

The information in relation to the connected transaction between the Company and Pico Art International Pte. Ltd. regarding Off-Shore Services Agreement dated 10 July 1992 (and amendments) and Intellectual Property License Agreement dated 10 July 1992 (and amendments)

The background of the license fee and service fee according to Intellectual Property License Agreement and Off-Shore Service Agreement

The background of the license fee and service fee according to Intellectual Property License Agreement and Off-Shore Service Agreement is divided into 2 parts. First is the information as specified in the Intellectual Property License Agreement and Off-Shore Service Agreement. Second is the actual practice of the fee calculation and payment. The detail is as follows.

1) Intellectual Property License Agreement and Off-Shore Service Agreement

Intellectual Property License Agreement (“IP License Agreement”) and Off-Shore Services Agreement (“Service Agreement”) were originally made between the Company and Pico Art International Pte. Ltd. (“Pico Art”) on 10 July 1992 and were latest amended on 3 November 2003. The fee specified in each of these agreements including their amendments is as below.

Intellectual Property License Agreement (“IP License Agreement”) :

License fee = 0.53% of accrued gross revenue of the fiscal year with additional condition as follows :

- i) in the event that the Company’s net profit before tax is equal to or exceed 9.54% of gross revenue, the license fee is 0.53% of gross revenue;
- ii) in the event that the Company has loss or net profit before tax equals to 0, no license fee is required to be paid;
- iii) in the event that the Company’s net profit before tax is less than 9.54% of gross revenue, the license fee is the following proportional rate which is net profit before tax of such fiscal year per gross revenue divided by the rate of 9.54 multiplied by 0.53% of gross revenue.

Off-Shore Service Agreement (“Service Agreement”) :

Service fee = 2% of accrued gross revenue of the fiscal year

2) Actual practice of the fee calculation and payment

However in term of actual practice and given the evidence that we can trace back, the payment of the fees under these agreements has never been clearly divided as license fee of 0.53% and off-shore service fee of 2%. For the purpose of the payment of such fees, the fee rates were combined as one at the rate of 2.53% of gross revenue (usually called as “management fee”). This practice began before the year 2004, which was the year that the Company became the listed company on the Stock Exchange of Thailand. As a result, the Company has never deducted the withholding tax on the license fee (0.53% of gross revenue) when making the payment to Pico Art. It should be noted that the Company has disclosed its obligation to pay the fee in relation to the right to use trademark and tradename including the cooperation and consultation on technology, human resources development, marketing, and etc. to Pico Art at the rate of 2.53% of gross revenue in “Part 2, Section 11 Related Party Transactions of its Prospectus”, which became effective on 24 March 2004.

The Company’s prospectus can be downloaded from SEC website.

In addition, it was also noted that since the years before the Company listed into Stock Exchange in 2004, the additional condition of IP License Agreement, which is the proportional fee based on the Company's profit before tax each year, has never been taken into account when calculating the fee to be paid each year rather the Company has usually requested for a waiver of some revenue items used for the base of calculation of the management fees, which resulted in the Company paying the fees less than the amount that it was supposed to pay.

After the entries into such agreements, the Company's CEO constantly made the written request to Pico Art for waiving some items of revenue, which were parts of the gross revenue, for the purpose of calculation of the management fee (2.53%). This resulted in the reduction of the amount of management fee that should have been actually paid in the relevant years.

When comparing the fee, calculated according to the means of calculation under each Services Agreement and IP License Agreement including its amendments, with the fee, calculated according to the actual practice, the fee calculated per actual practice would be lower than the fee calculated by means specified in agreements around 10 million Baht during the year 2004-2022.

In December 2022, the Company just found out that the actual payment of the management fee has not been calculated in accordance with those specified in the agreements as explained earlier. Therefore, the Company has sought for the legal opinion if the actual payment in the past was the wrongdoing or not. The legal opinion from Dharmniti Law Office Co., Ltd. and R&T Asia (Thailand) Limited (Rajah & Tann) were obtained. Both law firms gave their opinion that the practice that the Company has consistently done for the past years is not the wrongdoing and can be considered as implied agreement.

For the future, the Company can consider either continuing the current practice or going back to proceed according to the term and conditions specified in the agreements. However if the Company decides to continue the current practice, it is recommended to amend the agreements to reflect the current practice accordingly.

The information in response to Mr. Pised and Mr. Supavit's inquiries

Reference to the letter of Mr. Pised and Mr. Supavit dated 29 February 2024, the Company would like to provide the information in response to each of Mr. Pised and Mr. Supavit's inquiry as follows :

1) Has the entries into these two agreements been approved by the board of directors and/or shareholders or not? Please explain.

The Company's response :

As explained earlier, these two agreements were originally made on 10 July 1992 and the latest amendment was made on 3 November 2003, which was the time before the Company became the listed company in Stock Exchange of Thailand (the Company's shares were listed on Stock Exchange of Thailand in 2004). The Company is unable to locate the approving documents relating to the entries into the Off-Shore Services Agreement and Intellectual Property License Agreement including its amendments.

However, the Company has disclosed in "Part 2, Section 11 Related Party Transactions of its Prospectus" that the past related transactions between the Company and its shareholders or related company, which relates in term of general business operation and joint venture partner, who granted license to use intellectual property rights, have been approved by the Company's management, significantly taking into account the Company's best interest.

The correctness of the information stated in the Company's Prospectus was certified by the Company's directors as the details of which are shown in "Part 4 of the Prospectus".

2) Since there are a lot of issues covered in this inquiry from Mr. Pised and Mr. Supavit, the Company would like to respond to each issue as follows :

- Are both agreements made with general commercial terms and conditions? Please explain.

The Company's response :

As these 2 agreements and its amendments have been made long time ago and were approved by the Company's management at that time, significantly taking into account the Company's best interest, the Company believes that at that time, these agreements and its amendments were made in good faith with the commercial terms acceptable to both parties.

- How long (many years) shall the agreements be in effect?

The Company's response :

Assuming that neither parties are in breach of these agreements, they will continue to have effect until mutually terminated by both parties.

- Does the Company have the right to terminate the contract unilaterally without any breach of contract caused by Pico Art?

The Company's response :

No

- And what is the size of the transaction?

The Company's response :

As explained earlier, the transaction and the entries into these 2 agreements and its amendment were made before the Company became the listed company on the Stock Exchange of Thailand. Also the relevant information regarding this transaction has been disclosed in "Part 2, Section 11 Related Party Transactions of its Prospectus". As a result, the Company is not required to calculate the size or value of this transaction afterward or before it makes the payment under these agreement in each year. This is because the agreements were made before the Company became the listed company and has the duty under the Notification of the Board of Governors of the Stock Exchange of Thailand re: Disclosure of Information and Other Acts of Listed Companies Concerning the Connected Transactions, 2003 and the Notification of the Board of Governors of the Stock Exchange of Thailand re : Disclosure of Information and Other Acts of Listed Companies Concerning the Acquisition and Disposition of Assets, 2004. The investors, who bought the Company's IPO shares, were supposed to have been aware of that information.

From the year 2005 to 2007, the Company continued to disclose the same information in its annual report (Form 56-1) under the part dealing with "Related Parties Transaction". Unfortunately, subsequently for some unknown reason, this information has not been repeatedly stated in the Company's annual report (Form 56-1) under part dealing with "Related Parties Transaction" but the similar information has been disclosed in its financial statements under notes to financial statements (Related Parties Transaction).

Nevertheless, for the sake of disclosure matter, the Company will provide the information, which was originally disclosed in "Part 2, Section 11 Related Party Transactions of its Prospectus", in the annual report (Form 56-1) from the next year onward as follows

"the fee charged between Pico Art and the Company is in accordance with the Intellectual Property License Agreement and Off-Shore Service Agreement for the use of commercial copyrights with Pico Art, the cooperation and assistance from Pico Art in providing technology consulting, personnel development training, marketing cooperation, etc. The fee rate is 2.53% of total revenue, which is the lower rate when comparing with the royalty fee paid by other PICO affiliates across 26 countries around the world which range from 2.53% to 7% of total revenue."

- In calculating the transaction size, does it have to be calculated from total fee to be paid throughout the agreement period? Please explain.

The Company's response :

The above response should have covered the answer to this question.

- In this regard, the annual report does not explain about the size of the transaction and specify only that the said transaction is a general business transaction with appropriate prices and other conditions which are in accordance with the market price. Therefore, we request the confirmation from the Company and the board of directors that both agreements are made with general commercial terms and conditions. Especially in the case where the agreement period has not been specified, can it still be considered that both agreements are made with general commercial terms and conditions or not?

The Company's response :

As mentioned earlier, these agreements have been made long time ago, before the Company becoming the listed company. It was confirmed that such transaction had been approved by the Company's management at that time, significantly taking into account the Company's best interest. Therefore, the Company believes that at that time, these agreements and its amendments were made in good faith with the commercial terms acceptable to both parties. It is the Company's view that these agreements contain the commercial terms, which are generally used for these types of agreements. It is not unusual that these agreements can be terminated by mutual agreement of both parties or there is no specific period or term of the agreements. The Company believes that the management at that time thoroughly considered that the terms and conditions of these agreements are acceptable.

- And the fees are calculated at market rates which are comparable to which companies?

The Company's response :

As mentioned earlier, it is believed that the management at that time considered and agreed that the fees rate under these agreements were acceptable. However the Company would like to inform the shareholders that after the entries into such agreements, the Company's CEO constantly made the written request to Pico Art for waiving some items of revenue, which were parts of the gross revenue, for the purpose of calculation of the management fee (2.53% of gross revenue). This resulted in the reduction of the amount of management fee that should have been actually paid in the relevant years.

It should also be noted that when comparing the fee, calculated according to the means of calculation under each Services Agreement and IP License Agreement including its amendments, with the fee, calculated according to the actual practice, the fee calculated per actual practice would be lower than the fee calculated by means specified in agreements around 10 million Baht during the year 2004-2022.

In addition, the Company was informed by Pico Art that the normal fee rate charged to other companies by Pico Group is ranged from 3% to 7%.

- And because it is a long-term agreement or does not have a specified period of time, have the Company/board of directors/ audit committee regularly checked within a reasonable time whether the fee rate is still the actual market rate at present?

The Company's response :

As mentioned earlier, the fee rate of 2.53% is lower than the fee rate charged by Pico Group comparing with other companies. Also, 2.53% of gross revenue is the agreed rate between Pico Art and the Company. In fact, the Company rarely paid the full amount of the management fee to Pico Art as it mostly requested for waiver of some revenue items used for the base to calculate the management fees, which resulted in the Company paying the fees less than the amount that it was supposed to pay. The terms of the Agreements can be negotiated subject to mutual agreement by both parties.

3) Given that the fee disclosed in the annual report is the total fee rate for two agreements, what is the rate or calculation formula for calculating the fee for each agreement? If the Company makes a loss, does it have to pay a fee to Pico Art?

The Company's response :

"The background of the license fee and service fee according to Intellectual Property License Agreement and Off-Shore Service Agreement" explained earlier should have covered the information relating to the fee rates under these 2 agreements.

From the agreed practice between the Company and Pico Art, which was made before the Company became the listed company, the Company shall still pay the fee the relevant year although it incurs loss. Nevertheless, the Company mostly requested for waiver of some revenue items used for the base to calculate the management fees, which resulted in the Company paying the fees less than the amount that it was supposed to pay as mentioned earlier.

4) In the annual report, it is stated only that the Company has a process for approving related party transactions, which must be considered by the Audit Committee and must be approved by the Board of Directors. Therefore we would like the Company to explain the details of the process for approving the payment of fees, such as who is in charge of the calculation of fees and who will present such matters to the Audit Committee and the Board, have the details of the calculation methods been explained to the Audit Committee and the Board of Directors or not? Please explain.

The Company's response :

As mentioned earlier, the transaction under these 2 agreements and its amendments has been already carried out for more than 2 decades. The practice of the calculation of the fees under these 2 agreements was considered as a routine work and became normal practice of the Company's accounting department. According to the relevant evidence, the result of the calculation of the management fee has been reviewed by the Company's Chief Financial Officer (CFO) and approved by the Company's Chief Executive Officer (CEO) and then forwarded to Pico Art for further approval on the waiver of certain revenue items as mentioned earlier. After receiving Pico Art's approval on the waiver, the payments of the fees were made by the authorized persons in accordance with the Company's table of authority. The requests for the relevant waivers by the Company have not been rejected by Pico Art.

Neither the Audit Committee nor the Board of Directors has reviewed such calculation sheet but they are fully aware of the transaction, the relevant fee rate and the amount of the fee to be paid to Pico Art calculated and accrued in each quarter (as shown in the reviewed and audited financial statements). In the past 2 years, the Audit Committee has specifically and quarterly reviewed all connected/related transactions.

5) Please clarify the relationship between Mr. Chia Song Heng, Chairman of the Board of Directors and Vice Chairman of the Executive Committee and Ms. Chia Yuan Jiun, Director, Chairman of the Executive Committee (Acting) and Chief Executive Officer, with Pico Art. And in the case that Mr. Chia Song Heng and Ms. Chia Yuan Jiun are related persons with Pico Art, have both of them voted in the meeting to approve the calculation and the payment of fees to Pico Art or not? If the two persons are persons related to Pico Art, will they be considered to have a conflict of interest in voting on matters related to both agreements or not since in the annual report it is stated that directors or executives or persons with vested interests will not have the right to vote on such items?

The Company's response :

As mentioned earlier, according to the Company's normal practice, the Board of Directors has not been proposed to consider, review or approve the calculation sheet of the management fee or the amount of the fee paid to Pico Art. Therefore, Mr. Chia Song Heng (the Company's director and the Chairman of the Board of Directors) and Ms. Chia Yuan Jiun (the Company's director and the Chief Executive Officer), as the members of the Board of Directors, have never been involved in the reviewing or approving process of the calculation of the management fee and the payments of such fee to Pico Art. They are aware of the amount of the management fee calculated and accrued as shown in the Company's reviewed and audited financial statements as such financial statements require the approval of the Company's Board of Directors.

6) In paying fees to Pico Art, has the company withheld tax correctly?

The Company's response :

As mentioned earlier, given the evidence that we can trace back, the payment of the fees under the Off-Shore agreements has never been clearly divided as IP license fee of 0.53% and off-shore service fee of 2%. For the purpose of the payment of such fees, the fee rates were combined as one at the rate of 2.53% of gross revenue. This practice began before the year 2004, which is the year that Pico Thailand became the listed company on the Stock Exchange of Thailand. As a result, the Company has never deducted the withholding tax on IP license fee (0.53% of gross revenue) when making the payment to Pico Art.

The Company is now taking action to rectify this tax issue.

7) In the annual report, it is stated that Pico Art guarantees that it will not be a shareholder, partner, or conduct the business in competition with the Company. Which agreement is this term and condition stated?

The Company's response :

The Company is unable to identify such non-competition wordings that "Pico Art guarantees that it will not be a shareholder, partner, or conduct the business in competition with the Company" in any written agreements between the Company and Pico Art. However, such non-competition wordings also appear in the Company's Prospectus. It is believed that the duplicate of such wordings was also made in its annual report (Form 56-1) for the subsequent years.