tribes that have underperforming gaming facilities due to a rural location or a highly competitive market. Finally, there are even the most successful gaming tribes who realize that it is unwise to have an unbalanced business concentration, subject to industry sector and political risk. Therefore, as the markets begin to heal from the recent recession and dislocation, both gaming and non-gaming entities are looking at new economic opportunities to diversify tribal portfolios. Although such diversification is undoubtedly a wise move, the process itself provides some unique challenges.

For many tribes, gaming has generated returns in the 30 percent to 40 percent range. Few other ventures yield returns of that nature and can be characterized by the "build it and they will come" phenomenon of some of the more lucrative gaming establishments in Indian country. In fact, most non-gaming ventures that tribes will consider will show potential returns of 3 percent to 10 percent—figures common throughout other sectors of the business world as stable, modest return expectations on investments. For many gaming tribes, vertically integrated businesses within the gaming sector are a natural next step

when seeking early diversification, such as expansion into management companies, slot machine providers, food and beverage suppliers, and other gaming vendor services. This methodology can often provide immediate access into an established and existing customer base and is additional business diversification with added job creation, but to be clear, it does not provide true sector diversification, as these all remain in the gaming/hospitality industry. Therefore, many tribes are looking to expand into widely diverse sectors such as energy, transportation, banking and health care. Whatever the targeted business expansion, however, the keys to successful tribal economic development include managing expectations and then choosing the right ventures and the right "partners" with which to do business. This means that due diligence (i.e., complete and thorough vetting and review) is paramount.

There are many legitimate companies and individuals that can assist tribes in their economic development efforts and that are willing to do business in Indian country. Unfortunately, there are also more than a few such business suitors that are neither competent nor honorable. Some of the would-be tribal business partners will bring viable economic ventures to tribes, but they think that tribes will be easy marks from which they can wrest more than their fair share. Others are little more than snake oil salesmen who haven't done their own due diligence and are the fools who will soon be parted from their own money. Quality due diligence is the solution to avoiding doing business with either type.

Many tribal suitors invite tribes to invest what little money they have or can borrow on a venture for which market studies and business plans have never been developed. Economic development investment for a tribal government should be a thoughtful process requiring due diligence and the thorough review of the feasibility of the venture, including the market study and business plan for the venture, which should include the management capabilities and both historical and projected financials. More specifically, a tribe needs to know how much money it is being asked to invest, how long it will take before the tribe begins to see a return on its investment, and what the rate of return will be. If job creation is a primary goal, as it usually is, the tribe also needs to know how many jobs will be created and what the average wage will be. Likewise, the tribe needs to know what its suitor is willing to invest

and how it will see a return on its investment. Is the suitor willing to invest, and thereby risk, some of its own money, or is it proposing that the tribe provide all of the funding while it receives a management fee or compensation through some other means that requires little or no risk on its part? The market study and business plan, which should include projected financials for the operation of the proposed business over at least a five year period, are the primary documents from which the tribe can gain this basic information.

A tribe should never do business with any investor that has developed a market study and business plan but is unwilling to share them with the tribe. On the other hand, if the potential business partner has not developed these documents, they may be investing their own capital blindly and without performing their own due diligence. This is the snake oil salesman and the fool who will soon be parted with his own money. Misery may love company, but it will be no comfort to the tribe that its partner also lost money if the tribe invests in a venture that was not properly vetted from the beginning!

When considering potential economic development ventures, tribes should use firms or consultants specializing in business evaluations to work with its in-house staff to provide an impartial evaluation of the business opportunity and an estimate of what the optimal investment should be, including its risk profile and return expectation. Current comps (industry sector comparisons) in the market are also important to study and compare, as are reference checks for the proposed business partners. Any investor with a little bit of knowledge—and a lot of imagination—can cobble together facts and figures that make sense and sound great on the surface, but unsubstantiated claims of high returns and high-paying jobs for tribal members are not substitutes for reliable, well-documented information. It is important to retain professionals who are able to accurately and impartially evaluate the information. It is also wise to utilize professional advisors known and trusted by the tribe, such as intermediaries, business advisors, legal advisors and other professionals familiar with the tribe, to help facilitate and negotiate any necessary loans or to help achieve the best pricing and deal point results when the acquisition of an existing business or the investment and structuring of capital is involved.

A tribe should consider several other factors when performing its due diligence. For example, a tribe must know what role it will play in the management of the proposed venture. An important goal of tribal economic development should be building tribal capacity so that the tribe is increasingly able to create, fund and manage its own businesses and economic ventures. This is only achieved if the tribe has a significant management role in the ventures in which it invests. If a significant management role is not feasible from the outset due to specific and technical industry requirements unique to the business sector, the tribe should require extensive training for its members so the management goal can be achieved after a few years.

In addition, a tribe should possess a clear understanding of what each party brings to the table, especially the outside investor. Does it possess special technical or management expertise, access to capital, or some other valuable asset? Oftentimes, outside investors come to tribes with none of these and yet expect tribes to take most of the risk with little of the reward.

Likewise, a tribe must also understand what it brings to the table so that it can be sure to receive the maximum benefit from the venture. In

many instances, the primary value that a tribe brings to a venture is its sovereignty—it offers an outside investor the opportunity to engage in a business activity unfettered by state or local governmental regulation that would render the business otherwise infeasible. (Although its sovereignty is an intangible asset, it has a quantifiable economic value that should be realized by the tribe just like it would realize the value of a hard or tangible asset). With this in mind, the tribe should be prepared to provide its own oversight and regulation to make sure that the business is conducted in a fair and reputable manner in compliance

with its own regulations (which are typically modeled after federal regulations) and in ways that are not harmful to the environment and human health. Tribal reservations are not bastions of lawlessness, and companies who wish to rely on a tribe's sovereignty should understand that and be prepared to be subject to tribal laws and regulations.

Whatever it is that a particular tribe may bring to the table, every tribe can add a tremendous amount of value to many business ventures,

and all tribes should expect to be dealt with fairly and treated with respect. Tribes must be shrewd negotiators, perform thorough due diligence and insist that they be given value for value. Suitors that are unwilling to provide documentation, answer questions, share in the risks or agree to a significant tribal management role should be shown the door. No deal is better than a bad deal, and it is sometimes necessary to say "no." Nonetheless, there are many good deals to be made if tribes perform the necessary due diligence vetting process. The enormous success of the tribal gaming industry demonstrates that tribes and commercial entities can and should work together for common goals. Diversification into other sectors is wise, and if approached with a thoughtful, diligent process, should offer a tremendous advantage to those tribes that can achieve it.

Whatever the targeted business expansion ... the keys to successful tribal economic development include managing expectations and then choosing the right ventures and the right "partners" with which to do business. ■



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