

September 2018

FEATURE


Game On

Retailers turn to video gaming to boost in-store profits.

BY JERRY SOVERINSKY

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Business at the suburban truck stop, just 25 minutes from downtown Chicago, is brisk. The nearby interstate hums with activity day and night, with gas-seeking, soda-searching and pizza-craving motorists flocking to the convenience store for snacks, meals and more. Once inside, they flow easily through the pristine aisles and their neatly arranged fixtures displaying chocolates, chips and sundries, many stopping at an impressive fountain lineup to satisfy their thirst or find a caffeinated fix.

A few steps further, just past the coffee station through an open doorway, sits a video gaming room with players lounging comfortably in overstuffed chairs, each gazing intently before a buzzing, whirring and flashing video gaming terminal.

At a time of dwindling store trips (see “Tripped Up” and “Traffic Jam” in the June 2018 issue), thinning margins and falling revenues from traditional convenience store money-makers, it’s understandable that retailers have focused on alternative categories and services to boost sales. And while some are looking to natural extensions of products and services that emphasize convenience—car washes (“Clean Up Hitters” in the April 2018 issue), financial services and dry cleaning (“Pushing the Boundaries” from May 2018)—still others, to the extent permitted in the areas where they operate, are looking to video gaming to generate revenue and boost their bottom line.

Is it the winning ticket for your store? Or just a trendy gamble that detracts from other operational demands? Let’s take a look.

THE STATE OF GAMBLING

Gambling laws vary by state and constitute a patchwork of rules at the state and municipal levels that single out particular games, player restrictions, venues and the entities that implement and oversee them. Video gaming currently is permitted in nine states—eight where cash prizes are offered (Montana, Illinois, Louisiana, Pennsylvania, Nevada, Oregon, South Dakota,

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West Virginia), and one (Georgia) where non-cash payouts are given. And there are bills to introduce gaming that are making their way through the legislatures in three other states—Missouri, Indiana and Mississippi.

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Video gaming is currently permitted in nine states—eight where cash prizes are offered and one where non-cash payouts are given.

In some states, video gaming is run by the state lottery, while other states license private companies to operate the machines. Within a state, laws are not necessarily uniform; for instance, in Illinois, while video gaming is permitted at truck stops (those that pump at least 10,000 gallons of diesel a month, operate a convenience store and sit on at least three acres), cities and municipalities can prohibit them.

If you're asking yourself, "With all of these disparate laws, both among states and within them, why pursue an offering that requires such individualized attention?" The answer lies in the modest operational investment versus the potential payouts.

"Once you learn what the customer wants, it's plug-and-play," said Randy Meyer, president of Teutopolis, Illinois-based Meyer Oil Co., which operates 21 Mach 1 convenience stores in Illinois and Indiana. According to data provided by the Illinois Gaming Board website, operating five machines (the maximum allotment in Illinois) at a Teutopolis store, Meyer's company earned more than \$58,000 in the first six months of 2018. That's net income—his company's share after divvying up revenue with the state and his terminal operator.

"We were skeptical at first about the profitability," said Meyer, who was approached by a terminal operator shortly after Illinois legalized video gaming. "We were hesitant because we assumed it would add marginal additional income. That certainly wasn't the case."

At a minimum, Illinois requires that video gaming rooms be separated from the rest of the convenience store by ropes (think movie theater ropes), but Meyer decided to enhance the offering. "We built a separate room for the gaming; it's a substantial investment in our stores and we make them nice, adding restrooms. It's very comfortable and keeps the gamers in their own space," he said.

And with federal laws mandating a maximum 14-hour shift in which to drive 11 hours, drivers spending multiple days on the road need their space—and something to do. "They get bored," said a convenience store clerk in Pennsylvania to *The Daily Item*, in predicting the impact of video gaming on truck stops after Pennsylvania legalized the activity last fall. "I've seen some people play these non-lottery games for hours. I believe they'd welcome another diversion. It would be a good way to pass the time."

The Pennsylvania law, which allows truck stops to add as many as five video gaming terminals, began accepting applications in January. In response, Rutter's (with nearly 70 stores, based out of York, Pennsylvania) has been actively planning to retrofit existing stores that meet Pennsylvania's criteria

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(those that pump at least 50,000 gallons of diesel a month, offer parking for at least 20 trucks and sit on at least three acres), capitalizing on their larger store sizes, according to *Global Convenience Store Focus*.

“The bigger footprint has allowed us to grow from a deli to a restaurant, and we are not done yet,” said Scott Hartman, Rutter’s CEO and president. “Gaming has also been enabled by the bigger footprint.” And citing the success of gaming in Illinois, Hartman said the opportunity could also tap new customers. “There’s been a higher skew toward female than you would have expected. We love that—it’s new customers and a new revenue stream.”

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SAMPLE STRUCTURE: ILLINOIS

While each state that allows gambling can pursue its own implementation scheme, Illinois operates on a three-tier system. “There’s the game manufacturer, the terminal operator and the retailer,” said Bob Willenborg, managing member at J&J Ventures, a terminal operator (TO). “As the terminal operator, we own, operate and service the machines,” a hands-on process that minimizes the labor burden for convenience store operators.

“The terminal operator installs the machines, maintains them, removes the cash,” Meyer said, reemphasizing the plug-and-play aspect of the offering. “A payout machine reads the [play] slip and gives them money ... We get paid electronically, and there’s no reconciling on our end. The information is communicated to the state in real time.”

Out of the net income per terminal in Illinois, 30% goes to the state, 35% goes to the retailer and 35% goes to the TO. The process nets each retailer in Illinois \$70-\$140 per terminal per day, according to Willenborg, with the most profitable terminals generating more than \$200 per day. He said this payout sets video gaming apart from all other convenience store offerings: “Nothing makes more money per square foot than a video gaming terminal.”

With so much money at stake, there are of course numerous regulations, a state-by-state learning curve that’s best acquired with the help of legal assistance, said Willenborg. For instance, there are penalties for underage participation (Illinois has a minimum age of 21), which make compliance every bit as critical as for alcohol and tobacco sales. As such, Meyer is vigilant at his stores. “We take the monitoring of age very seriously, and we sting each of our gaming rooms at least twice a month,” he said, sending in people close to 21 (but just older) to play the video games and report back whether their ID was verified by store personnel.

GEORGIA PEACH

A WINNING STRATEGY

To maximize returns on your video gaming offering, Illinois-based J&J Ventures, a terminal operator that specializes in working with the convenience store industry, offers the following best practices:

- **Shhh:** Privacy and discretion are key for maximum play. Private rooms, segregated rooms and half walls are optimal to create privacy for your video gamers.

While Georgia's video gaming system operates on a similar three-tier structure as Illinois, it differs in one important respect: There are no cash prizes, as all winnings must be spent in the store where you win them (you cannot spend the winnings on alcohol, tobacco or firearms). "Retailers can have up to nine games per location," said Angela Holland, president of the Georgia Association of Convenience Stores, "with each retailer earning about \$89 per day per machine ... Done properly, store owners are making decent money."

"The games help increase traffic flow inside the store, which is especially important with pay-at-the-pump," said Shawn Fellows, president of Georgia-based Diamond Amusements Inc. "And unlike in Illinois, where there is an age restriction, in Georgia, these are considered amusement games, so there is no age restriction and the machines are not in separate spaces. They're in plain view in the retail environment."

Startup costs are minimal, Fellows said, with the usage fee per device just \$125 per year. And many machines leverage loyalty technology, with winnings accumulated on a card. "This simplifies the process for players, while making things transparent for the retailer and state."

Fellows agrees with the \$85-per-day retailer take per machine, but he clarifies that the figure is before it gets split with the state and the TO. "It comes down to about \$35 per day per machine as profit, but keep in mind, there is also profit associated with the redemption of the winnings [on merchandise or fuel]."

As in Illinois, Georgia TOs assume nearly all labor associated with the machines, making video gaming an appealing profit-maker for a piece of equipment that takes up roughly two square feet of space. And while Holland has seen little to be concerned with regarding video gaming, she said a small percentage of retailers have offered cash payouts, in violation of state law. "That's a challenge," she said. "It's illegal to do that and they're risking asset forfeiture."

SPORTING CHANCE

Beyond video gaming, there is perhaps an emerging gaming opportunity for convenience stores, thanks to a U.S. Supreme Court ruling in May. In *Murphy v. National Collegiate Athletic Assn.*, the Supreme Court, in a 6-3 opinion, ruled that the Professional and Amateur Sports Protection Act of 1992, which (with some exceptions) banned state-sponsored sports betting throughout the United States, was unconstitutional. "Congress can regulate sports gambling directly, but if it elects not to do so, each state is free to act on its own," wrote Justice Alito in the majority opinion. As a result, states are permitted to legalize sports betting, something that many states already are actively pursuing, and which likely will affect sales of a staple c-store offering.

- **Comp, comp and comp:** Provide your gamers free nonalcoholic beverages and food specials.
- **A matter of time:** Adjust hours of operation to open mornings to capture early gamers. Open Sundays when possible.
- **Focus on fundamentals:** Keep restrooms clean, and preferably plan to create your gaming area close by.
- **Set the mood:** Modify lighting in the video gaming area to be well lit, but not necessarily bright.
- **Service with a smile:** Employ engaged and friendly staff to accommodate your video players.

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“Should a state legalize sports betting, that could hurt the lotteries,” said Lyle Beckwith, senior vice president of government relations for NACS. “But that’s also an opportunity. If c-stores have been selling lottery tickets for years, as that market dries up, why not have a sports betting kiosk? A machine that you can bet on. As states get into legalized sports betting, c-stores could play a role in that. They would fit right into that niche. I really think that’s where the opportunity is.” Beckwith said the topic is one that NACS is “looking into.”

CROSS SELLING, UPSELLING AND MORE

While increasing trip frequency and basket size are ongoing concerns for retailers, adding gaming may boost the former but

not necessarily the latter. “We’ve found that the gaming customer is not really a store customer, at least at that time,” Meyer said. “They come to game and they don’t want to be bothered. That’s their pastime. They play for a period of time, and they take their winnings and leave.”

At the same time, he adds, “It’s been a good thing for our company.”

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BY CHRIS BLASINSKY

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