

SUMMARY

Public interest foundations performing a public function have significant assets or receive significant grants or subsidies from the Founder to carry out their public functions. Society has a legitimate expectation to have a comprehensive picture of the operations and activities of organisations managing public funds. Based on its statutory powers, the State Audit Office of Hungary (SAO) audited the John von Neumann University Foundation (hereinafter referred to as the Foundation), which maintains the Kecskemét-based John von Neumann University, to determine whether its investment decisions regarding its liquid assets, totalling HUF 127.5 billion, were regular, purposeful and well-founded, and whether the investment contributed to the preservation and growth of its assets.

Following its establishment in 2020, the Foundation received HUF 44.4 billion in financial assets in the same year, and a further HUF 100.0 billion in 2021, from state funds, which it could use for infrastructure development, the development of the University, and for statutory purposes.

In June, August and October 2021, the Foundation decided to invest its available liquid funds of HUF 127.5 billion in three tranches of HUF 5.0, 22.5, and 100.0 billion, respectively, in a 10-year corporate bond with an exceptionally low interest rate of 2.5 percent issued by OPTIMA Investment Ltd. (OPTIMA Befektetési Zrt.), owned by the PADME Foundation. The sole owner of OPTIMA Investment Ltd. is the PADME Foundation, whose Chairman of the Board of Trustees was also the Chairman of the Board of Trustees of the John von Neumann University Foundation, and the operational manager and director of the PADME Foundation was also a trustee of the Kecskemét-based Foundation.

The purchase of the bond was presented as liquid investment that was easy to redeem and cash in, in spite of the fact that the bond's issuer knew that the proceeds of the issue would be used to finance long-term, illiquid investments, meaning that there was no realistic chance that the option could actually be exercised and that the bond could be converted into enough cash to settle the obligation within three months (8 banking days or 90 calendar days) without loss or risk. The Board of Trustees deciding on the investment was also aware of this, as, at the meeting of the Board of Trustees discussing the proposal for the subscription of the first bond package, the then-CEO of OPTIMA Investment Ltd. presented the company's strategy as one that 'focuses primarily on investments in high income generating real estate in Central and Eastern Europe'.

According to the minutes of the January and September 2023 Board of Trustees meetings, the statements made by the speakers also confirm that the Board of Trustees was aware that liquidity was only apparent: 'While the right of redemption deserves consideration, we cannot destroy the real estate rental and operating activities that were financed by this investment, and the Foundation's assets must not be exposed', and 'in relation to the

changed bond structure, redemption sounds good, but carries an extremely high risk. This may not even be a real and realistic option.'

At the time of the investment, the Board of Trustees failed to assess the Foundation's future cash demand, and therefore did not consider the maturity of the investments. The choice of liquid investment was presumably made to underpin the very low interest rate. It was known to the Board of Trustees that the investment was, in fact, illiquid. In the years since the investment decision, the Foundation did not even need the money invested in the bond, the bond was not redeemed, and, therefore, the apparent liquidity was, in practice, unnecessary.

The Foundation has not established rules and controls to manage the significant risks inherent in the size and type of this very large investment, and to ensure the soundness of initial and subsequent investment decisions.

Before making their investment decision, the Foundation did not use the services of an investment adviser, in spite of the fact that the size and concentration of the amount it intended to invest would have justified such a decision. Instead, they commissioned an accountant, who was also employed by the PADME Foundation, to draw up an unprofessional comparative analysis of the potential investments, which highlighted the advantages of the corporate bonds of OPTIMA Befektetési Zrt. while failing to present the risks.

The external auditor of the asset management activity failed to promote responsible asset management at the Foundation and, with regard to the decisions about making or holding investments, failed to draw the attention of the Board of Trustees to the fact that the Foundation was not operating in accordance with the provisions of the Deed of Foundation or the law, or to the risks arising from the excessive concentration of investments.

The decision to subscribe to the first tranche of HUF 5.0 billion of bonds was not in conformity with the regulations because it violated the conflict of interest provision of the Deed of Foundation. The conflict of interest provision in the Deed of Foundation was later repealed, prior to the HUF 22.5 billion and HUF 100.0 billion bond subscriptions, allowing the Chairman of the Board of Trustees to remain a member of the Board of Trustees. However, in 2023 and 2024, another member of the Board of Trustees, who was also the director of the PADME Foundation, regularly voted – in breach of the law – in the Board of Trustees meetings that discussed the future fate of the investments, but failed to indicate their involvement.

The personal entanglements between the sole owner of the bond issuer OPTIMA Investment Ltd., the PADME Foundation and the John von Neumann University Foundation may have contributed to the Board of Trustees putting the interests of the bond issuer before the organisational interests of the Foundation.

The Foundation have concentrated their investments significantly by subscribing to the bond packages. After subscribing to the bond, the Foundation failed to continuously follow up on the financial, asset and income situation of OPTIMA Investment Ltd., which issued the bond, on the operation of a monitoring system ensuring the transparent monitoring of the risks assumed by the issuer, as well as on the establishment of a realistic, collateralised contractual framework and an effective system of controls, thus failing to assess global trends and to take into account the persistent and trend-like downturn in the price of GTC shares, which represented the most significant volume of assets related to the bond, or the deterioration of their credit rating.

Following the subscription of the bonds in 2022, the Foundation commissioned an independent expert analysis of its investment, but ignored its findings. At that time, the expert drew the attention of the Board of Trustees to the need to diversify its investments and to the fact that the secondary market yield on Hungarian government bonds with a maturity of over one year, which can be considered risk-free, exceeded the yield on OPTIMA bond investments.

Despite what was indicated in the independent expert opinions, the Foundation did not take steps to diversify its investments, to redeem its bonds or to exercise its right to sell, as a consequence, among others, of the failure to establish controls and effective safeguards.

In January 2024, the Board of Trustees decided to enter into negotiations with OPTIMA Investment Ltd. to initiate the redemption of the bonds within one year. Since OPTIMA Investment Ltd. was unable to redeem the bonds in accordance with its contractual obligations, negotiations between the issuer and the Foundation on the method and timing of the settlement of the bond purchase price were still ongoing at the time when the SAO audit was concluded.

In the course of the 2024 negotiations with OPTIMA Investment Ltd., an agreement was outlined under which the Foundation would receive, contrary to the option contracts, a significant part of its investment back in company shares and investment units with uncertain returns instead of bank money.

The Foundation recorded the bond in their books at its cost value as at 2021. In their accounting reports for 2022 and 2023, the Foundation still reported the bonds at cost without any impairment, which would have been justified by the fact that the price of GTC shares held by OPTIMA Investment Ltd., which represented the most important volume of assets, was steadily declining on the stock market, and by the fact that it became clear to the Foundation's decision-makers that OPTIMA Investment Ltd. would not be able to pay the purchase price of the bonds by the deadline set in the contract.

The Foundation also suffered significant losses due to the very low interest rates on the bonds. When assessing the yield of bonds, it is necessary to assess not only the yield

environment at the time of their subscription, but also its evolution over time, as they are liquid bonds redeemable at any time with a maximum redemption period of 90 days. If the Board of Trustees had managed the HUF 127.5 billion of assets entrusted to it and invested in OPTIMA bonds with due care, it would have taken into account the drastic change in the yield environment since the bonds were subscribed, and would have recognised that the fixed 2.5 percent paid by OPTIMA Investment Ltd. on the bonds is blatantly lower than the risk-free (!) benchmark yield available on government bonds. The maximum 12-month benchmark yield during this period (March 2023) was 14.64 percent, which is 12.14 percentage points higher than the 2.5 percent interest rate on the bonds – hardly risk-free – issued by OPTIMA Investment Ltd. Thus, in addition to the fact that the recovery of the total amount invested in the bond has become doubtful, the loss in the form of lost profits alone could reach HUF 15.4 billion in the first full year for March 2023 investments.

BACKGROUND

In the year of its establishment and the following year, the Foundation received a total of HUF 144.4 billion in financial assets from the Founder for infrastructure development, the development of the University and the achievement of the Foundation's objectives. Based on the decisions of the Board of Trustees, the Foundation invested the liquid funds available from the capital infusion, totalling HUF 127.5 billion, in three tranches in the 10-year corporate bonds OPTIMA2031 and OPTIMA2031/B, with an interest rate of 2.5 percent, issued by OPTIMA Investment Ltd.

Following the decisions of the Board of Trustees in June, August and October 2021, the subscription letter for the bonds was signed by the Chairman of the Board of Trustees. Commitment letters have been issued for each bond package by the CEO of GTC Holding Ltd. (GTC Holding Zrt.) and the Chairman and Vice-Chairman of the Board of Trustees of PADME Foundation on behalf of PADME Foundation as the sole shareholder of OPTIMA Investment Ltd. In these letters, they agreed to put OPTIMA Investment Ltd., if necessary, in a position to meet its payment obligations under the bonds and to ensure its solvency. In addition, according to the information memorandum of the HUF 5.0 billion bond, the payment obligations arising from the bonds were secured in significant part by GTC shares issued by Globe Trade Centre S.A., in respect of which GTC Holding Ltd. has undertaken in a commitment letter not to dispose of them without the prior written consent of the Foundation.

For all three bond packages, a contract for the creation of a put option was also concluded between the Foundation as the beneficiary and OPTIMA Investment Ltd. as the obligor, on the recommendation of the auditor. According to these contracts, after the opening of the put option, OPTIMA Investment Ltd. is obliged to purchase the bonds at the specified purchase price based on the Foundation's declaration of sale submitted to OPTIMA Investment Ltd., within 8 banking days after the receipt of the declaration in the

case of the HUF 5.0 and the HUF 22.5 billion bond packages and within 90 calendar days in the case of the HUF 100.0 billion bond package. Under the contract, payment of the purchase price is to be made by bank transfer to the bank account specified by the Foundation, provided that the Foundation exercises its right of redemption. The date of opening of the put option was 9 July 2022 for the HUF 5.0 billion bond package, 18 February 2022 for the HUF 22.5 billion bond package, and 11 October 2022 for the HUF 100.0 billion bond package.

NOTIFICATIONS FROM THE SAO

Since the responsible management of public funds is of utmost importance for the SAO, in the summer of 2024, the President of the SAO, based on the facts revealed during the SAO audit, addressed the Chairman of the Board of Trustees with a call for action included in Annex VI, drafted in accordance with Article 31 of the SAO Act, with a view to the preservation and responsible management of the assets allocated to the Foundation. The Chairman of the Foundation's Board of Trustees informed the President of the SAO in his reply included here as Annex VII that negotiations were ongoing with OPTIMA Investment Ltd. for the redemption of the bonds and that a comprehensive agreement was expected to be concluded. Based on the reply to the call for action, included in Annex VIII, the Vice-President of the SAO reminded the Chairman of the Foundation's Board of Trustees to ensure that the Foundation's assets invested in the bonds are paid in bank money, in compliance with the provisions of the contracts on the put option and the payment of the purchase price. The President of the SAO addressed the President of the Board of Trustees with the call for action as per Article 31 of the SAO Act, included here in Annex IX, calling for action based on the additional risks identified during the audit. The Chairman of the Foundation's Board of Trustees informed the President of the SAO in his reply included here as Annex X that negotiations were ongoing for the redemption of the bonds and for the conclusion of the framework agreement.

Based on the audit findings, the SAO established the suspicion of several criminal offences and filed a complaint with the prosecutor's office pursuant to Article 30(1) of the SAO Act.

In order to ensure the lawful operation of the Foundation, the SAO initiated a legality supervision procedure at the prosecutor's office.

In connection with the audit of the Foundation's annual accounts for the years 2021–2023, the SAO contacted the Auditors' Public Oversight Authority in order to consider conducting an extraordinary quality control pursuant to Article 173/B(4)(c) of the Act on Auditors.