

INTERNATIONAL BOWLING INDUSTRY

Cat and

mouse



Frank Seninsky

Redemption can pay off the best of all games—provided the two sides in the contract don't play games with each other.

In 2003, the last year for which statistics are available, there were 1.2 million video games in commercial locations across the country. Video games are traditionally—*were* traditionally played by male teenagers. In a bowling center or FEC, these young folks have other ways to spend their money. They are playing computer games at home and group games on the Internet. They no longer spend all of their money in video arcades. That's why I say male teens *were* the traditional customers for video games.

Meanwhile, redemption games have seen constant growth. In 2003, there were 140,000 of them. They are played by everybody *except* male teens. 70-75% of the revenue in commercial game rooms is now generated from redemption games, the rest split between video, novelty, and merchandise dispensing machines. (The last category should not be confused with redemption games, by the way. A redemption game rewards the player with tickets or points stored on a debit card that he exchanges for prizes. A merchandise-dispensing machine pays off with the merchandise itself, for example a crane machine where the player manipulates a claw in order to retrieve the prize.)

The opportunity for

growth in redemption, I believe, is substantial. My company's redemption games in almost every facility are grossing five times as much as the video games. If you are a location (bowling center or FEC) that is considering adding redemption games, you might choose to have them supplied by a vendor (redemption games provider/servicer) experienced in this specialty field. If so, the following are some pointers for what should be included in a redemption games contract.

In the simplest agreement, one party would be responsible for buying the prizes. Since that party's cost of participating in the agreement would be higher (equal to his cost for the prizes), he would take a higher percentage of the gross. Usually, this party would be the vendor. Let's suppose that under the contract, the location is going to receive 35% of the redemption game gross revenue, the vendor receives 35%, and the remaining 30% is retained by the party that purchases the prizes.

This looks like a fair arrangement as long as the cost of the prizes given out (including shipping and any sales taxes) remains very close to 30% of the redemption revenue. After all, the parties want equal shares of the revenue. But what tends to happen due to human nature is that a deadly game of cat and mouse takes place. If the vendor is given the 30% to buy the prizes, he may adjust the games to award fewer tickets overall and pocket the difference between the 30% and the cost of the prizes given out (technically, the redeemed prize percentage, that is, the cost of prizes given out ÷ gross revenue). The location may respond by decreasing the number of tickets required to win the prizes, thereby increasing the value of the prizes given out (the redeemed prize percentage).

On the other hand, if the location owner buys the prizes, he might increase the number of tickets required to win the prizes, so that the prizes will move more slowly off the shelf, and pocket the difference between 30% of the revenue and the cost of the prizes given out. The

vendor, in order to balance the playing field, might then increase the value of the tickets given out by the games (technically, raising the ticket payout percentages).

How can you avoid this situation? One of the parties has to buy the



prizes, and both parties should be smart enough to include guidelines in the agreement to circumvent it. My recommendation is to each week deduct off the top of the gross the cost of the prizes given out, and present it to the party who purchases the prizes. The remaining revenue can then be divided according to the agreed revenue split: Put another way: each week, the cost of replacement redemption prizes is subtracted from the redemption gross and *then* the parties split the remaining proceeds.

With this scenario, if the ticket payout is too low, both parties pay less in prize costs and both parties suffer from the potential loss of redemption game revenue. If the ticket payout is too high, too much merchandise is awarded and both parties share the burden of this additional cost as well as any increases in redemption game revenue. At least in this case, both parties are carefully monitoring the situation. The problem here is that the location could increase the number of tickets required for prizes (above the prize/point formula stated in the agreement) and pocket a percentage of the difference.

In my experience it usually is better for the location to buy the prizes, stock the prize center and be responsible for any prize theft. This helps avoid all-out hostilities between the parties because the vendor has no control over the operation of the redemption prize center if it is staffed by the location's employees. If the location runs a loose operation and light-fingered employees cart off some of the prizes or counter people give their friends a "break" on the tickets required for a certain prize, there will be a shortfall on the location's side. The value of the prizes taken off the shelf will be greater than the value of the tickets redeemed. Asking the vendor to share in a shortfall that is due to the poor business practices of the location—hiring practices, supervision on the job,

and the like—is not a good idea. It's not equitable and it's not good business. The vendor's money could better be spent to purchase additional games for the location and/or hire additional staff to maintain the games to keep revenue as high as possible.

The negotiating of most redemption contracts begins at a 50-50 split between the parties. The vendor says, "I need 50% to give you this much service, so many game rotations, response within 24 hours"—all the things locations want. The location comes to the table and says, "What if you gave me less service and less costly games? What could I do to get more than 50% of the net gross?" In the end, most parties settle where they began: with a 50-50 split.

So much for how the parties should split between themselves, but how should they "split" with the game player? How much in prizes should they pay out to their customers? Suppose a customer spends \$10 and wins prizes that approach \$10 in perceived retail value. He's spent \$10, he's won (about) \$10 (from his point of view), and he's had the fun of playing the games and winning tickets. Suppose the prizes won by this customer cost the location \$2.50

The bowling center should buy the prizes. This will help prevent all-out hostilities.

(wholesale in bulk). This translates to a 25% cost of sales and would be a great win-win for the customer as well as the location and the vendor.

The ratio, or formula, here is 4:1. That is, the retail (perceived value) of the prizes won is four times what they cost the location. We are fortunate that a vast majority of quality merchandise for redemption games can be purchased at 1/4 to 1/3 of its perceived value. Taking in \$1 and awarding 25 cents worth of prizes leaves 75 cents to be split by the location and the vendor. The vendor uses his share to pay for the equipment,

service on the equipment, overhead, and for his share of the cost of tickets, tokens and licenses. This is the Golden Rule of Redemption, and just like the Golden Goose, this rule should never be broken.

In my business, I can take on three different roles. As a consultant, I represent bowling center owners. Or I might negotiate for the bowling center with a game vendor and assist both parties in setting up a profitable game zone, with the bowling center along side me at table. Or I may assist the bowling center in purchasing its own games and make sure that its staff is trained properly to maintain the games. If a client for whom I'm consulting says he wants my company to be his games vendor, and if I'm comfortable that he runs a good business, I change hats and try to put together an agreement that is completely fair to both of us. There is always a part of me that is looking out for him, since I want to continue working both for him and with him for many years to come.

In much the same way, negotiating a redemption contract does not have to create adversaries. You do need to keep your wits about you. And bear in mind this consoling thought: the greedy ones, the people who are not satisfied with a *mutually* satisfactory deal when all the cards are on the table, don't tend to stick around very long. They go out of business. They really do. □

Frank Seninsky is President of Alpha-Omega Group of East Brunswick, New Jersey, a consulting agency and a revenue-sharing equipment provider. He is current President of the International Association for the Leisure and Entertainment Industry (IALEI), a trade organization for FEC owners. He can be reached at (732) 254-3773, fseninsky@aol.com, or www.aemllc.com.



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