VALSTYBĖS KONTROLĖ
PUBLIC AUDIT

USE OF FINANCIAL INSTRUMENTS (LOANS, GUARANTEES, VENTURE CAPITAL INVESTMENTS) TO PROVIDE STATE AID

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SUMMARY

Relevance of the Audit

Financial instruments in the form of loans, guarantees and venture capital investments are an important part of the state aid for business, the public sector and agriculture. They aim to stimulate long-term investment and business development, economic growth and competitiveness. In order to ensure a common financing strategy and a more efficient use of resources, in 2023 the four national promotional institutions providing financial instruments were consolidated into one, ILTE, which was granted the status of a national development bank on 12 November 2024. As of 31 December 2024 December 2024, ILTE UAB managed 105 financial instruments with a financing volume of EUR 5.2 billion.

Financial instruments are particularly relevant for the implementation of the country's strategic objectives in areas where market financing is insufficient and/or non-optimal, while avoiding the use of these instruments and subsidies for similar investments for the same target group. According to the Bank of Lithuania's survey, the problem of access to finance is a topical issue for enterprises, and the indicator of access to credit

for enterprises lags behind other EU countries. One of the factors to achieve this goal is to increase the effectiveness of financial instruments.

Audit Objective and Scope

The objective of the audit was to assess whether financial instruments (loans, guarantees, venture capital investments) to provide state aid are managed efficiently.

Main audit questions:

- ✓ whether decisions to use financial instruments (loans, guarantees, venture capital investments) are taken to finance priority activities;
- ✓ whether the financial instruments used contribute efficiently to business, public sector and agricultural promotion decisions.

Audited entities:

- ✓ The Ministry of Finance of the Republic of Lithuania, which formulates the state policy in the field of financial markets and financial services, organises, coordinates and controls its implementation[1], and is the representative institution of the State, the shareholder of ILTE UAB.
- ✓ ILTE UAB, which operates as a national development bank.
- ✓ Ministries of Environment, Energy, Economy and Innovation, National Defence, Culture, Social Security and Labour, Agriculture of the Republic of Lithuania, responsible for identifying the need for the financial instruments evaluated and supervising the implementation.

We would like to thank the audited entities, representatives of the Association of Lithuanian Banks, the Confederation of Lithuanian Industrialists, the Bank of Lithuania and the Competition Council for their cooperation.

Audit period - Q3 2021-2024. In order to assess trends and developments, in some cases we have used data for the previous years and for 2024-2025.

The audit was carried out in accordance with international standards of supreme audit institutions. The scope of the audit and the methods used are described in more detail in Annex 2 (page 42).

Key Audit Results

Financial instruments (loans, guarantees, venture capital investments) are managed partially efficiently in the context of the state aid, as there is a need to improve needs and impact assessments of financial instruments, to assess the potential impact of subsidies and grants already in place or planned, and to ensure that, where money is temporarily available, it is used for other financial instruments or public activities.

[1] Regulations of the Ministry of Finance of the Republic of Lithuania, approved by Government Resolution No 1088 of 8 September 1998, paragraph 7.2.

Independent prudential oversight of the management of the risks assumed by incentive finance would help to ensure the proper implementation of these activities.

1. Consolidation of national promotional institutions allows to increase funding for priority activities

✓ The National Progress Plan 2021-2030 envisages promoting 10 priority areas, all of which are promoted (Sub-section 1.1, page 13).

✓ After the consolidation of the four[2] national promotional institutions in 2023, the national development bank ILTE UAB:

- implements the consolidation objectives (one-stop shop; international visibility; strong partnership with sectoral ministries; mobilisation of resources; attraction of large international investors; increasing investment potential in strategically important areas) and pursues the activities in line with the new ILTE Strategic Plan for 2025-2030[3];
- integrated the State's objectives and expectations set out on 30 July 2024[4] into the Strategic Action Plan 2025-2030, but did the following important objectives were not included: to consolidate financial instruments and exploit synergies between them; to assess the feasibility of launching promotional finance activities abroad. Without these objectives, no actions will be envisaged to achieve them;
- set a strategic objective in the above-mentioned Strategic Action Plan to increase the volume and accessibility of funding, ensuring that financial instruments reach as many beneficiaries as possible. To this end, the company's activities are to be expanded, with a view to financing them with own money from the company's balance sheet, by attracting more private investment through the securitisation[5] of loans. In this context, this expansion will have an impact on public debt.

The implementation of the new Strategic Action Plan of ILTE UAB may have a significant impact on the State budget and society. Decisions taken by the company must be justified and coordinated and their implementation monitored (Sub-section 1.3, page 20).

2. Independent prudential oversight of the management of the risks assumed by incentive finance needs to be improved

✓ 5 (out of 6[6]) institutions operating in France, Germany, Poland and Slovenia have similar activities to those of ILTE UAB and are subject to independent prudential

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[2] Investment and Business Guarantees UAB, Agricultural Loan Guarantee Fund UAB, Public Investment Development Agency UAB, Public Investment management Agency UAB.

[3] Decision No 2 of the Supervisory Board of ILTE UAB of 14 January 2024.

[4] Letter No 1K-260, approved by Order No 1K-260 of the Minister of Finance of 30 July 2024, "On the State's Objectives and Expectations for the Investments and Business Guarantees UAB and its Group of Companies".

[5] "Securitisation is the process by which a credit institution combines several types of financial assets (such as loans) and converts them into liquid financial securities (such as bonds) and sells them on the capital markets through a company set up specifically for securitisation. Investors who buy such securities are entitled to the cash flows generated by the loans or other financial assets pooled in the securitisation. They can sell the securities they have bought to other investors at any time. Internet access: https://www.lba.lt/lt/apie-mus/asociacijos-naujienos/lietuvos-banku-asociacija-rinkai-pristato-finansinio-turto-sekiuritizacijos-gaires (žiūrėta 2024-12-09).

[6] Bpifrance, Kreditanstalt für Wiederaufbau (KfW), Landwirtschaftliche Rentenbank, Bank Gospodarstwa Krajowego (BGK), Slovenska izvozna in razvojna banka (SID Bank).

oversight. In Lithuania, no prudential oversight of ILTE's UAB activities has been carried out for the period 2021-2024. National regulation provides for prudential oversight only for financial institutions that provide licensed financial services as defined in the Law on Banks and the Law on Payments. The Bank of Lithuania, which is indicated in the Law on the National Development Bank as a supervisory authority, is responsible for the inclusion of the institution in the list of institutions of the same status, the examination of managers, and the assessment of internal control. ILTE UAB carries out monthly and quarterly assessments of the credit risks of the portfolios, assets and cash liquidity of the funds and does not provide any information to external institutions regarding its activities or prudential oversight. Insufficient independent oversight may not ensure proper management of the risks incurred by ILTE's incentive funding (Sub-section 1.4, page 23).

- ✓ The Law of the National Development Bank provides for the possibility for ILTE UAB to finance its activities with equity. ILTE's Strategic Plan 2025-2030 foresees the expansion of the company's activities, aiming at at least 50% of the total financing of the institution with own funds. Such activities of ILTE UAB will be subject to risks inherent to credit institutions, which require adequate independent oversight (Sub-section 1.4, page 23).

3. 60% of the funding allocated to financial instruments has not been used to finance them

- ✓ The 30 financial instruments under implementation assessed by the auditors have a planned allocation of EUR 5311.8 million, of which EUR 3271.6 million (or 62%)[7] has not yet been distributed to the final beneficiaries. EUR 987.7 million (60% of the EUR 1652.4 million) of the funding allocated to the 10 funds of funds under these instruments was invested in fixed-term deposits and securities[8] as decided by ILTE UAB. The investment activities generated income of EUR 45.5 million in the first 9 months of 2024. The opportunity to invest temporarily free money arises when funding for the instruments is obtained before contracts with applicants are concluded. The European Union's temporarily unrestricted cash may not be allocated elsewhere, except for investment in fixed-term deposits or government securities. Other money raised from the State budget and from third countries is not subject to this requirement. The absence of a legal framework for the allocation of temporarily unused money (other than money subject to European Union regulation) in the context of the implementation of financial instruments does not ensure that the State's monetary resources are used optimally to achieve its objectives (Sub-section 2.1, page 26

4. The planning, monitoring and impact assessment of financial instruments to be improved

- ✓ Planning of financial instruments requires attention:

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[7] Data as at 30 September 2024.

[8] Provided for in the Rules on the Investment of Temporarily Available State Monetary Resources, approved by Order No 49 of the Minister of Finance of 28 February 2001 (as of 17 September 2024 - in accordance with the procedure for the investment of temporarily available funds as specified in the Order of the Minister of Finance of 8 May 2023, No 1K-180, On the Implementation of the Law of the Republic of Lithuania on the State Treasury of the Republic of Lithuania).

- 47% (14 out of 30) of the financial instruments under implementation have insufficient justification in the need or ex ante evaluation documents: only the purpose of the instrument and/or the funding projection is given, and there is no explanation of the identified funding gap and need. Inadequate justification of these assessments may result in financial instruments being designed without taking into account real market conditions and with limited impact on the target groups (Sub-section 1.1, page 13);

- None of the 30 financial instruments assessed by the auditors in their needs assessments included an assessment of the potential impact of subsidies and grants already in place or planned on the planned financial instruments. In addition to the financial instruments implemented by ILTE UAB, ministries provide similar aid in the form of grants, which compete with financial instruments. In the period 2021-2024, 1 684 entities benefited from both the financial instruments assessed and aid from other sources, and received other state aid amounting to EUR 642.6 million. Without assessing the impact of other state aid and creating financial instruments that are essentially equivalent to other forms of the state aid already in place or planned, the appropriateness of financial instruments will not be ensured (Sub-section 1.1, page 13)

✓ Monitoring of financial instruments needs improvement:

- 7 (out of 8 assessed) ministries'[9] documents include progress targets, measures, and indicators related to financial aid/incentive, but their achievement is not monitored. Without monitoring the indicators for incentive finance activities, the benefits and economic impact of these activities are not assessed

- Supervisory committees are set up to oversee the management of the funds of funds. ILTE UAB submitted progress reports on the implementation of the financial instruments during the period 2021-2024 to these committees, but the committees did not consider issues related to discrepancies between the funding allocated to a financial instrument and the funding used. Thereby, opportunities for action in the context of the decreasing intensity of the financial instrument are missed. The Ministries indicated that they had not taken decisions on the modification of the financing of financial instruments other than those proposed by the Supervisory Committees (Sub-section 1.2, page 18).

✓ No economic impact assessments have been carried out on the achievement of the objectives of the 3 financial instruments completed in Q3 2021-2024. Without evaluating the financial instruments, it is difficult to determine at the end of the financial instruments whether they have achieved their objectives or whether they have covered a market shortfall (Sub-section 1.2, page 18).

5. Financial instruments promote business, the public sector and agriculture, but there is scope for making them more efficient

✓ Assessment of beneficiaries of financial instruments needs to be improved:

- the final beneficiaries of financial instruments are eligible, and the creditworthiness of the beneficiary is taken into account when deciding whether to grant financing. In

[9] Ministries of Environment, Economy and Innovation, Energy, Finance, Culture, Social Security and Labour, Agriculture.

2 (out of 3) financial instruments, we found cases where the decision to grant financing was made in cases where the beneficiary's risk profile was high and additional risk management measures were applied (beneficiary's promissory note, pledge of other assets, letter of guarantee or surety from a financial institution) (Sub-section 2.2, p. 27);

- In 5 financial instruments, the time allowed for the evaluation of an application has been exceeded in between 3% and 95% of the evaluations. The Billion for Business instrument does not have a deadline for the evaluation of applications and no contracts were signed within 5 months (until 30 September 2024). When ILTE UAB asks applicants to clarify the data submitted or to provide additional information and does not set a maximum time limit for the submission of documents and/or clarifications, the overall duration of the evaluation of the application may be 3 months or more. Lengthy evaluation of applications may result in the aid not being granted at the time when it is most needed (Sub-section 2.2, page 27).

✓ Financial intermediaries have implemented 14 of the 30 financial instruments assessed by the auditors. All participating intermediaries were assessed according to the requirements set out in the Financial Intermediaries' Terms of Reference. ILTE has implemented actions to strengthen the supervision of financial intermediaries: 8 inspections were carried out between 2023 and 2024, which also included financial intermediaries; as of June 2024, reports on the supervision of financial intermediaries were launched, which identify irregularities detected by the financial intermediaries, and are discussed at the ILTE Board; and the internal audit of ILTE has been used for the supervision of the financial intermediaries (Sub-section 2.3, page 31).

✓ On 30 September 2024, ILTE UAB administered the debts of 11 financial instruments, which increased by 30.5% (from EUR 31.3 million to EUR 40.8 million) in the first 9 months of 2024, with the largest part of the amount represented by the debts of insolvent customers (45.5%). 5 (out of 11) instruments have an acceptable loss rate in their financing agreements; one instrument exceeded it by 0.14 percentage points. In 10 of the 15 cases examined, debt recovery actions took on average between 64 and 143 days longer than expected. Financial intermediaries provide ILTE with information on the problem debts they manage. 163 out of 268 (61%) of these debts were incurred 90 calendar days or more ago. Delays in recovery actions or takeover of debts have a negative impact on proper debt administration and risk management (Sub-section 2.4, page 32).

Changes during the Audit

A new debt recovery and administration procedure has been adopted by order of the Director General of ILTE UAB dated 21 November 2024, which specifies the department responsible for debt recovery and administration, the specific deadlines and the sequences of procedures. Intervals between notifications and the filing of a claim have been defined to reduce the time needed to manage debts.

Recommendations

To the Ministry of Finance

1. To adequately manage the risks of the incentive financing of ILTE UAB, improve the independent prudential oversight of compliance with the internal risk management and control measures and/or requirements of ILTE UAB's activities (establish requirements for operational risk management and supervisory procedures, capital adequacy and liquidity ratios, procedures for their monitoring, etc.) (Audit result 2).

2. To improve the efficient use of money from the State budget (excluding money subject to European Union regulation), to provide the conditions (legal basis) for decisions on the use of temporarily available money for other financial instruments (Audit result 3).

3. To ensure the efficient use of financial instruments, ensure that needs or ex ante evaluations assess compatibility with other state aid (grants and subsidies) in a way that promotes the use of the financial instrument being developed and does not compete with it (Audit result 4).

4. To assess the efficiency of the use of financial instruments and the achievement of the intended objectives, set up to carry out an assessment of the benefits of the financial instruments, the achievement of the objectives, and the impact on the market (Audit result 4).

To ILTE UAB

5. To speed up the distribution of the funding allocated to financial instruments, the following should be established:

   5.1. the target deadlines for the evaluation of applications for all financial instruments;

   5.2. the target deadlines for the applicant for clarification of the information provided by the applicant or for the provision of additional information (Audit result 5).

We have submitted written proposals to the Ministry of Finance and to ILTE UAB on the content and frequency[10] of reporting on the implementation of the financial instruments to the Ministries. We drew ILTE's attention to the oversight[11] of the final beneficiaries involved in social impact projects.

The measures and timeframes for the implementation of the recommendations, the expected impact of the audit and the indicators for measuring change are set out in the report under the heading 'Plan for the implementation of the recommendations' (Plan, page 35). Up-to-date information on the status of implementation of the recommendations, results and developments is published in open data, on the website of the National Audit Office at: https://www.valstybeskontrole.lt/LT/AtviriDuomenys.

[10] Letter No SD-(210-9.3.1-E-6224)-263 of the National Audit Office of 3 April 2025 "On the findings of the public audit".

[11] Letter No SD-(210-9.3.1-E-6224)-262 of the National Audit Office of 3 April 2025 "On the findings of the public audit".