February 2017

社会经济研究中心

SOCIO-ECONOMIC RESEARCH CENTRE

Understanding the "Price Control and Anti-Profiteering (Mechanism to Determine Unreasonably High Profit for Goods) Regulations 2016"

SERC

AGENDA

- Background
- Comparison between the new and previous mechanisms
- Mechanism to determine “unreasonably high profit”
- SERC’s comments and recommendations
- Appendix: Exceptional scenarios and illustrations

BACKGROUND

- The Price Control and Anti-Profiteering (“PCAP”) Act 2011 was gazetted to protect consumers against making unreasonably high profit (profiteering) on goods and services by businesses. The PCAP Regulations 2014 specified a time frame (2 Jan 2015 – 30 June 2016), which was subsequently extended to 31 December 2016, in which businesses must not increase their net profit margin.
- On 22 December 2016, the Ministry of Domestic Trade, Co-operatives and Consumerism (KPDNKK) gazetted a new regulation -- PCAP Regulations 2016, which came into effect on 1 January 2017. This regulation has no expiry date, meaning that it shall be enforced until being repealed.

27 Jan 2011
PCAP
Act 2011

24 Jul 2014
PCAP
(Amendment)
Act 2014

26 Dec 2014
PCAP
Regulations
2014

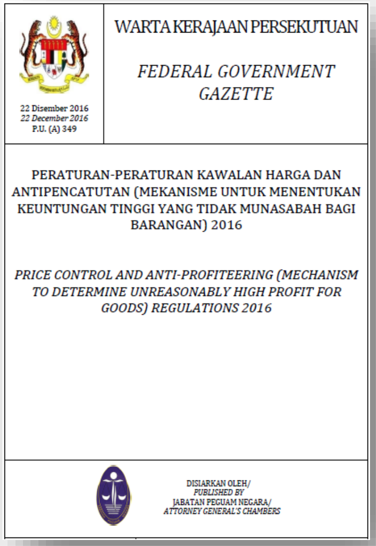
w.e.f.
2 Jan 2015 to
30 Jun 2016

24 Jun 2016
PCAP
(Amendment)
Regulations
2014

w.e.f.
1 Jul 2016 to
31 Dec 2016

22 Dec 2016
PCAP
Regulations
2016

w.e.f.
1 Jan 2017


WARTA KERAJAAN PERSEKUTUAN

FEDERAL GOVERNMENT GAZETTE

22 Disember 2016
22 December 2016
P.U. (A) 349

PERATURAN-PERATURAN KAWALAN HARGA DAN ANTIPENCATUTAN (MEKANISME UNTUK MENENTUKAN KEUNTUNGAN TINGGI YANG TIDAK MUNASABAH BAGI BARANGAN) 2016

PRICE CONTROL AND ANTI-PROFITEERING (MECHANISM TO DETERMINE UNREASONABLY HIGH PROFIT FOR GOODS) REGULATIONS 2016

DISIARKAN OLEH/
PUBLISHED BY
JABATAN PEGUAM NEGARA/
ATTORNEY GENERAL'S CHAMBERS

COMPARISON BETWEEN THE NEW & PREVIOUS MECHANISMS

- The PCAP Regulations 2016 has narrower coverage compared to the previous PCAP Regulations 2014, i.e. only applicable to two classes of goods:
  1. **Food and beverages** – entire supply chain on food or drink for human consumption, including the ingredients; and
  2. **Household goods** – non-durable household goods and personal care products, excluding cosmetic products

No	Previous Mechanism (PCAP 2014)	New Mechanism (PCAP 2016)
1.	Formula is based on Net Profit Margin (NPM) in Ringgit term	Formula is based on **Mark-up (MU) or Margin (MG)** stated in **percentage (%)**
2.	NPM cannot be increased for a duration of 24 months	**MU% or MG% can be increased** every first day of the year (Financial year, FY or Calendar Year, CY) within the allowable range
3.	Selling price can be increased, provided that NPM not exceeds the base NPM as on 1 January 2015	Selling price for the year can be increased, as long as the MU% or MG% for goods offered for sales do not exceed MU% or MG% as at baseline first day of that particular year
4.	NPM can be increased due to business efficiency	MU% or MG% can be increased due to business efficiency
5.	Applicable to all goods and services	Applicable to **two classes** of goods
6.	Liable for penalty of fine, imprisonment or both upon prosecution of profiteering offence	Indications by KPDNKK that non-compliance would not be prosecuted immediately. Prosecution only when profiteer fails to adhere to advice to reduce their MU% or MG%

MECHANISM TO DETERMINE "UNREASONABLY HIGH PROFIT"

$P_A = X_1 + Y$

P_B or P_C cannot > P_A

1. The formula to compute the baseline MU% or MG% (**P_A**) for the first day of the year (FY or CY) by making reference to the MU% or MG% (X_t) for up to three (t=3) preceding years.

2. The allowable increase (**Y**) is the higher value of increase in MU% or MG% between the first day of the last three preceding years:

$$Y = T_1 \text{ or } T_2 \text{, whichever higher}$$

where
$$T_1 = X_1 - X_2$$
$$T_2 = X_2 - X_3$$

3. To comply with non-profiteering, the MU% or MG% throughout that particular year (**P_B** or **P_C**) shall not be higher than the computed base (**P_A**).

Assumed business adopts 1 Jan 2017 as first day of the current year with computed P_A of 5.7%.

How to comply the regulations?

1 Jan 2017	2 Jan 2017 – 31 Dec 2017
P_A = 5.7%	P_B or P_C cannot > 5.7%

** P_B or P_C refers to MU% or MG% for the entire year*

How to determine profiteering?

- If P_B or P_C is > P_A of 5.7% ➔ **Profiteering**
- If P_B or P_C is ≤ P_A of 5.7% ➔ **Not Profiteering**

Remarks:

1. Mechanism only applicable to the goods with **same description and same class**.
2. If MU% or MG% exceeds its base P_A due to **cost efficiency**, it is not considered as profiteering.

AN ILLUSTRATION OF THE GENERAL RULE

Assumed the business adopts 1 Jan 2017 as first day of the current financial year (FY) or calendar year (CY).

(Third preceding year) 2014		(Second preceding year) 2015		(First preceding year 2016		(Current year 2017	
1 Jan 2014	2 Jan 2014 – 31 Dec 2014	**1 Jan 2015**	2 Jan 2015 – 31 Dec 2015	**1 Jan 2016**	2 Jan 2016 – 31 Dec 2016	**1 Jan 2017**	**2 Jan 2017 – 31 Dec 2017**

Step 1: *Identify X_1, X_2 and X_3 from past three preceding years from business records.*

X_3 = 5%

X_2 = 5.3%

X_1 = 5.4%

Step 2: *Compute the differentials T_1 and T_2 , choose the higher value between the two.*

$T_2 = X_2 – X_3$ = 0.3%

$T_1 = X_1 – X_2$ = 0.1%

Y = 0.3%

Step 3: *Compute the base MU% or MG% for the year 2017.*

$P_A = X_1 + Y$
= 5.4% + 0.3%
= 5.7%

To comply with PCAP Regulations 2016, the selling prices can be increased throughout the year, provided that the MU% or MG% resulting from the change in prices do not exceed the value of P_A , i.e. 5.7%.

COMPARISON BETWEEN THE NEW & PREVIOUS MECHANISMS

First day of the year		Cost	Selling Price	Margin	Previous Mechanism	New Mechanism (MU%)		New Mechanism (MG%)	
		C	SP	Margin (RM)	Base NPM (RM)	$MU\% = \frac{SP - C}{C} \times 100\%$		$MG\% = \frac{SP - C}{SP} \times 100\%$	
Third Preceding	1 Jan 2014	1.95	2.80	0.85		$X_3 = 43.6\%$		$X_3 = 30.4\%$	
Second Preceding	1 Jan 2015	2.00	2.90	0.90	0.90	$X_2 = 45.0\%$	$T_2 = 1.4\%$	$X_2 = 31.0\%$	$T_2 = 0.7\%$
First Preceding	1 Jan 2016	2.10	3.00	0.90	0.90	$X_1 = 42.9\%$	$T_1 = -2.1\%$	$X_1 = 30.0\%$	$T_1 = -1.0\%$
Current	1 Jan 2017	2.20	3.10	0.90		$P_A = X_1 + Y = 42.9\%+1.4\% = 44.3\%$		$P_A = X_1 + Y = 30.0\%+0.7\% = 30.7\%$	

If within 1 Jan 2017 - 31 Dec 2017:

Δ COGS	Δ Selling Price	Cost	Selling Price	Margin in Ringgit	Profiteering?	P_B	$P_B > P_A$?	*C_B lower?	Profiteering?	P_C	$P_C > P_A$?	*C_C lower?	Profiteering?
(-0.20)*	0.10	2.00	3.20	1.20	Profiteering	60.0%	Yes	Yes	Not Profiteering	37.5%	Yes	Yes	Not Profiteering
(-0.20)*	0.00	2.00	3.10	1.10	Profiteering	55.0%	Yes	Yes	Not Profiteering	35.5%	Yes	Yes	Not Profiteering
(-0.20)*	(-0.10)	2.00	3.00	1.00	Profiteering	50.0%	Yes	Yes	Not Profiteering	33.3%	Yes	Yes	Not Profiteering
(-0.20)*	(-0.20)	2.00	2.90	0.90	Not Profiteering	45.0%	Yes	Yes	Not Profiteering	31.0%	Yes	Yes	Not Profiteering
0.00	0.10	2.20	3.20	1.00	Profiteering	45.5%	Yes	No	Profiteering	31.3%	Yes	No	Profiteering
0.10	0.10	2.30	3.20	0.90	Not Profiteering	39.1%	No	No	Not Profiteering	28.1%	No	No	Not Profiteering
0.10	0.20	2.30	3.30	1.00	Profiteering	43.5%	No	No	Not Profiteering	30.3%	No	No	Not Profiteering
0.20	0.35	2.40	3.45	1.05	Profiteering	43.8%	No	No	Not Profiteering	30.4%	No	No	Not Profiteering
0.30	0.50	2.50	3.60	1.10	Profiteering	44.0%	No	No	Not Profiteering	30.6%	No	No	Not Profiteering
0.40	0.60	2.60	3.70	1.10	Profiteering	42.3%	No	No	Not Profiteering	29.7%	No	No	Not Profiteering
0.50	0.75	2.70	3.85	1.15	Profiteering	42.6%	No	No	Not Profiteering	29.9%	No	No	Not Profiteering

** Lower costs due to cost efficiency*

- The new mechanism provides greater flexibility compared to the previous mechanism. Price revisions that previously did not comply to the regulations do not constitute unreasonably high profit under the new mechanism (as indicated in upper circle).
- The new mechanism gives recognition to cost efficiency (as indicated in lower circle).

EXCEPTIONAL BUSINESS SCENARIOS

- The PCAP Regulations 2016 have provisions that allow exception for certain business situations. In some of these business situations, the MU% or MG% on a date in a particular year may exceed the baseline MU% or MG% on the first day of that year. A good example is when there is a reduction in costs due to cost efficiency.
- Other business scenarios that require separate formula in determining profiteering are as follows:

Scenario A – for the first day of the respective three preceding years:

i. Goods are sold or offered for sale at the **cheap sale price**;
ii. New goods are sold or offered for **sale at the introductory price**;
iii. Goods are **not sold or offered for sale**;
iv. Goods are sold or offered for sale at the **price below the cost**; and
v. There is **no business operation conducted**

Scenario B – **the values of X and Y do not exist** due to:

i. Newly operating business;
ii. Business starts selling the particular goods for the first time; and
iii. Business resumes selling the goods which have not been sold or offered for sale in the past three preceding years

Scenario C – **when Y is zero or less than zero** due to:

i. When the values of baselines MU% or MG% remain the same for last three preceding years; and
ii. When there were consecutive reductions in the values of baseline MU% or MG% for last three preceding years

*Note: The formula to determine "Profiteering" for these situations are illustrated in **Appendix.***

1. Short notice prior to the implementation

- The new PCAP Regulations 2016 was announced in late notice before the effective date of implementation on 1 January 2017.
- This has created unnecessary anxiety for the business community as they could potentially encounter practical issues associated with the computation and compliance with the new rules.
- Amid a grace period of three (3) months for familiarization and adaption, there are areas/issues that require further clarification. KPDNKK is expected to provide more details of the mechanism, including the classification of goods and FAQs for ease of understanding.

2. Mechanism contradictory with real business approaches

- The "one-size-fits-all" formula approach is seen as impractical given a complexity of variables and factors in determining the cost and pricing structure of businesses.
  - Interactions of supply and demand, subject to domestic and external factors.
  - It is unrealistic to assume uniform pricing approach as businesses would adopt differing cost structure and pricing strategies.
  - As part of the group-wide business strategy, businesses would adopt redistribution of profit contributions by products and market demand.

3. Narrower coverage

- The PCAP Regulations 2016 only applies to food and beverage as well as household goods compared to covering all goods and services previously. However, the classes of household goods are too broad and too general. It is proposed to have a negative list approach for simplification.
- It is a huge relief for those businesses not under the coverage. As they would no longer be burdened by compliance costs and hence, have greater flexibility in revising their pricing policy.

4. Pending issues remained unresolved

- Additional compliance cost and cumbersome records keeping, especially for small businesses. The compliance with documentation and paperwork as required by KPDNKK would add to compliance and administrative costs. Many small businesses have been accustomed to setting their profits based on "gut feeling" and experience, with no or little paper work.
- The compliance cost incurred may eventually passed on to consumers, in the form of higher prices.

5. Continuous engagement

- Amidst the unresolved pending issues, KPDNKK must ensure that there are continuous engagements with the business sectors and trade associations to improve the PCAP Regulations 2016's practicability.
- KPDNKK should adopt the approach of "to educate" rather than "to punish" the businesses when enforcing the PCAP Regulations 2016. KPDNKK should pro-actively create awareness and educate the businesses about the new anti-profiteering mechanism prior to strict enforcement. The enforcement can be carried without creating any fear and anxiety, and/or disrupts business operations.
- Continuous engagement with consumers should be enhanced. KPDNKK must work together with the relevant consumer bodies and trade associations to build consumer activism and also cultivate smart spending.
- Strong consumers' awareness of price watching can be achieved through enhancing the Ministry's pricing dissemination activities such as "Paparan Harga", targeting higher number of active users for "Friends of KPDNKK" as well as the strengthening of this mobile application's effectiveness.

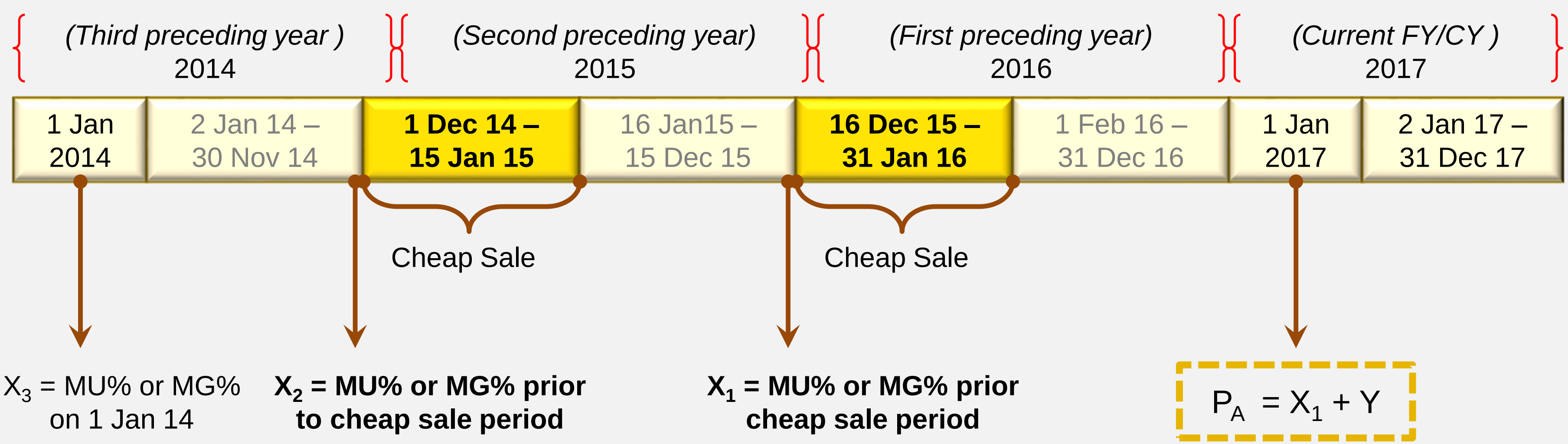
APPENDIX

EXCEPTIONAL BUSINESS SCENARIOS

Scenario A (i): *Goods are sold/offered for sale at the cheap sale price on the first day of the respective FY or CY*

1. When the first day of last preceding year falls within the period when the goods are offered for sale at cheap sale price, then the MU% or MG% for the current year shall not be higher than the MU% or MG% on **the first day prior to that cheap sale** (X_1) plus an allowance of increase (Y).
2. The allowable increase (Y) is computed based on the higher value of increase in MU%/MG% on the first day or the day prior to the commencement of cheap sale of three preceding years.
3. In the illustration below, the cheap sale period was 16 Dec 2015 to 31 Jan 2016 and 1 Dec 2014 to 15 Jan 2015. Hence, X_1 shall be the MU% or MG% on 15 Dec 2015 (the day prior to cheap sales), X_2 shall be the MU% or MG% on 30 Nov 2014 while X_3 remained as the MU%/MG% on 1 Jan 2014.

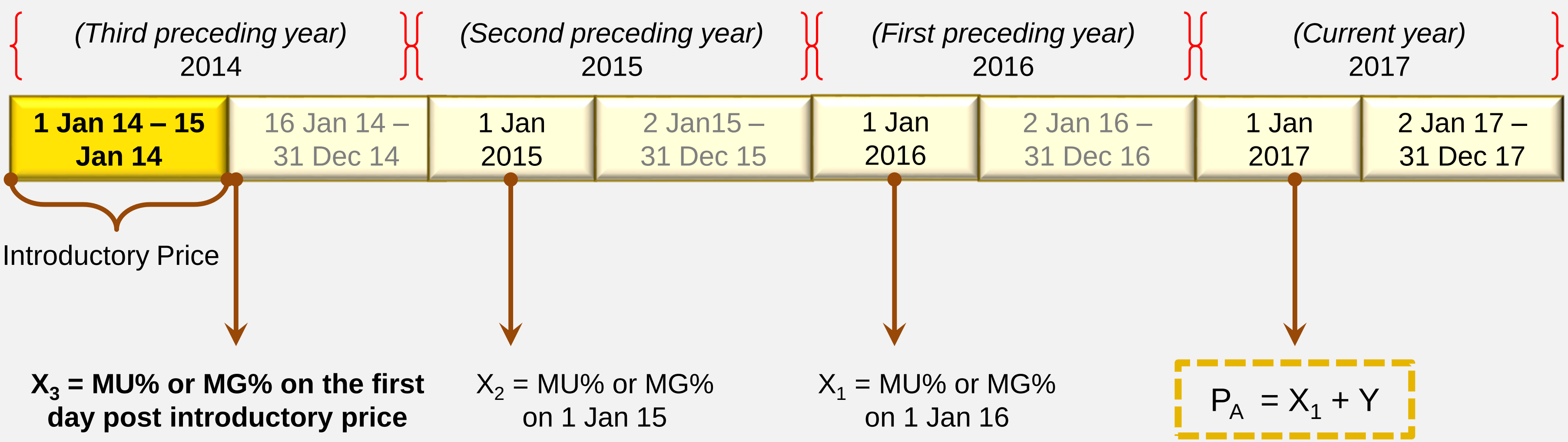
Illustration – Assumed business adopts 1 Jan 2017 as first day of the current year (FY or CY):



Scenario A (ii): *New goods are sold or offered for sale at the introductory price on the first day of the respective FY or CY*

1. MU% or MG% for the current year shall not be higher than the MU% or MG% on the **first day immediately after the introductory period** of the previous year (X_1) plus an allowance of increase (Y).
2. The allowable increase (Y) is computed based on the higher value of increase in MU%/MG% on the first day or the day after the introduction price of three preceding years.
3. In the illustration below, the goods were first offered for sale at introductory price during 1 -15 Jan 2014. Hence, X_1 and X_2 remained as the MU% or MG% on the first day of the year while X_3 shall now be the MU% or MG% on 16 Jan 2014 instead of 1 Jan 2014.

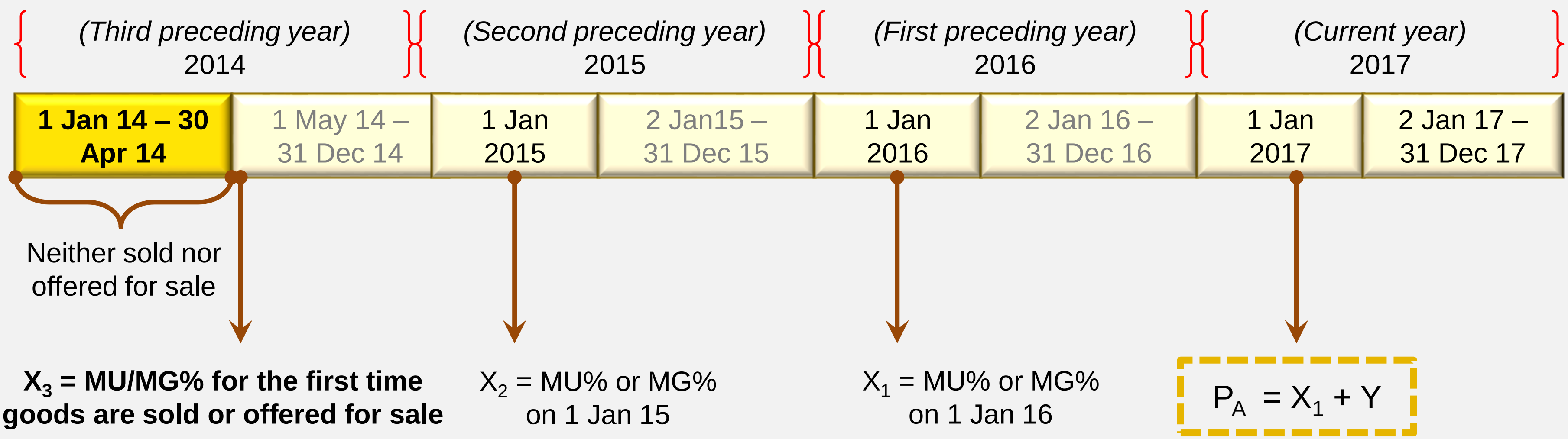
Illustration – Assumed business adopts 1 Jan 2017 as first day of the current year (FY or CY):



Scenario A (iii): *No Goods offered for sale on the first day of the respective FY or CY*

1. In the situation where there was no goods offered for sale on the first day of the year (FY or CY), then the value of MU% or MG% shall be taken **when the goods are offered for sale for the first time**.
2. As illustrated below, the good was neither sold nor offered for sale during 1 Jan – 30 Apr 2014. Such scenario may include the good that was only introduced into the market on 1 May 2014.
3. To compute the MU% or MG% of the current year, X_1 and X_2 remained as the MU% or MG% on the first day of the particular year as required in the general rule while X_3 shall be the MU% or MG% on 1 May 2014 since X_3 does not exist on 1 Jan 2014.

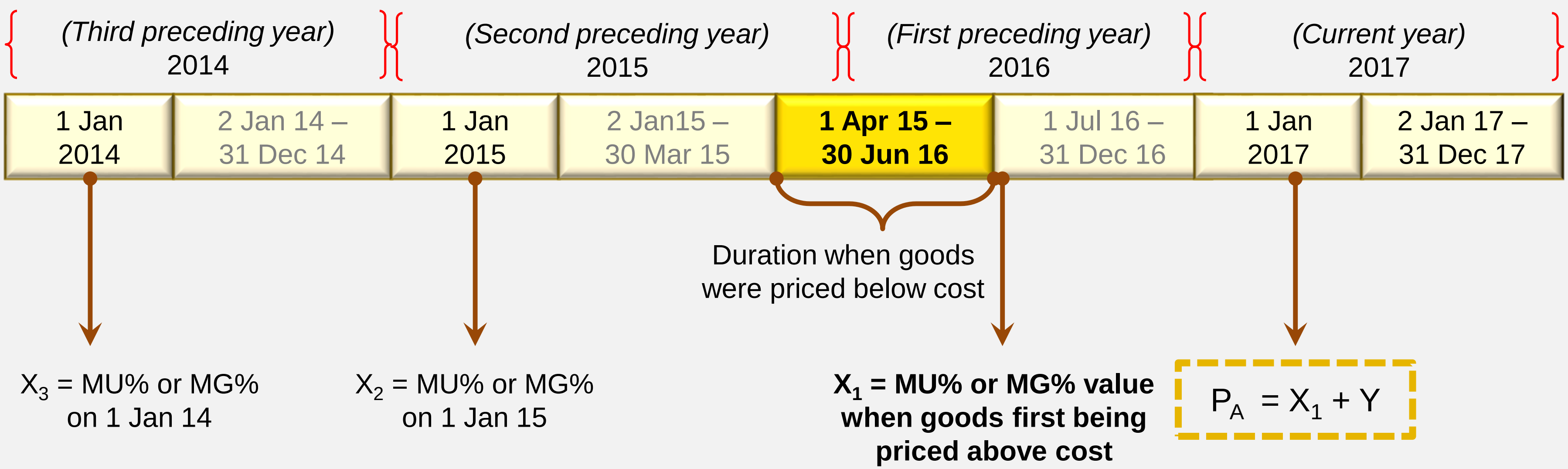
Illustration – Assumed business adopts 1 Jan 2017 as first day of the current year (FY or CY):



Scenario A (iv): *Goods are sold or offered for sale at the price below the cost on the first day of the respective FY/CY*

1. In the case where the first day of any of the preceding years happened to fall within the period when the goods were offered for sale at below cost, the treatment of MU% or MG% values are quite similar to situation of introductory price period, as illustrated in Scenario A(ii).
2. In the illustration below, the goods were previously offered or sold at below cost during 1 Apr 2015 to 30 Jun 2016. This means that baseline MU% or MG% of 1 Jan 2016 falls within this period.
3. Therefore in computing the MU% or MG% for the current year (2017), the value of X_1 shall be taken as the value of MU% or MG% on 1 Jul 2016, i.e. when **the goods were offered at above cost for the first time** during that respective year.

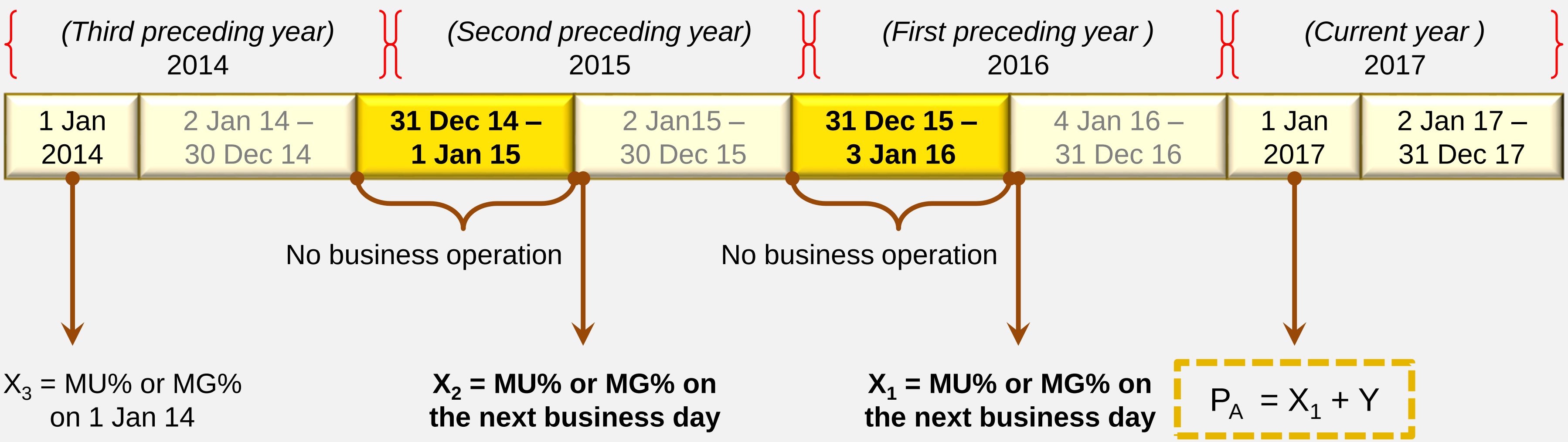
Illustration – Assumed business adopts 1 Jan 2017 as first day of the current FY/CY:



Scenario A (v): *No business operation on the first day of the respective year (FY or CY)*

1. Assuming that the business adopts 1 Jan 2017 as the first day of the current year (FY or CY).
2. Since 1 Jan in any year is usually a public holiday (with no business operation), then the MU% or MG% values of next business day shall be applied in the computation.
3. In the illustration below, X_1 shall be the MU% or MG% on 4 Jan 2016 since 1 Jan, 2 Jan and 3 Jan 2016 were not business days. The value of X_2 shall be the MU% or MG% on 2 Jan 2015 while X_3 remained as the MU% or MG% on 1 Jan 2014.

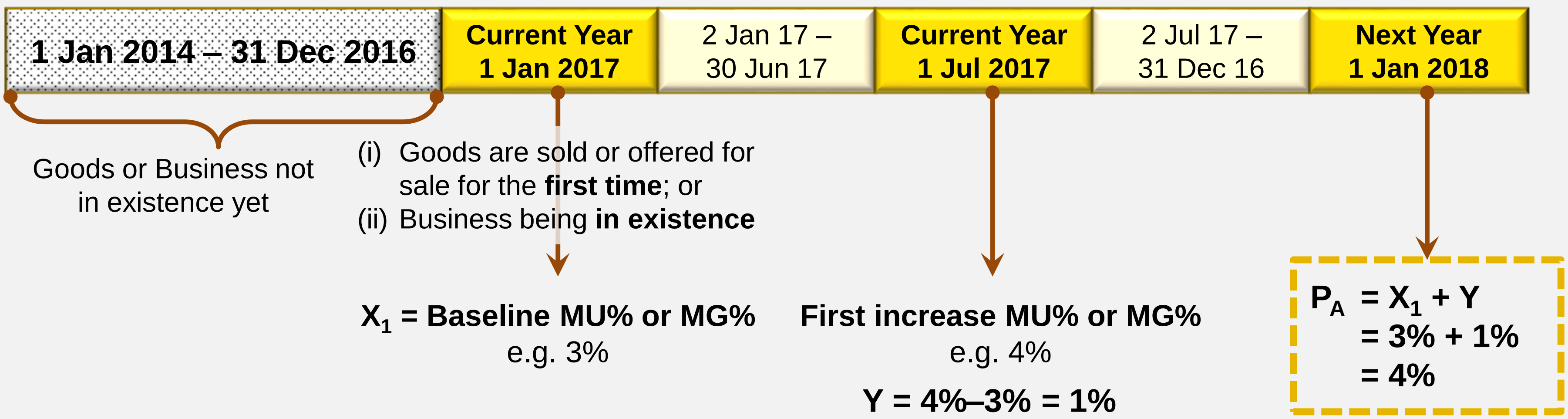
Illustration – Assumed business adopts 1 Jan 2017 as first day of the current year (FY or CY):



Scenario B: *When the values of X and Y do not exist*

1. In the general rule of determining profiteering, the values of costs and selling prices of last three preceding years were taken into account when computing the MU% or MG% value for current year.
2. These historical values do not exist in the following business situations: (i) Newly operating business; (ii) Business starts selling the particular goods for the first time; or (iii) Business resumes selling the goods which have not been sold or offered for sale in the past three preceding years.
3. Since there is no historical records, the MU% or MG% for the current year will be assumed as the baseline values. As illustrated below, the MU% or MG% on 1 Jan 2017 of 3% is the first MU% or MG% (X_1) in the absence of Y (Y does not exist).
4. The business is allowed to increase price for the particular goods once at anytime throughout 2017. In this case, the first increase of MU% and MG% took place on 1 Jul 2017, say from 3% to 4%.
5. In the coming 1 Jan 2018, the P_A can be computed, where X_1 (3%) will be the baseline MU% or MG% for first day of preceding year 2017 while Y is the difference between MU% or MG% during 2017 (4% - 3%).

Illustration – Assumed business adopts 1 Jan 2017 as first day of the current year (FY or CY):



Scenario C (i): *When the baselines values of MU% or MG% remain unchanged for last three years*

In cases where businesses have maintained the same baselines MU% or MG% for first day of last three preceding years (implying that Y=0), the general rule of determining profiteering will be redefined as follows:

Illustration: Assumed business adopts 1 Jan 2017 as first day of the current FY/CY:

(Third preceding year) 2014		*(Second preceding year)* 2015		*(First preceding year)* 2016		*(Current year)* 2017
1 Jan 2014	2 Jan 2014 – 31 Dec 2014	**1 Jan 2015**	2 Jan 2015 – 31 Dec 2015	**1 Jan 2016**	2 Jan 2016 – 31 Dec 2016	**1 Jan 2017**

X_3 = 5.4%

X_2 = 5.4%
T_2 = 0.0%

X_1 = 5.4%
T_1 = 0.0%

P_A = X_1 + Y
= 5.4% + 0.0%
= 5.4%

First time increase of MU% or MG% e.g. to 5.6%

X_3 = 5.6%

First time increase of MU% or MG% e.g. to 5.9%

X_2 = 5.9%
T_2 = X_2 - X_3 = 0.3%

First time increase of MU% or MG% e.g. to 5.5%

X_1 = 5.5%
T_1 = X_2 - X_3 = -0.4%

Following general rule of baseline MU% or MG%, the P_A would have been 5.4%

Redefined Y = 0.3%

<u>With Redefined Y:</u>
P_A = X_1 + Y
= 5.4%+0.3%
= 5.7%

Implication: **With redefined Y, business is actually allowed to have higher profit margin of 5.7% (instead of the unchanged 5.4%) and still comply with PCAP Regulations 2016.**

Scenario C (ii): *When consecutive reductions in baseline MU% or MU% occurred for last three years*

In cases where businesses faced consecutive declines in baselines MU% or MG% for last three preceding years (implying that Y < 0), the general rule of determining "Profiteering" will be redefined as follows:

Illustration: Assumed business adopts 1 Jan 2017 as first day of the current FY/CY:

(Third preceding year) 2014		*(Second preceding year)* 2015		*(First preceding year)* 2016		*(Current year)* 2017
1 Jan 2014	2 Jan 2014 – 31 Dec 2014	**1 Jan 2015**	2 Jan 2015 – 31 Dec 2015	**1 Jan 2016**	2 Jan 2016 – 31 Dec 2016	**1 Jan 2017**
X_3 = 5.4%	First time increase of MU% or MG% e.g. to 5.6% **X_3 = 5.6%**	**X_2 = 5.3%** **T_2 = -0.1%**	First time increase of MU% or MG% e.g. to 5.9% **X_2 = 5.9%** **$T_2 = X_2 - X_3$ = 0.3%**	**X_1 = 5.1%** **T_1 = -0.2%**	First time increase of MU% or MG% e.g. to 5.5% **X_1 = 5.5%** **$T_1 = X_2 - X_3$ = -0.4%**	**$P_A = X_1 + Y$** **= 5.1% - 0.1%** **= 5.0%**

Redefined Y = 0.3%

Following general rule of baseline MU% or MG%, the P_A would have been 5.0%

<u>With Redefined Y:</u>
$P_A = X_1 + Y$
= 5.1%+0.3%
= 5.4%

Implication: With redefined Y, business is actually allowed to have higher profit margin of 5.4% (instead of the reduced 5.0%) and still comply with PCAP Regulations 2016.

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谢谢

THANK YOU

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