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May 17, 2014

Shortfalls in Indian Gaming Funds

LEGISLATIVE ANALYST'S OFFICE

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Overview of Gaming in California

☑ ***Number of Tribal-State Gaming Compacts.*** The Legislature has ratified tribal-state gaming compacts with 72 of California's 109 federally recognized tribes. Of these tribes, 58 tribes currently operate 59 casinos.

☑ ***Compacts Requiring Payments From Tribes.*** These compacts require the tribes make payments to various state accounts under certain conditions. Specific payment requirements differ across tribes and depend on various factors, such as the number of machines operated and/or the average slot machine net win (a measure of slot machine revenue). Currently, 46 tribes make payments into the following three state accounts:

- The Revenue Sharing Trust Fund (RSTF) receives payments from 37 tribes.
- The Special Distribution Fund (SDF) receives payments from 25 tribes.
- The General Fund receives payments from 11 tribes.

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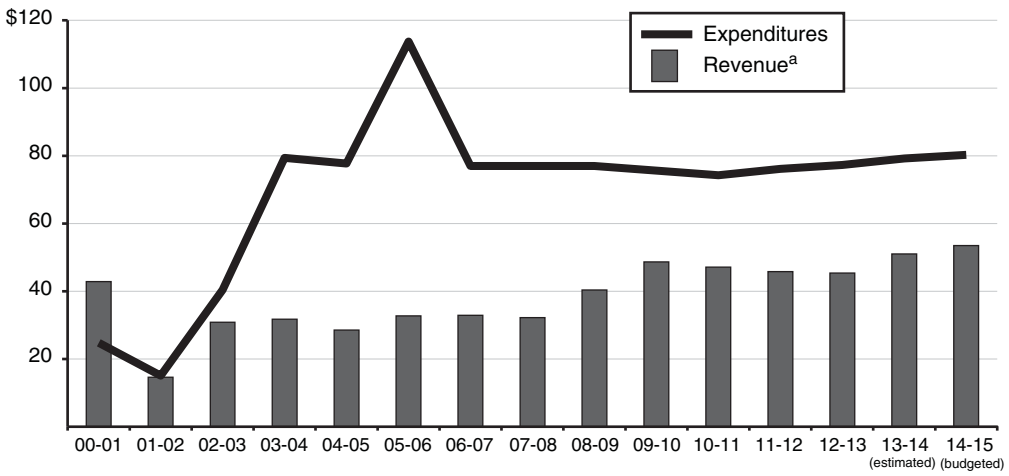
Revenue Sharing Trust Fund

RSTF Shortfalls Annually Since 2001-02

(In Millions)



[a] Excludes SDF transfers required to make up shortfall.
RSTF = Revenue Sharing Trust Fund and SDF = Special Distribution Fund.

☑ ***Use of RSTF Funds.*** Funds deposited into the RSTF are distributed to certain federally recognized Indian tribes that either do not operate casinos or operate casinos with less than 350 slot machines. These tribes generally each receive $1.1 million annually. In 2014-15, 73 tribes are eligible to receive such payments.

☑ ***Annual RSTF Shortfalls Since 2001-02.*** As shown in the figure above, annual RSTF expenditures have routinely exceeded revenues since 2001-02, the year after the fund was first created. In recent years, this shortfall has averaged around $30 million.

☑ ***Addressing RSTF Shortfalls.*** State law requires that these shortfalls be addressed by transferring sufficient funds from the SDF annually to ensure every eligible tribe receives its full $1.1 million payment.

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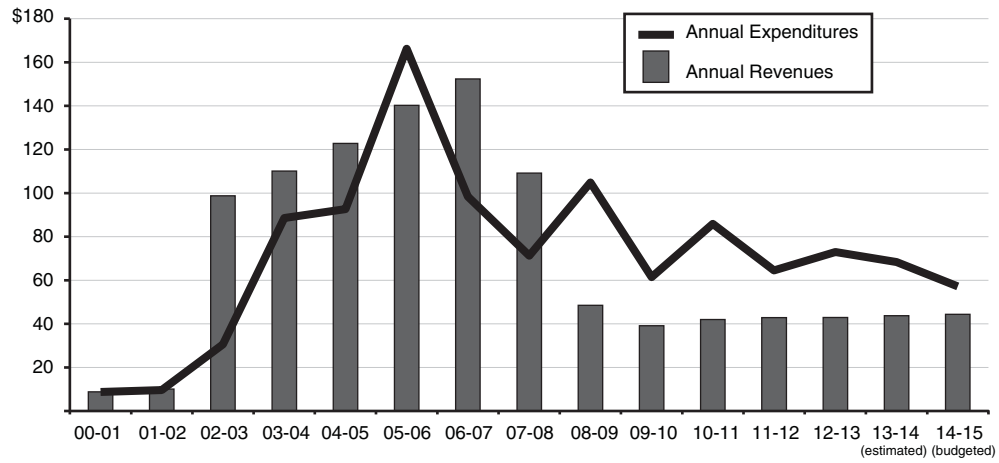
Special Distribution Fund

Annual SDF Expenditures Exceed Revenues in FY 2008-09

(In Millions)



SDF = Special Distribution Fund and FY = fiscal year.

☑ ***Use of SDF Funds.*** Funds deposited into the SDF are prioritized for the following purposes: (1) shortfalls in the RSTF, (2) problem gaming, (3) regulatory costs, and (4) local governments impacted by tribal casinos. Additionally, SDF funds may be used for other gambling purposes specified by law.

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Special Distribution Fund *(Continued)*

☑ ***Redirection of SDF Revenues to the General Fund.*** In 2006, five tribes negotiated amendments to their existing tribal-state compacts. These amended compacts went into effect towards the end of 2007-08 and required payments to the state's General Fund instead of the SDF. (Increased RSTF payments were also required.)

☑ ***Annual SDF Shortfalls Since 2008-09.*** Upon full implementation of the amended compacts in 2008-09, the majority of SDF revenues shifted to the General Fund. As shown above, annual expenditures have exceeded revenues by about $30 million since then. The expenditures in excess of revenues were supported by using prior-year fund balances in the SDF. The SDF fund balance is expected to be exhausted by 2014-15.

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General Fund

- ***Payments to General Fund.*** In 2013-14, the General Fund will receive an estimated $333 million in revenue from tribes.

- ***Redirection of Payments.*** Currently, tribal-state compacts for three tribes—the Morongo Band of Mission Indians, the Pechanga Band of Luiseño Indians, and the San Manuel Band of Mission Indians—require that up to $124.2 million of their General Fund payments be available annually for redirection if the RSTF shortfalls. Specifically, the compacts require the transfer of sufficient funds to ensure that each eligible tribe receives their full $1.1 million annual allocation.

- **Rincon *Decision.*** The Ninth Circuit Court of Appeal decided in the *Rincon Band v. Schwarzenegger* case that the state cannot require tribes to make payments to the General Fund. While the compacts requiring these payments still stand, tribes currently making payments to the General Fund will likely no longer make such payments when their compacts are renegotiated.

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Governor's Proposal to Address Shortfalls

☑ ***Insufficient Funds in the SDF to Address RSTF Shortfall.*** Similar to prior years, the Governor's budget assumes the SDF will transfer funds to address the annual RSTF shortfall. However, because of the steady depletion of the SDF fund balance, the SDF is projected to have insufficient dollars available to fully address the RSTF shortfall as well as all other regulatory and problem gaming costs.

☑ ***Redirection of General Fund Payments to Address RSTF Shortfall.*** To ensure full RSTF payments will be made, the Governor's budget proposes budget bill language authorizing the redirection of tribal General Fund payments to the RSTF. We estimate that this redirection will be approximately $7 million in 2014-15.

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Short-Term Issues for Legislative Consideration

☑ ***Continued General Fund Transfers Likely in the Near Term.*** Due to an ongoing mismatch between revenues and expenditures in the SDF and RSTF, we estimate that annual General Fund transfers to the RSTF will be necessary in the short-run to maintain current levels of regulatory and problem gaming services.

☑ ***Reducing General Fund Transfers Would Require Reduced Expenditures.*** If the Legislature would like to reduce the amount of General Fund redirected to the RSTF, it has limited options in the short term. Specifically, the Legislature would need to reduce SDF expenditures on either problem gaming or regulation—likely impacting the level and quality of these services.

☑ ***Increased Expenditures Require Greater Redirection From General Fund.*** In recent years, there have been requests for additional spending from the SDF. Any additional expenditures from the SDF, such as grants for local mitigation, would result in the need for larger General Fund transfers to the RSTF.

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Long-Term Issues for Legislative Consideration

☑ ***Structural Imbalance and Need for General Fund Transfer May Decrease Over Time.*** With the *Rincon* decision, any new compacts or amendments of existing compacts will likely no longer require General Fund contributions. Instead, these compacts will likely require additional payments to the RSTF and SDF. Depending on the terms of each negotiated compact, this could potentially eliminate the structural imbalances in the SDF and RSTF and the need for General Fund transfers to the RSTF. However, it could take years before such changes take effect.

☑ ***State May Want to Consider Proposing Changes to Payment Structure Included in Compacts.*** The state may want to consider changing the payment structure required in tribal-state compacts to better reflect the state's priorities with respect to payments to non-gaming tribes, regulation, problem gaming, and local mitigation. For example, the state may want to consider:

- Increasing payments to the RSTF to more closely align the fund's revenues and expenditures.
- No longer supporting state gaming regulation costs and problem gaming from the SDF. Instead the state could support these programs by billing gaming tribes to ensure these costs are addressed regardless of the fund condition of the RSTF or SDF.
- Eliminating expenditures for local mitigation grants from the SDF. Instead the state should require tribes to fully address all local costs through memorandums of understanding negotiated with affected local governments.