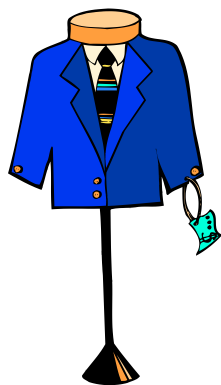


## Topic 6: Understand and work out the true cost of spending

After completing this topic, you will be able to:

- understand the term 'value for money';
- understand discounts and special offers;
- understand why some products are more expensive than other similar ones;
- understand taxes and hidden charges; and
- work out the true cost of spending.

### Cost of purchases



Everything that we buy has a cost. In the UK, most items have a price label and we expect to pay the price stated. There are some purchases for which we expect not to have to pay the price on the label – that is, we expect to negotiate. This will reduce the cost.

We can buy both goods and services:

- **goods** are things that we can physically hold, such as a CD, DVD, mobile phone, or clothes;
- **services** are items for which we pay that help us, such as a mobile phone network, a current account, or a haircut.

We usually have a good idea how much these things are going to cost through experience. For example, we know that a haircut is likely to be less than £50 and we know that a CD can range from a couple of pounds to over £20. We also learn through experience that the cost of things like clothes can vary enormously: for example, jeans can cost anywhere between £10 and £300 – or even more.



### Activity 6a

*Discuss the type of goods for which you would expect to negotiate on price.*

- *How easy is it to negotiate?*
- *Are there other countries that you may have visited where it is usual to 'haggle' over the price?*

## Value for money

'Value for money' means that we feel we have paid a fair price for the product that we have bought. It does not necessarily mean that we have bought the cheapest, because the cheapest could be the poorest quality and the item might fall apart. Value for money means that we thought that what we got was worth the money that we paid.

Value for money means different things to different people. Some people are happy to compromise on quality to get an item more cheaply; others prefer to pay more for a better quality product, but may still consider that product to be value for money.



### Activity 6b

**Discuss some recent things that you have bought.**

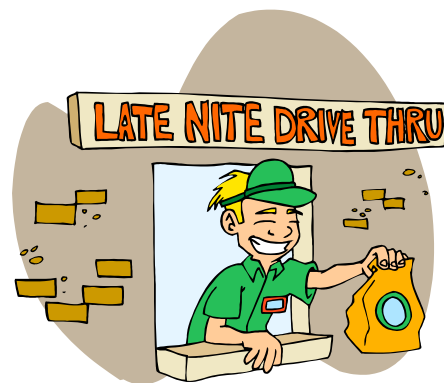
- **Did you think that they were value for money?**
- **What helps you to judge whether the price that you have paid is value for money?**



### Case study

If you were to buy a big box of food from a fast-food outlet, including drinks, for £10 and it would feed a whole family of four, would this be good value for money?

- The answer would be 'yes' if it were to be good-quality, tasty food, with plenty for everyone.
- The answer would be 'no' if it were to be poor quality, not enough, or taste horrible. Then you would feel that you had wasted your £10, because you might have to eat again when you got home.



You also have to ask yourself whether you could all have eaten for £10 by staying at home instead. And you have to take into account whether you enjoyed the experience of eating out and had a good time.

## Price comparison

When we are looking for clothes, we might visit several shops and look at the prices in each. We are *comparing* prices. In this case, however, we may not be comparing exactly the same product.

If we are choosing a DVD of a particular film, however, then we can visit all of the DVD shops and compare the prices. It might take a bit of time, but you will feel sure that you have got value for money when you make your purchase.

But if you had to spend money on bus fares or petrol to be able to visit all of these shops, you have to take this cost into account when deciding which is the cheapest.



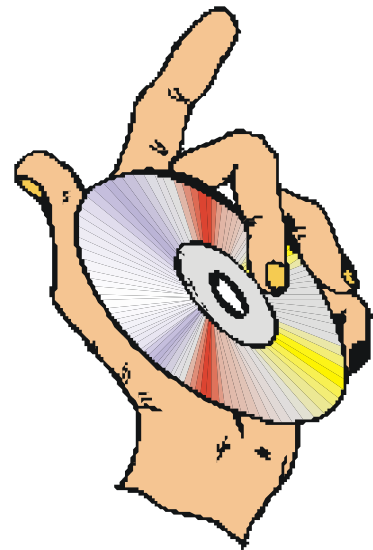
### Case study

It is your friend's birthday and she wants a particular CD as a present from you. The CD that she wants is £12.99 in the local music store. You are sure that you saw it for £10.99 in the out-of-town supermarket, but the bus fare to get there and back is £3.

So, by going to the out-of-town supermarket, the CD will cost you:

$$£10.99 + £3 = £13.99$$

It will be cheaper for you to buy it in the local music store.



## Price comparison websites

Price comparison websites take away all of the walking around between shops, because they will collect prices from other websites and let you have a summary of the best ones. Price comparison sites can be used for goods and services, although you will be more familiar with those for financial services through their television advertising.



### Activity 6c

See how many price comparison sites you can name.

**Use an internet search engine to find products such as ‘mobile phones’ or ‘sports clothes’, or ‘books’, or a new stereo system, and see how many more comparison sites are named as ‘sponsored links’.**

**Once you have your list, visit <http://www.pricerunner.co.uk/> and [www.kelkoo.co.uk](http://www.kelkoo.co.uk) to see how many price comparison sites there are. Visit a few of which you may not have heard.**

Price comparison sites help you to find a good price for something – but not all providers of a good or service are actually on the sites, so you may not always get the best price or see every product that is available.

Comparison websites make their money in a number of ways, one of which is from sponsored listings. This means that companies pay to have their products appear at the top of search results. The websites must make it clear that these listings are paid for and not always the ‘best buys’.

## Making sure that we pay the best price

### Shopping around

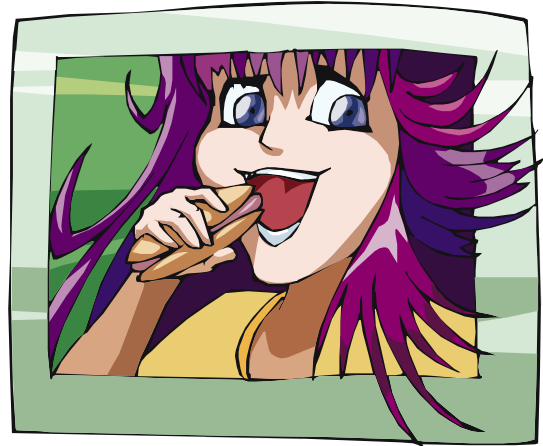
One way in which to get the best value for money is to shop around. This means that you have to do a bit of research before buying something. The more expensive a product, the more worthwhile it is to shop around, because you might save a lot of money.



#### Case study

If you want to buy a sandwich for lunch from a local shop, you might not mind spending 10p more in one shop than another for the same quality of sandwich – although, even here, you will save 50p a week if you buy the cheaper one.

If you are saving up to buy a new mobile phone, however, you might be able to save quite a lot by getting some information beforehand.



### Shop discounts and offers

There are other good ways of getting things for a lower price.

- **Discounts**

A discount means that the seller takes off a percentage of the price. This might be because you have bought a lot or because you are a good, regular customer.



#### Case study

What does '10% off' mean?

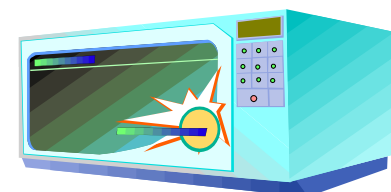
It means that the shop or retailer is knocking off 10 per cent of the normal price to attract more customers.

So, if the usual price for a microwave oven is £150 and the shop has a '10% off all items in the shop today' offer, this means that the discount will be:

$$10\% \times £150 = £15$$

The microwave oven will cost:

$$£150 - £15 = £135$$





### Activity 6d

A supermarket is offering 20 per cent off all fizzy drinks. Calculate the price that you would have to pay for the following.

a) Cola (normal price £1.25 for a 2 litre bottle)

b) Lemonade (normal price £1.50 for six cans)

c) Orange (normal price 85p for a 1.5 litre bottle)

- **Bulk-buy discount**

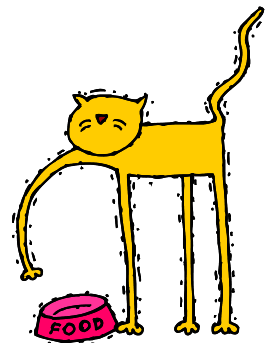
A bulk-buy discount means that the product is cheaper if you buy more of it.



### Case study

One tin of cat food might be 30p. But if you were to buy a box of 12 tins, the price might be £3, instead of £3.60. By buying 12 instead of only one, you save 60p or, looking at it another way, each tin costs only:

$$£3 \div 12 = 25p$$



Bulk-buy discount is often given to regular customers who buy lots of a particular item because the seller wants to keep their business.

- **Special offers**

A special offer might apply if you buy several items at the same time. Some bookshops, for example, offer 'three for the price of two' on older stock (books that they have had in store for a long time and that they want to clear). Some offers say 'buy one get one free' (BOGOF).



### Case study

You want to buy three books, the prices of which are £13, £8 and £6. If the shop is offering 'three for the price of two', you will pay only for two of them – the two most expensive ones. The cheapest book – the £6 book – will be free.

You would pay a total of:

$$£13 + £8 = £21$$

The average price per book would then be:

$$£21 \div 3 = £7$$



### Case study

'Buy one get one free' offers really mean that the item is half-price. For example, one can of deodorant might be £1.28. If you are able to buy one and get one free, this means that you get two cans for £1.28, with each can costing:

$$£1.28 \div 2 = 64\text{p}$$



- **Collect 'money-off' coupons**

You might collect coupons from leaflets, newspapers and supermarkets. For example, you might get a leaflet through the door giving you £1.50 off a box of washing powder. You can take this to most shops and supermarkets, and they will give you this discount. Sometimes, these offers are made by one particular shop, in which case you get the discount only if you buy the item there. Others are vouchers that you can take to any shop – the shop owner claims the £1.50 from the manufacturer of the product.

- **Loyalty cards**

A lot of stores have their own loyalty cards that give you points on everything you buy. You can use these points to get discounts off your bill or you can exchange them for free gifts.

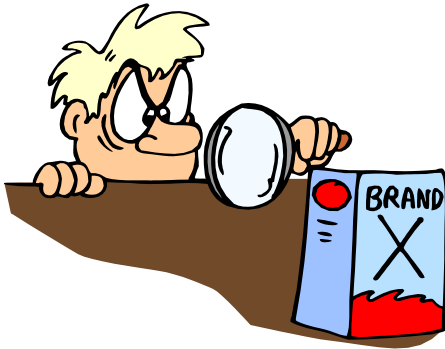
For example, Nectar is a loyalty card that has links with Sainsbury's, Argos and American Express. You collect points and you can get money off holidays, and other goods and services.

- **Free gifts**

A lot of catalogues offer free gifts when you place an order for more than a certain value. The gift might be just what you want and this will reduce the price of what you buy – but make sure that you do want the items that you order and the gift.



## Buying the label



When we buy certain items, we are given a wide variety of choices, some of which are more expensive than others. Everything has a label, or a name, telling you which manufacturer made it or which shop sold it. Certain labels are better known than others, either because the manufacturer or retailer is a bigger, better-known company, or because it has a reputation for making or selling good-quality items or items that are more desirable (more fashionable).

You will nearly always pay extra for a well-known name or label, and these items are not always good value for money – but you are not looking only at the price. You are also looking at how long the item will last and how well it does the job for which it is designed. You should also consider how having that item will make you feel: sometimes, it feels good to treat yourself and buy something that you really want, and that other people will admire.



### Activity 6e

**Complete the table to show whether you think the following items represent value for money and what you think you are paying for in each case.**

Item	Value for money? (Y/N)	What you are paying for
Pair of Armani jeans		
A Rolex watch		
Coffee and a croissant in a trendy coffee bar beside the Thames in London		
An Apple Mac laptop		
A Thornton's Easter Egg		
Cristal Champagne		



## Opportunity cost

Sometimes, you have to give up one thing to get another and, when it comes to spending money, you have to work out whether the cost of that item is worth what you have to give up to get it.



***You have planned to go out this evening, but you have just been offered an extra shift at work that will earn you £25. What do you do?***



### Activity 6f

***You have been given £50 as a birthday present and cannot decide how to spend it. The choice is a new pair of trousers (you are going to a party next weekend and want to look good) or a thick winter jacket (it is getting a bit cold standing at the bus stop).***

***What are the opportunity costs of each option?***

## Taxes on spending

In the UK, as in most other countries, the government charges a tax on the goods and services that we buy, so that they cost more. In other words, when we buy a product that has been taxed, we pay the seller's price plus the tax.

### Value added tax (VAT)

The main expenditure tax in the UK is value added tax (VAT). VAT is charged on most goods and services.

There are three main rates of VAT, as follows.

- **Standard rate (20 per cent)**

This is the rate on the majority of goods and services that we buy, from clothes, to electrical equipment, to personal services such as hairdressing or plumbing.

- **Reduced rate (5 per cent)**

This is the rate charged on domestic fuel (gas, electricity, etc).

- **Zero rate (0 per cent)**

This is the rate charged on a range of products considered to be necessities, such as food, children's clothes and children's shoes, books, newspapers and magazines. We call these types of product 'zero-rated'.



The reason that the government charges VAT is not to discourage us from spending, but to raise money to finance the many public services that it has to provide. The government feels that there is a limit to the amount of tax that it can raise by means of income tax and National Insurance contributions (NICs), and this is another way in which it can raise money.

### Calculating VAT

#### Case study

There is a burst pipe in your house and a plumber comes round to fix it. Her bill is £136 plus VAT, which is calculated as:

$$20\% \times £136 = £27.20$$

The total bill to pay is:

$$£136.00 + £27.20 = £163.20$$



You will give this money to the plumber, who keeps the £136 for herself and passes the £27.20 to the government.



## Case study

Mrs Jones has just received her electricity bill. The total charge for the electricity that she used over the last three months is £160 plus VAT.

Remembering that VAT on domestic fuel is 5 per cent, rather than 20 per cent, the VAT is calculated as:

$$5\% \times £160 = £8$$

The total bill to pay is:

$$£160 + £8 = £168$$

The electricity company will pass the £8 to the government.

## Duties

Some items, such as petrol, cigarettes and alcohol, are subject to another type of government tax called 'duty'. The reason that the government charges duty on these items is to discourage us from buying them, or to make them so expensive that we buy less of them.



**Why do you think that the government wants us to buy less petrol, fewer cigarettes and less alcohol?**

**Did you know?**

Just over two-thirds of the price that people pay on petrol goes in tax to the government. Look at the following breakdown of the price of 1 litre of petrol at 112p to see where the money paid goes.

	<b>Pence</b>
Production cost and profit and retailer profit	30.43
Retailer's profit	5.00
VAT	18.62
Petrol duty	57.95
	<b>112</b>



## Insurance premium tax (IPT)

When people buy insurance (for their house, car, pet or holiday), they pay a 'premium'. This is the amount that they pay to the insurance company to cover the risk of theft, fire, illness, lost luggage, etc. The government charges a tax on this premium called insurance premium tax (IPT).

For most types of insurance policy, IPT adds 10 per cent to the premium cost.



### Case study

Samina's car insurance premium is £220 per year. The insurance premium tax is 10 per cent:

$$10\% \times £220 = £22$$

So her total premium is:

$$£220 + £22 = £242$$



### Did you know?

IPT on travel insurance is charged at 20 per cent.

## Hidden charges

If you are shopping online or over the telephone, the price that you see on the label is sometimes not the total cost of your goods. Before you confirm your order, you need to know the costs that you may have to pay. You should look carefully at the total price, because an item may not be the bargain that it seems to be.

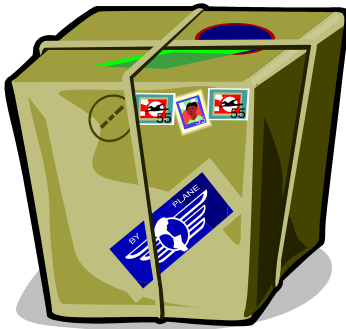


### Activity 6g

*Discuss any purchases that you have made by telephone, online, or through catalogues.*

***Were there any extra charges and were you surprised by the total cost?***

These types of charge usually include booking fees and postage. Sometimes, if you buy something from abroad, you have to pay customs charges (that is, an import duty). This is because the item has been shipped from the foreign country, so no UK VAT has been added to the price.



## Postage and packing

If you are buying goods over the phone, by mail order or online, rather than in the shops, the items that you buy will have to be posted to your house. This costs money, so you need to check with the retailer if this is included in the total price quoted or if you have to pay extra.

Some companies do not charge at all. If they do not do so, it is likely that they will make this very clear on their home pages, because it will be one of their main selling points.

Companies that do add a delivery cost to your order can charge per item, per delivery or both. The actual amount that is added depends on the size of the item: delivery for a couple of paperbacks, for example, probably will not be as much as it is for a new laptop.

## Booking fees

If you are buying tickets for a gig or cinema tickets over the phone or the internet, you will often have a booking fee added to your bill. Booking fees pay for general administration costs, such as issuing and posting out tickets, and the cost of running a computerised system.

Booking fee costs often vary, depending on what you are buying and from where you are buying it. For example, if you are buying tickets directly from the cinema, the booking fee is usually less than £1. But if you are buying tickets for an international sporting match or a sell-out concert, they are often issued through a ticket agency that charges extra for its services. Do not be surprised if you are charged £5 or more per person when you are going to see a really top event.



When you are confirming your payment, make sure that you ask or find out how much the booking charge is per ticket. '£2 or £3 per ticket' may not sound like a lot – but if you are buying gig tickets for yourself and a group of mates, an extra £20 on top of what you were expecting to pay can come as a shock.

## Service charges

Many restaurants – particularly expensive ones – will add a 'service charge' to the bill, which is typically around 10–15 per cent of the value of the bill. This money is meant to be for the benefit of the waiters and waitresses, but is sometimes not paid directly to them.

If a restaurant decides that it is going to charge for service, this must be clearly stated before the diners get to their table – outside the restaurant or just inside the door – as well as on the menu. If diners have been properly warned in advance of this charge, they have to pay it, unless the service is very poor, in which case they can refuse. Diners who are not charged a service charge will often leave a ‘tip’ for their waiter or waitress if the service has been good.

## Online shopping

The main risk of shopping online is that you cannot see what it is that you are buying before you get it. If the item does not fit, or you do not like the colour, or it is bad quality, or damaged, you will have to send it back.



This also applies to things that you might buy out of a catalogue.

So, as well as checking if there is a charge for posting the item to you in the first instance, you will also need to check who pays the postage if the item has to be returned. Some companies will send you an address label to stick to your parcel if you want to return the item, but you should check if they will also pay for the postage on returns, or if this has to come out of your pocket.

Buying online can save you a lot of money – but not if your saving is swallowed up in postage fees and returns fees.



### Activity 6h

*Amazon's returns policy reads as follows:*

If you return an item/s to us using a pre-paid, personalised return label and the reason for the return is not because of an error on our part or because the item is defective, **we will deduct the cost of return postage from your refund.** We will not deduct the cost of return postage for shoes from customers within the UK.

**a) When will Amazon refund the postage?**

**b) Why does Amazon not charge for the return of shoes?**



### **Activity 6i**

***Discuss the types of item that you buy online.***

- ***Is there a risk of having to return them?***
- ***What sort of clothes or shoes might you buy online?***





## Review questions

1. Name three items that are zero-rated in terms of VAT.
2.
  - a. An item costs £30 before VAT. Calculate the VAT payable at 20 per cent and the total price.
  - b. An item costs £56 before VAT. Calculate the VAT payable at 20 per cent and the total price.
  - c. You are intending to buy computer game online. The price is £39.95. The website tells you that postage and packing is £3.80. What is the total cost?
  - d. You are planning to buy four tickets for a gig. The price is £36 for each ticket. The website tells you that there is a booking fee of £5 for each ticket. What is the total price for all four tickets?
3. What does 'VAT' stand for?
4. What does 'IPT' stand for?
5. Why do you think price comparison websites have to advertise on television?
6. The advantage of buying in bulk is that you save money – but what can be a disadvantage of buying in bulk?

## Learning activities



### Internet

- Visit [www.ryanair.com](http://www.ryanair.com) and find out how much it would cost you and your family to book a return flight between Birmingham and Lanzarote during your next half-term. The fare will differ according to the day and time. What is the cheapest price that you can find? Are there any hidden charges?
- Visit the website of an online seller such as [www.amazon.co.uk](http://www.amazon.co.uk), select an item and find out how much is charged for delivery. Look at the different rates for speed of delivery. Is this a hidden charge?



### Group

Select some products and look at different price comparison sites. Do they give the same advice?



### Individual

Visit some restaurants and find out whether they impose a service charge. This will be clearly stated on the menu, usually at the bottom of each page. Make a list of the restaurants that you visited that do charge for service and whether you were able to find a warning about this charge displayed somewhere near the entrance to the restaurant.



## Key points for Topic 6

You should now understand:

- what is the cost of a purchase;
- what is value for money and three things that help us to decide whether something is value for money;
- what 'shopping around' is and three advantages of shopping around, including discounts, special offers and buying in bulk;
- what 'price comparison websites' are, and some advantages and disadvantages of them;
- what is meant by 'buying the label', and an advantage and a disadvantage of doing so;
- what is meant by 'opportunity cost';
- three taxes on spending;
- why you should be aware of hidden costs and be able to give examples;
- the risks involved in online shopping;
- how to work out the VAT payable on an item;
- how to work out the postage and packing costs of an item;
- how to work out the effect of booking fees on the cost of a ticket.