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The Golden Age of Free Play

By **Andrew Klebanow** *Mon, Feb 27, 2012*



The hidden benefits and advantage of a powerful slot promotion



A considerable amount of debate has occurred over the costs of free slot play, how to account for it, measuring its impact on profitability, calculating its effect on slot hold and other metrics. What has not been explored are the hidden benefits of free slot play.

Indeed, free slot play can have a profound and positive impact on customer satisfaction, the casino's profit and loss statement and even the privilege taxes the casino pays on gaming revenue. The industry may in fact be in the midst of a golden age of free play—an age that may soon vanish. Until that time, customers, casino leadership and even the gaming organization's chief financial officer can enjoy free play's hidden benefits.

Up until recently, free play has been used as a replacement for direct mail offers and bonus point redemption: Slot club points that were previously redeemed for cash rebates (cash back) have largely been replaced with points redeemable for free play. The advantage to the casino operator is that cash rebates that once appeared as an expense on the income statement have disappeared. Accounting managers record free play in a contra revenue account, but since free play is not a cash expense, it no longer makes it to the income statement. The net result to the casino is a modest increase in net income.

Customers, however, have not benefited from this conversion. They no longer have the option of redeeming their points for cash and taking it home with them. At the very least, they must cycle their free play through a slot machine and then redeem whatever drops to the win meter for cash.

The Benefits to Customer

Recently, casinos have begun to offer free play in promotional drawings in lieu of merchandise such as cars, boats and motorcycles. Traditionally, casinos would offer a cash option in lieu of merchandise, but at a discount. More often than not, customers will take the cash, since they are responsible for paying income tax on the value of the prize, or they have no use for that particular prize.

With free play, the casino now can offer a third option: \$30,000 in free play, which the customer can download from his account, at his leisure. The casino may impose certain restrictions (for instance, maximum amount that can be downloaded in a day, an expiration date or like cash, offer it at some discount), but let's assume the casino offers the free play without restrictions and at the same face value as the car.

Assuming a tax liability of 30 percent, if the customer chooses the car, his liability would be \$9,000. If the winner takes the cash option, the tax liability would be \$6,750. However, if the player selects the free play, the tax liability would be nothing.

Unlike a car, free play cannot be transferred to someone else. It essentially has no monetary value. Free play by definition, is simply something that initiates a handle pull. That handle pull may or may not generate a winning outcome. Just like bonus points that are redeemed for free play, there is currently no tax consequence for receiving that free play. If the free play is wagered and generates a winning outcome of \$1,200 or more, it will trigger a taxable event. However, it is possible that the customer could cycle through the free play without generating a taxable event, in which case whatever winnings do occur will drop to the win meter, which the customer can then cash out. Alternatively, it is possible, albeit slim, that the free play does not generate any winnings at all, in which case there is nothing to cash out. To the gambler who visits the casino with any degree of frequency, the free play option is the best alternative.

Benefits to Property Leadership

The free play option also offers benefits to property leadership. Assume that every month a casino has a drawing for some expensive piece of merchandise, a fairly common occurrence. This merchandise may be comprised of a car, a motorcycle, a recreational vehicle or a boat. It may also be a vacation cruise or a trip to some exotic destination. On occasion casinos have even been known to give away a house or condominium in a promotional drawing. In each of those occurrences, the casino generates a marketing expense that it must pay cash for and that ultimately appears on the income statement. If the average monthly prize is \$30,000, a fairly low expense for many casinos, the annual expense for prizes and awards will be \$360,000.

If each month the casino offers the winner \$30,000 in free play as an option and each month the customer accepts that option, the decrease to marketing expense and offsetting increase to net income will be \$360,000.

Benefits to Corporate Leadership

For years, casino operators in many jurisdictions bemoaned the fact that they had to pay privilege taxes to the state on the money they gave customers as an incentive to return. With free play, the casino does not have that tax liability.

The Future of Free Play

Until federal and state tax authorities re-evaluate their positions on free play and until outside accounting firms reach a consensus on how to address free play in all its permutations on the income statement, customers, casino operators and corporate leadership can enjoy this golden age of free play. However, like all golden ages, they eventually come to an end. Enjoy the moment.

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