

TRANSGAZ SA

**FINANCIAL STATEMENTS FOR THE THREE
YEARS ENDED 31 DECEMBER 2006**

**PREPARED IN ACCORDANCE WITH
INTERNATIONAL FINANCIAL REPORTING
STANDARDS**

TRANSGAZ SA

FINANCIAL STATEMENTS

31 DECEMBER 2006

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GENERAL INFORMATION

Description of the business

The National Company for Transportation of Natural Gas – SNTGN Transgaz SA (“the Company”) is a company involved in the transportation and sale of natural gas.

Establishment of the Company; reorganisation of the Romanian gas sector

In accordance with Government Decision No 334 published on 4 May 2000, the gas sector in Romania was reorganized. The shares held by the former Romgaz SA in its subsidiaries were transferred to the Ministry of Industry and Trade and, as a consequence, the following independent companies were established:

- Transgaz SA, in charge with the transportation of natural gas from the producers to the distribution companies, the successor entity of Romgaz SA;
- Exprogaz SA, a natural gas exploration, production and storage company, incorporating the activities of the former Exprogaz Medias and Exprogaz Targu Mures;
- Depogaz SA, a natural gas exploration, production and storage company, the successor entity of Exprogaz Ploiesti SA;
- Distringaz Nord SA, a gas distribution company covering the northern half of the country;
- Distringaz Sud SA, a gas distribution company covering the southern half of the country.

The Romanian Gas Industry was further re-organized through Government Decision No 575 published on 27 June 2001. According to this decision, SNGN Romgaz SA was established through the merger of Exprogaz SA Mediaş and Depogaz SA Ploieşti.

Information on the natural gas sector

The gas sector is regulated by the National Agency for Regulation of the Natural Gas Sector (“Agenția Națională pentru Reglementare în Domeniul Gazelor Naturale” - ANRGN) which was incorporated through the Government Ordinances 60/2000 and 41/2000. The main responsibilities of ANRGN are the following:

- issuance or withdrawal of licenses for companies operating in the natural gas sector;
- publication of framework contracts for sale, transport, acquisition and distribution to end users of natural gas;
- setting criteria, requirements and procedures related to the selection of eligible customers;
- setting pricing criteria and computation methods for the natural gas sector.

GENERAL INFORMATION

Description of the business (continued)

In view of the EU accession agreements concluded by Romania, ANRGN coordinates an internal gas market liberalization process; this is scheduled to be completed in 2007. The completion of the liberalization process is not expected to have a significant impact on the Transgaz's operations and profitability because the Company is already providing gas transportation to all the significant consumers in the market and barriers to entry in the gas transportation market are very high.

Starting in May 2007, ANRGN became part of the National Agency for Regulation of the Energy Sector which will regulate both gas and electrical power sector.

Ownership

Prior to 2005, the Ministry of Economy and Commerce was the sole shareholder of the Company. During 2005, based on Law 247/2005 the Ministry contributed 15% of the shares of the Company to the establishment of "Proprietatea" Fund. The Fund was set up with assets (primarily securities in large state-owned enterprises) contributed by the Romanian State; shares in the Fund will be provided to individuals dispossessed by the State in the Communist period, in lieu of in-kind compensation.

The Company is in course of a listing process which is planned to be completed by the end of 2007 and following which approximately 10% of the Company's shares will be listed on the Bucharest Stock Exchange.

Statutory information of the Company

The registered office of the Company is I.C. Motas Square Nr 1, Medias, Romania.

Employees

The average number of employees for the years ended 31 December 2006, 2005 and 2004 was 4,838, 4,755 and 4,674 respectively.

Nature of operations

Transgaz SA is involved in the following activities:

- transportation and dispatch of natural gas, which is the core activity of the Company;
- maintenance and operation of the national gas transportation system;
- import and re-sale of natural gas;
- international transit of natural gas;
- research and design in the field of equipment for the natural gas industry.

GENERAL INFORMATION

Description of the business (continued)

Management structure

The persons who served office during the year were the following:

<u>Position</u>	<u>Name</u>	<u>Period</u>
General Manager	Muntean Florin	1 January 2006 – 31 December 2006
Economic Deputy General Manager	Goage Laurentia	1 January 2006 – 31 October 2006
Technical Deputy General Manager	Pintican Juga L Traian	1 January 2006 – 31 December 2006
Finance and Budgeting Director	Marin Dumitru	1 January 2006 – 31 December 2006

REPORT OF THE AUDITORS TO THE SHAREHOLDERS OF TRANSGAZ SA

- 1 We have audited the accompanying financial statements of Transgaz SA (the "Company") which comprise the balance sheet as of 31 December 2006 and the income statement, statement of changes in equity and cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

- 2 Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

- 3 Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.
- 4 An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements

in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.

- 5 An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
- 6 We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Basis for Qualified Opinion


- 7 As discussed in note 8 to the financial statements, due to the lack of audited financial information prepared in accordance with International Financial Reporting Standards for a company controlled by Transgaz SA, the respective investment is recorded at cost less impairment. This practice is not in accordance with the requirements of IAS 27 "Consolidated and Separate Financial Statements", which requires that investments in subsidiaries should be consolidated.

Qualified Opinion

- 8 In our opinion, except for the possible effects of the matter presented in paragraph 7, the accompanying financial statements present fairly, in all material respects, the financial position of Transgaz SA as of 31 December 2006, and its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards.

Other Matters

- 9 This report, including the opinion, has been prepared for and only for the Company's shareholders as a body and for no other purpose. To the fullest extent permitted by law, we do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come.


PricewaterhouseCoopers Audit SRL



Bucharest, 16 July 2007

TRANSGAZ SA

BALANCE SHEET

31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

	Note	31 December 2006	31 December 2005	31 December 2004
ASSETS				
Non-current assets				
Intangible assets	8	11,131	10,549	11,499
Property, plant and equipment	6	2,619,675	2,602,485	2,521,865
Available for sale financial assets	9	<u>3</u>	<u>1,160</u>	<u>1,159</u>
		2,630,809	2,614,194	2,534,523
Current assets				
Inventories	10	36,204	37,559	40,117
Trade and other receivables	11	161,433	151,159	132,626
Cash and cash equivalents	12	<u>79,259</u>	<u>66,186</u>	<u>54,794</u>
		276,896	254,904	227,537
Total assets		<u>2,907,705</u>	<u>2,869,098</u>	<u>2,762,060</u>
EQUITY AND LIABILITIES				
Shareholders' equity				
Share capital	13	545,249	545,222	545,123
Public property reserve	14	1,265,797	1,265,797	1,265,797
Retained earnings		<u>471,793</u>	<u>387,855</u>	<u>350,450</u>
		2,282,839	2,198,874	2,161,370
Non-current liabilities				
Long term borrowings	15	130,071	186,345	200,845
Long term income tax payable	17	-	-	2,155
Provision for employee benefits	22	11,452	11,278	10,443
Deferred income	16	49,144	15,895	7,730
Deferred tax liability	18	<u>131,627</u>	<u>147,488</u>	<u>164,458</u>
		322,294	361,006	385,631
Current liabilities				
Trade and other payables	19	218,726	210,052	107,247
Current income tax liabilities		16,859	4,110	21,957
Short term borrowings	20	65,709	82,087	73,381
Provision for liabilities and charges	21	<u>1,278</u>	<u>12,969</u>	<u>12,474</u>
		302,572	309,218	215,059
Total liabilities		<u>624,866</u>	<u>670,224</u>	<u>600,690</u>
Total equity and liabilities		<u>2,907,705</u>	<u>2,869,098</u>	<u>2,762,060</u>

These financial statements have been approved for issue by the Board of Directors on 16 July 2007.

Ioan Rusu
General Manager



Dumitru Marin
Finance and Budgeting Director

The accompanying notes 1 to 34 are an integral part of these financial statements.

TRANSGAZ SA

INCOME STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2006
(Expressed in RON thousand, unless otherwise stated)

	Note	Year ended 31 December 2006	Year ended 31 December 2005	Year ended 31 December 2004
Revenue	22	905,760	767,188	768,777
Other income	24	<u>29,197</u>	<u>13,377</u>	<u>5,427</u>
		934,957	780,565	774,204
Cost of gas sold		(71,488)	(36,554)	(89,415)
Gas, materials and consumables used		(179,024)	(176,868)	(137,131)
Depreciation and amortisation	6; 8	(165,297)	(161,203)	(154,524)
Wages and salaries		(146,701)	(121,006)	(124,418)
Maintenance and transportation		(61,508)	(40,886)	(14,950)
Other employee benefits	28	(43,860)	(20,312)	-
Royalty expense	3.4	(42,313)	(35,851)	(33,854)
Third party services		(11,690)	(10,907)	(8,631)
Taxes and other state dues		(8,053)	(2,986)	(2,940)
Provision for liabilities and charges	21	11,691	(495)	(12,474)
Provision for employee benefits	22	(150)	(800)	(1,300)
Other operating expenses	25	<u>(40,283)</u>	<u>(34,535)</u>	<u>(34,917)</u>
Operating profit		176,281	138,162	159,650
Financial income	26	38,778	12,925	33,693
Financial expense	26	<u>(20,981)</u>	<u>(35,309)</u>	<u>(24,507)</u>
Profit before taxation		194,078	115,778	168,836
Taxation	18	<u>(32,517)</u>	<u>(19,774)</u>	<u>55,224</u>
Net profit for the period		<u>161,561</u>	<u>96,004</u>	<u>224,060</u>

Earnings per share for profit or loss attributable to the equity holders of the Company during the year (expressed in RON per share) are:

Basic and diluted	31	15.56	9.25	21.62
Dividend distribution (RON/share)	13	7.26	0.39	-

These financial statements have been approved for issue by the Board of Directors on 16 July 2007.

Ioan Rusu
 General Manager



Dumitru Marin
 Finance and Budgeting Director

The accompanying notes 1 to 34 form an integral part of these financial statements.

TRANSGAZ SA

STATEMENT OF CHANGES IN THE SHAREHOLDERS' EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

	<u>Note</u>	<u>Share capital</u>	<u>Public property reserve</u>	<u>Retained earnings</u>	<u>Total equity</u>
Balance at 1 January 2004		545,049	1,265,797	136,728	1,947,574
Share capital increase	13	74	-	-	74
Profit for the year		-	-	224,060	224,060
Tax and other charges on distributions ¹⁾		-	-	(10,338)	(10,338)
Balance at 31 December 2004		545,123	1,265,797	350,450	2,161,370
Share capital increase	13	99	-	-	99
Profit for the year		-	-	96,004	96,004
Tax and other charges on distributions ¹⁾		-	-	(9,116)	(9,116)
Dividends referring to 2002 previously retained		-	-	(4,000)	(4,000)
Additional distribution decided by shareholder ²⁾		-	-	(45,483)	(45,483)
Balance at 31 December 2005		545,222	1,265,797	387,855	2,198,874
Share capital increase	13	27	-	-	27
Profit for the year		-	-	161,561	161,561
Dividends		-	-	(71,389)	(71,389)
Additional distribution decided by shareholder ²⁾		-	-	(6,234)	(6,234)
Balance at 31 December 2006		<u>545,249</u>	<u>1,265,797</u>	<u>471,793</u>	<u>2,282,839</u>

Share capital includes an adjustment for inflation. This is shown separately in Note 13 together with the movements in the statutory value of share capital.

¹⁾ During 2005 and 2004, in accordance with legislation in force, the Company declared dividends of RON 78,238 and RON 91,156 to the Ministry of Economy and Commerce in respect of 2004 and 2003 respectively. According to the provisions of the Emergency Government Ordinance 137/December 2004 (note 3.10), the Company is entitled to retain and re-invest the respective dividends (net of related dividend tax). The Statement of Changes in Shareholders' Equity presents only the net movement which corresponds to the taxation on dividends.

²⁾ The Ministry of Economy and Commerce, as sole shareholder of Transgaz, has decided to require the Company an additional distribution in relation to the dividends declared and unpaid during the period 2000-2003, which management had decided to retain in the Company based on their interpretation of existing

The accompanying notes 1 to 34 form an integral part of these financial statements.

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STATEMENT OF CHANGES IN THE SHAREHOLDERS' EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

legislation. Given the substance of this additional distribution, the Company's management decided to record and present it as a movement in retained earnings (see also Note 19).

The accompanying notes 1 to 34 form an integral part of these financial statements.

TRANSGAZ SA

CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2006
(Expressed in RON thousand, unless otherwise stated)

		Year ended	Year ended	Year ended
	<u>Note</u>	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
Cash generated from operations	27	381,283	314,215	414,875
Interest paid, net		(12,870)	(13,813)	(12,769)
Income taxes paid		<u>(35,628)</u>	<u>(54,592)</u>	<u>(65,314)</u>
Net cash inflow from operating activity		332,785	245,810	336,792
Cash flow from investment activities				
Payments to acquire property, plant and equipment		(147,176)	(223,228)	(283,920)
Proceeds from disposal of property plant and equipment		20,272	(7,743)	-
Dividends received		-	32	8
Sale of financial investments		1,157	1	-
Acquisition of financial investments		<u>-</u>	<u>-</u>	<u>(233)</u>
Net cash used in investment activities		(125,747)	(230,938)	(284,145)
Cash flow from financing activities				
Dividends paid		(71,391)	-	(32,960)
Proceeds from long term borrowings		-	6,562	9,937
Repayments of long term borrowings		<u>(104,678)</u>	<u>(13,849)</u>	<u>(50,150)</u>
Net cash used in financing activities		(176,069)	(7,287)	(73,173)
Net change in cash and cash equivalents		30,969	7,585	(20,526)
Cash and cash equivalents at the beginning of the year	12	<u>29,970</u>	<u>22,385</u>	<u>42,911</u>
Cash and cash equivalents at the end of the year	12	<u>60,939</u>	<u>29,970</u>	<u>22,385</u>

The accompanying notes 1 to 34 form an integral part of these financial statements.

TRANSGAZ SA

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

1 REPORTING ENTITY

These financial statements are presented by TRANSGAZ SA (the "Company").

2 BASIS OF PRESENTATION OF THE FINANCIAL STATEMENTS

2.1 Basis of preparation

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). They are not the statutory accounts of the Company.

The Company maintains its accounting records in RON and prepares its statutory financial statements in accordance with the Regulations on Accounting and Reporting of Romania. These IFRS financial statements are based on the statutory records, with adjustments and reclassifications recorded for the purpose of fair presentation in accordance with IFRS.

The financial statements have been prepared using the historical cost convention, except as disclosed in the accounting policies below.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Company's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 5.

Standards, amendments and interpretations effective in 2006 but not relevant

The following standards, amendments and interpretations are mandatory for accounting periods beginning on or after 1 January 2006 but are not relevant to the Company's operations:

- IAS 21 (Amendment), Net Investment in a Foreign Operation;
- IAS 19 (Amendment), Employee Benefits
- IAS 39 (Amendment), Cash Flow Hedge Accounting of Forecast Intragroup Transactions;
- IAS 39 (Amendment), The Fair Value Option;
- IAS 39 and IFRS 4 (Amendment), Financial Guarantee Contracts;
- IFRS 1 (Amendment), First-time Adoption of International Financial Reporting Standards;
- IFRS 6 (Amendment), Exploration for and Evaluation of Mineral Resources;
- IFRIC 6, Liabilities arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment;
- IFRIC 4, Determining whether an Arrangement contains a Lease; and
- IFRIC 5, Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds.

2 BASIS OF PRESENTATION OF THE FINANCIAL STATEMENTS (CONTINUED)

Standards and interpretations to existing standards that are not yet effective and have not been early adopted by the Company

The following standards and interpretations to existing standards have been published and are mandatory for the Company's accounting periods beginning on or after 1 May 2006 or later periods that the Company has not early adopted:

- IFRIC 8, Scope of IFRS 2 (effective for annual periods beginning on or after 1 May 2006). IFRIC 8 requires consideration of transactions involving the issuance of equity instruments – where the identifiable consideration received is less than the fair value of the equity instruments issued – to establish whether or not they fall within the scope of IFRS 2. The Company will apply IFRIC 8 from 1 January 2007, but its adoption is not expected to have any impact on the Company's accounts;
- IFRIC 10, Interim Financial Reporting and Impairment (effective for annual periods beginning on or after 1 November 2006). IFRIC 10 prohibits the impairment losses recognised in an interim period on goodwill, investments in equity instruments and investments in financial assets carried at cost to be reversed at a subsequent balance sheet date. The Company will apply IFRIC 10 from 1 January 2007, but its adoption is not expected to have any impact on the Company's accounts;
- IFRS 7, Financial Instruments: Disclosures, and the complementary Amendment to IAS 1, Presentation of Financial Statements – Capital Disclosures introduces new disclosures relating to financial instruments. This standard is not expected to have any impact on the classification and valuation of the Company's financial instruments.
- IFRS 8, Operating Segments, sets out requirements for disclosure of information about an entity's operating segments and also about the entity's products and services, the geographical areas in which it operates, and its major customers. The standard is effective for annual periods beginning on or after 1 January 2009. The Company management has decided not to early adopt this standard and estimates that its adoption will have no impact on the Company's presentation of segment information.
- IFRIC 11, Group and Treasury Share Transactions, clarifies the accounting treatment for:
 - i. share-based payment transactions in which an entity receives services as consideration for its own equity instruments;
 - ii. transactions where a parent grants rights to its equity instruments to the employees of its subsidiary; transactions where a subsidiary grants rights to equity instruments of its parent to its employees. The standard is effective for annual periods beginning on or after 1 March 2007. The Company will apply IFRIC 11 from 1 January 2007, but its adoption is not expected to have any impact on the Company's accounts;

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

2 BASIS OF PRESENTATION OF THE FINANCIAL STATEMENTS (CONTINUED)

- IAS 23, Borrowing Costs, revised. The revision to IAS 23 is principally concerned with the elimination of one of the two treatments that exist for borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset. Thus, the revised standard eliminates the option of immediate recognition of such borrowing costs as an expense. The standard is effective for annual periods beginning on or after 1 January 2009. The Company will apply the revised standard from 1 January 2007, but its adoption is not expected to have any impact on the Company's accounts.
- IFRIC 12, Service Concession Arrangements, gives guidance on the accounting by operators for public-to-private service concession arrangements. The interpretation is effective for annual periods beginning on or after 1 January 2008, and will not be early adopted by the Company. IFRIC 12 applies to certain property, plant and equipment which is part of the national gas transportation system. The respective assets were constructed by the Company after it concluded a concession agreement to operate the national gas transportation pipeline system. Management estimates that the adoption of IFRIC 12 would impact :
 - i. property, plant and equipment with a net book value of RON 122,113 will be re-classified as intangible assets, their carrying value will be re-assessed and their amortisation period will be adjusted to the lower of their useful lives (3 to 24 years) and the remaining period of the concession agreement (25 years from 2008);
 - ii. revenue and cost recognised in each period presented in FS;
 - iii. recognition of the provision resulting from the contractual obligation to restore or maintain infrastructure.

The management is currently assessing the full impact of the adoption of IFRIC 12 on the Company's financial statements.

- IFRIC 13, Customer Loyalty Programmes, addresses the accounting treatment for customer loyalty award credits that:
 - i. an entity grants to its customers as part of a sales transaction, ie a sale of goods, rendering of services or use by a customer of entity assets; and
 - ii. subject to meeting any further qualifying conditions, the customers can redeem in the future for free or discounted goods or services.

This interpretation is applicable for annual periods beginning on or after 1 July 2008. The management considers that its adoption is not expected to have any impact on the Company's financial statements.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

2 BASIS OF PRESENTATION OF THE FINANCIAL STATEMENTS (CONTINUED)

Interpretations to existing standards that are not yet effective and not relevant for the Company's operations

The following interpretations to existing standards have been published that are mandatory for the accounting periods beginning on or after 1 May 2006 or later periods but are not relevant for the Company's operations:

- IFRIC 7, Applying the Restatement Approach under IAS 29, Financial Reporting in Hyperinflationary Economies (effective from 1 March 2006). IFRIC 7 provides guidance on how to apply requirements of IAS 29 in a reporting period in which an entity identifies the existence of hyperinflation in the economy of its functional Currency, when the economy was not hyperinflationary in the prior period. As the Company does not have the Currency of a hyperinflationary economy as its functional Currency, IFRIC 7 is not relevant to the Company's operations; and
- IFRIC 9, Reassessment of embedded derivatives (effective for annual periods beginning on or after 1 June 2006). IFRIC 9 requires an entity to assess whether an embedded derivative is required to be separated from the host contract and accounted for as a derivative when the entity first becomes a party to the contract. Subsequent reassessment is prohibited unless there is a change in the terms of the contract that significantly modifies the cash flows that otherwise would be required under the contract, in which case reassessment is required. As the Company has not concluded contracts with embedded derivative, IFRIC 9 is not relevant to the Company's operations.

2.2 Accounting for the effect of hyperinflation

Romania has previously experienced relatively high levels of inflation and was considered to be hyperinflationary as defined by IAS 29 "Financial Reporting in Hyperinflationary Economies" ("IAS 29"). IAS 29 requires that the financial statements prepared in the currency of a hyperinflationary economy be stated in terms of the measuring unit current at the balance sheet date. As the characteristics of the economic environment of Romania indicate that hyperinflation has ceased, effective from 1 January 2004 the Company no longer applies the provisions of IAS 29. Accordingly, the amounts expressed in the measuring unit current at 31 December 2003 are treated as the basis for the carrying amounts in these financial statements.

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NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

2 BASIS OF PRESENTATION OF THE FINANCIAL STATEMENTS (CONTINUED)

The restatement was calculated using the conversion factors derived from the Romanian Consumer Price Index ("CPI"), published by the Comisia Nationala de Statistica. The indices used to restate corresponding figures, based on 1998 prices (1998 = 100) for the five years ended 31 December 2003, and the respective conversion factors are:

<u>Year</u>	<u>Movement in CPI</u>	<u>Indices</u>	<u>Conversion Factor</u>
1999	54.8%	1.548	2.46
2000	40.7%	2.178	1.75
2001	30.3%	2.838	1.35
2002	17.8%	3.343	1.14
2003	14.1%	3.815	1

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

3.1 Intangible assets

Computer software

Acquired computer software licenses are capitalized on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortized over their estimated useful lives (three years). Costs associated with developing or maintaining computer software are recognized as an expense as incurred.

3.2 Property, plant and equipment

Buildings comprise mainly buildings ancillary to operating assets (e.g. buildings housing pumping stations, gas treatment stations etc.), a research centre and office buildings. Transportation system assets consist of the assets comprising the national gas pipeline transportation system (e.g. pipelines, compressors, gas filters, measuring devices etc.). Property, plant and equipment are stated at cost, restated to the equivalent purchasing power of the Romanian Leu at 31 December 2003 for assets acquired prior to 1 January 2004, less accumulated depreciation and provision for impairment, where required.

Items acquired after 1 January 2004 are stated at cost less accumulated depreciation and provision for impairment, where required.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Assets in course of construction are capitalized and will be depreciated over the useful life of the asset, from the date when they are available for use.

Depreciation on other assets is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, as follows:

	<u>Years</u>
Buildings	50
Assets in the gas transportation system	20 - 50
Other fixed assets	4 - 20

Land and assets in course of construction are not depreciated.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 3.3).

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the income statement.

3.3 Impairment of non-financial assets

Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. An impairment loss recognised for an asset in prior periods is reversed if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial

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FOR THE YEAR ENDED 31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

assets that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

TRANSGAZ SA

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

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3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.4 Public property assets

In accordance with the Public Property Law 213/1998, gas transportation pipelines represent state property. Government Decision 491/1998, as confirmed in Government Decision 334/2000, specifies that fixed assets with a statutory gross book value of RON 499,726 (at 31 December 2006 a statutory gross book value of RON 490,809 and a restated net book value of RON 541,449) representing gas pipelines are to be administered by the Company. Therefore, the Company has the exclusive right to use these assets over the concession period and will return them to the State at the end of the period (see Note 7). The Company receives the majority of the benefits associated with the assets and is exposed to the majority of risks, including the requirement to maintain the network assets over a period which is at least equal to their remaining useful life, and the Company's financial performance is directly linked to the condition of the network system. Consequently, the Company has recognized these assets in its balance sheet, together with a corresponding reserve in equity.

As per the Public Concession Law 219/1998, a royalty must be paid in respect of public property assets which are administered by companies other than state bodies. In accordance with the Concession Agreement signed by the Company with the National Agency for Mineral Resources ("ANRM") in May 2002 (the "Concession Agreement"), further described in note 7, and approved by the Government Decision 668 /20 June 2002, the royalty to be paid in respect of public property assets has been set for the period 2002 – 2032 at the level of 5% of the revenues from gas transportation and transit. The duration of the concession agreement is of 30 years.

As detailed at Note 2.1, the Company decided to not early adopt IFRIC 12. Public property assets are excluded from the scope of IFRIC 12 as they were used and recorded as property, plant and equipment on the Company's balance sheet before the service concession Agreement was entered into. The Company will continue to apply the current accounting treatment to these assets after adoption of IFRIC 12.

3.5 Financial assets

The Company classifies its financial assets in the following categories: at fair value through profit or loss, loans and receivables, and available for sale. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition and re-evaluates this designation at every reporting date.

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3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(a) *Financial assets at fair value through profit or loss*

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management. Derivatives are also categorised as held for trading unless they are designated as hedges. Assets in this category are classified as current assets if they are either held for trading or are expected to be realised within 12 months of the balance sheet date. During the period the Company did not hold any trading or fair value through profit or loss financial assets.

(b) *Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the balance sheet date. These are classified as non-current assets. Loans and receivables are classified as 'trade and other receivables' in the balance sheet (Note 3.7).

(c) *Available-for-sale financial assets*

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the investment within 12 months of the balance sheet date.

Regular purchases and sales of investments are recognised on trade-date – the date on which the Company commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss.

Financial assets carried at fair value through profit or loss are initially recognised at fair value and transaction costs are expensed in the income statement. Investments are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership. Available for-sale financial assets and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables and held-to-maturity investments are carried at amortised cost using the effective interest method.

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3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Gains or losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss' category, including interest and dividend income, are presented in the income statement in the period in which they arise.

Gains or losses arising from changes in the fair value of the 'available-for-sale financial assets' are recognised in equity.

When securities classified as available-for-sale are sold or impaired, the accumulated fair value adjustments recognised in equity are included in the income statement as 'gains and losses from investment securities'. Interest on available-for-sale securities calculated using the effective interest method is recognised in the income statement. Dividends on available-for-sale equity instruments are recognised in the income statement when the Group's right to receive payments is established.

For unlisted equity shares, the Company establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, and option pricing models making maximum use of market inputs and relying as little as possible on entity-specific inputs. When it is impracticable to determine the fair value, the company estimates the impairment of such shares based on the financial condition of the entity in which it holds shares.

The Company assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity securities classified as available for sale, a significant or prolonged decline in the fair value of the security below its cost is considered as an indicator that the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement. Impairment testing of trade receivables is described in Note 3.7.

3.6 Inventories

Inventories are stated at the lower of restated cost and estimated net realizable value. Cost is calculated on a weighted average cost basis. Where necessary, provision is made for slow moving and obsolete inventories in order to arrive at the net realizable value. Obsolete or defective inventories identified individually are provided for in full or written-off. For slow moving inventories, an estimation of the age of inventories based on their turnover is made for each main category; inventories older than one year are provided in full.

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3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.7 Trade receivables

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments (more than 60 days overdue) are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in the income statement within selling and marketing costs. When a trade receivable is uncollectible it is written off against the allowance account for trade receivables.

3.8 Value added tax

Value added tax (VAT) is payable to the Tax Authorities based on the monthly VAT return by the 25th of the following month irrespective of collection of receivables from customers. The Fiscal Authorities permit the settlement of VAT on a net basis. When input VAT is higher than output VAT, the difference is refundable at the Company's request. The VAT refund may be made after a tax inspection is performed or without a tax inspection, if certain conditions are met. VAT related to sales and purchases which has not been settled at the balance sheet date is recognised in the balance sheet on a net basis and disclosed as a current asset or liability. Where provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

The related VAT needs to be paid to the State and can only be recovered after the debtor is declared bankrupt.

3.9 Cash and cash equivalents

Cash and cash equivalents include cash on hand and in the bank as well as all short-term debt instruments with a maturity of less than three months. For the purposes of the cash flow statement, cash and cash equivalents are presented net of bank overdrafts. In the balance sheet, bank overdrafts are included within borrowings in current liabilities.

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NOTES TO THE FINANCIAL STATEMENTS

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3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.10 Shareholders' equity

Share capital

Ordinary shares are classified as equity. Transaction costs of an equity transaction (cost incurred in issuing its own equity instruments) are accounted for as a deduction from equity, net of any related income tax benefit. Any excess of the fair value of consideration received over the par value of shares issued is recognized as a share premium.

Dividends

Discretionary dividends are recognized as a liability and deducted from equity at the balance sheet date only if they are declared before or on the balance sheet date. Dividends are disclosed when they are proposed before the balance sheet date or proposed or declared after the balance sheet date but before the financial statements are authorized for issue.

In accordance with Government Ordinance 64/2001, companies in which the state has a majority ownership have to distribute 50% of their net profit after deduction of any contractual profit distributions to employees, as dividends to the state.

According to the provisions of the Emergency Government Ordinance 137/December 2004, approved by the Law 50/March 2005, by exception to Government Ordinance 64/2001 the Company was entitled to retain and re-invest the dividends declared for 2004 and 2003 (net of related dividend tax) to finance its major investment projects relating to the modernization and development of the natural gas transportation infrastructure. As a consequence, unpaid dividends for 2003 and 2004 were maintained in retained earnings, net of the associated dividend tax.

3.11 Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Company has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

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NOTES TO THE FINANCIAL STATEMENTS

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3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.12 Leases

Leases where a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the statement of income on a straight-line basis over the period of the lease.

3.13 Income taxes

Income taxes have been provided for in the financial statements in accordance with Romanian legislation enacted or substantively enacted by the balance sheet date. The income tax charge comprises current tax and deferred tax and is recognised in the income statement unless it relates to transactions that are recognised, in the same or a different period, directly in equity.

Current tax is the amount expected to be paid to or recovered from the taxation authorities in respect of taxable profits or losses for the current and prior periods. Taxes, other than on income, are recorded within operating expenses.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax basis of assets and liabilities and their carrying amounts in the financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

3.14 Trade and other payable

Trade and other payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

3.15 Deferred income

Deferred income is recorded for connection fees charged to customers for connecting them to the gas transportation network. The deferred income is released in the income statement over the weighted average useful life of the related assets (connection pipes, gas flow regulator, counter).

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NOTES TO THE FINANCIAL STATEMENTS

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3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.16 Employee benefits

The Company, in the normal course of business, makes payments to the Romanian State on behalf of its employees for social security, health and pension benefits. All employees of the Company are members of the Romanian State pension plan, which is a defined contribution plan. These payments are recognised within the income statement together with the salary expenses.

Benefits on retirement

Under the collective labour contract, the Company should pay to its employees at the time of their retirement an amount equal to a multiplier of their gross salary depending on the employment period in the gas industry, working conditions, etc. The Company has recorded a provision for such payments (see Note 22).

Social costs

The Company incurs employee costs related to the provision of benefits such as health services. These amounts principally represent an implicit cost of employing production workers and, accordingly, have been charged to wages and salaries costs.

Free gas

The Company is also committed through the collective labour agreement to provide current employees free of charge with certain quantities of gas or the cash equivalent (see Note 28); these amounts are charged to "Other employee benefits" in the period in which they are incurred.

3.17 Provisions

Provisions for liabilities and charges are recognised when the Company has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small. Where the Company expects a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

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NOTES TO THE FINANCIAL STATEMENTS

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3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The Company has recognised provisions in respect of legal claims and guarantees (note 21). The long term provisions have been discounted to present value using a discount rate as detailed in Note 21.

3.18 Revenue recognition

Revenues from sale of goods and services

Revenue comprises the invoiced value of gas delivered, and services for gas transportation and transit rendered, net of value-added tax, rebates and discounts.

Revenue from gas transportation and transit and from the sale of gas is recognized when the gas has been delivered and measured in accordance with contract.

Revenues are measured at the fair value of the consideration received or receivable. When the fair value of goods received in a barter transaction cannot be measured reliably, the revenue is measured at the fair value of the goods or service given up.

Interest income is recognised on a time-proportion basis using the effective interest method.

Dividends are recognised when the right to receive payment is established.

Mutual cancellation and barter transactions

A portion of sales and purchases are settled by mutual cancellations, barter or non-cash settlements. These transactions are generally in the form of direct settlements by dissimilar goods and services from the final customer (barter) or cancellation of balances through a chain involving several companies.

Sales and purchases that are expected to be settled by barter or other non-cash settlements are recognised based on the management's estimate of the fair value to be received or given up in non-cash settlements. The fair value is determined with reference to observable market information.

Non-cash transactions have been excluded from the cash flow statement, so investing activities, financing activities and the total of operating activities represent actual cash flows.

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NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.19 Foreign currency transactions

a) *Functional currency*

Items included in the financial statements of the Company are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The financial statements are presented in RON, which is the functional and presentation currency of the Company.

b) *Transactions and balances*

Monetary assets and liabilities are translated into Company's functional currency at the official exchange rate of the National Bank of Romania ("NBR") at the respective balance sheet date. Foreign currency transactions are recorded by applying to the foreign currency amount the spot exchange rate between the functional currency of the Company and the foreign currency at the date of the transaction. Foreign exchange gains and losses resulting from the settlement of the transactions and from the translation of monetary assets and liabilities into the Company's functional currency at year-end official exchange rates of the NBR are recognised in profit or loss. Translation at year-end rates does not apply to non-monetary items, including equity investments. Effects of exchange rate changes on the fair value of equity securities are recorded as part of the fair value gain or loss.

At 31 December 2006, the exchange rate communicated by the National Bank of Romania, was US Dollar ("USD") 1 = RON 2.5676 (31 December 2005: USD 1 = RON 3.1078 and 31 December 2004: USD 1 = RON 2,9067) and Euro ("EUR") 1 = RON 3.3817 (31 December 2005: EUR 1 = RON 3.6771 and 31 December 2004: EUR 1 = RON 3,9663). Exchange restrictions and currency controls exist relating to converting RON into other currencies. The RON is not a convertible currency outside of Romania.

NOTES TO THE FINANCIAL STATEMENTS

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4 FINANCIAL RISK MANAGEMENT

(i) Credit risk

Financial assets, which potentially subject Company entities to credit risk, consist principally of trade receivables. The Company has policies in place to ensure that sales of products and services are made to customers with an appropriate credit history. The carrying amount of accounts receivable, net of bad debt provision, represents the maximum amount exposed to credit risk. The Company's credit risk is concentrated in its top 5 clients, which together amount to 85% of trade receivable balance at 31 December 2006 (2005: 86%, 2004: 91%). Although collection of receivables could be influenced by economic factors, management believes that there is no significant risk of loss to the Company beyond the provision already recorded.

Cash is placed in financial institutions, which are considered at time of deposit to have minimal risk of default.

(ii) Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash and availability of funding through an adequate amount of committed credit facilities.

(iii) Interest rate risk

The Company is exposed to interest rate risk through its interest-bearing short and long-term borrowings, the majority of which are at variable rates. The Company has not entered into any arrangements to mitigate this risk. The Company has no significant interest-bearing assets.

(iv) Currency risk

The Company incurs substantial amount of foreign currency denominated long-term borrowings and is thus exposed to foreign exchange risk. Foreign currency denominated assets and liabilities give rise to foreign exchange exposure.

The Company does not have formal arrangements to mitigate currency risks of the Company's operations; consequently the Company does not apply hedging accounting. However, management believes that the Company is largely secured from foreign exchange risks as foreign currency denominated sales are used to cover repayment of foreign currency denominated borrowings.

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NOTES TO THE FINANCIAL STATEMENTS

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4 FINANCIAL RISK MANAGEMENT (CONTINUED)

(v) Fair value estimation

The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques.

The carrying value less impairment provision of trade receivables and payables are assumed to approximate their fair values. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Company for similar financial instruments.

5 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The Company makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgments are continually evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Management also makes certain judgments, apart from those involving estimations, in the process of applying the accounting policies. Judgments that have the most significant effect on the amounts recognised in the financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial year include:

5.1 Tax legislation

Romanian tax, currency and customs legislation is subject to varying interpretations. Refer to Note 33(ii).

5.2 Related party transactions

In the normal course of business the Company enters into transactions with its related parties. These transactions are priced predominantly at market rates. Judgement is applied in determining if transactions are priced at market or non-market interest rates, where there is no active market for such transactions. The basis for judgment is pricing for similar types of transactions with unrelated parties and effective interest rate analyses.

NOTES TO THE FINANCIAL STATEMENTS

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(Expressed in RON thousand, unless otherwise stated)

5 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES (CONTINUED)

5.3 Useful lives of property, plant and equipment

For the periodic review of the useful life of property, plant and equipment, the Company's management considers:

- technical obsolescence of existing equipment
- the significant investments programme reflected in the future annual capital expenditure budgets subjected to approval by the shareholders
- the application of new standards and interpretations (e.g. IFRIC 12).

In assessing the useful life for property, plant and equipment, the Company's management assumed that there will not be major technological changes in its industry requiring a substantial replacement of the existing assets used for the gas transportation activities and that its annual investment programme for future periods will be approved by the shareholders.

The management of the Company estimates that the useful lives and method of depreciation used (Note 3.2) reflect accurately the pattern in which the future economic benefits are expected to be consumed by the Company.

5.4 Impairment of property, plant and equipment

In deciding on the amount of impairment for property, plant and equipment, the Company management assumed that the assets transferred to public property assets with the view of decommissioning, as per Government Decision 1644/October 2004, will be decommissioned in the next financial period and the decision will not be cancelled by the Government. No other impairment indicators were identified by management in the periods presented.

5.5 Assumptions to determine amount of provision for retirement benefits

This provision has been computed based on the estimations of the average salary, average staff turnover, average number of salaries to be paid at the time of the retirement and the time frame when the benefits are to be paid. The provision has been discounted to its present value by applying a discount factor based on the risk free interest rate (i.e. interest rate on government bonds). If the estimated pre-tax discount rate applied to the discounted cash flows had been 1% higher than management's estimates, the Company would have recognized in its balance sheet for the year ended 31 December 2006 a provision for employee benefits 8% lower than the current one. The Company does not operate any other pension scheme or post retirement benefit plan and, consequently, has no obligation in respect of pensions.

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5 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES (CONTINUED)

5.6 Impairment of receivables

The accounting policy of the Company for impairing its receivables is to provide for all balances older than 365 days. Had the company provided all balances older than 180 days, the impairment provision for current assets would have increased by RON 3,001.

5.7 Accounting treatment for concession agreement

As further described in note 7, In May 2002, Transgaz SA has concluded a Concession Agreement with ANRM giving the Company the right to operate the major pipelines of the national gas transportation system for a period of 30 years. Before the conclusion of this agreement, the pipelines were owned by Transgaz SA. According to the clauses of the Concession Agreement, the Company receives the majority of the benefits associated with the assets and is exposed to the majority of risks. Consequently, the Company has recognized these assets in its balance sheet, together with a corresponding reserve in equity.

The management of the Company decided not to early adopt IFRIC 12, "Service Concession Arrangements", interpretation effective for annual periods beginning on or after 1 January 2008. Management estimates that the adoption of IFRIC 12 would impact:

- i. property, plant and equipment with a net book value of RON 122,113 which will be re-classified as intangible assets and their amortisation period will be adjusted to the lower of their useful lives (3 to 24 years) which is shorter than the remaining period of the concession agreement (25 years from 2008);
- ii. revenue and cost recognised in each period presented in FS;
- iii. recognition of the provision resulting from the contractual obligation to restore or maintain infrastructure.

The management is currently assessing the impact of the adoption of IFRIC 12 on the Company's financial statements.

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6 PROPERTY, PLANT AND EQUIPMENT

	<u>Land and buildings</u>	<u>Transportation system assets</u>	<u>Other fixed assets</u>	<u>Assets in course of construction</u>	<u>Total</u>
At 31 December 2003					
Cost	445,786	4,111,393	283,833	170,969	5,011,981
Accumulated depreciation	<u>(140,344)</u>	<u>(2,250,505)</u>	<u>(208,522)</u>	-	<u>(2,599,371)</u>
Net book value	<u>305,442</u>	<u>1,860,888</u>	<u>75,311</u>	<u>170,969</u>	<u>2,412,610</u>
Year ended 31 December 2004					
Opening net book value	305,442	1,860,888	75,311	170,969	2,412,610
Additions	-	-	-	284,540	284,540
Transfers from AICC	16,621	281,589	33,062	(331,272)	-
Net book value of disposals	(1,411)	-	(4,842)	-	(6,253)
Impairment charge	-	(18,302)	-	-	(18,302)
Depreciation charge	<u>(12,473)</u>	<u>(119,744)</u>	<u>(18,513)</u>	-	<u>(150,730)</u>
Closing net book value	308,179	2,004,431	85,018	124,237	2,521,865
At 31 December 2004					
Cost	460,790	4,392,981	293,031	124,237	5,271,039
Accumulated depreciation	<u>(152,611)</u>	<u>(2,388,550)</u>	<u>(208,013)</u>	-	<u>(2,749,174)</u>
Net book value	<u>308,179</u>	<u>2,004,431</u>	<u>85,018</u>	<u>124,237</u>	<u>2,521,865</u>
Opening net book value	308,179	2,004,431	85,018	124,237	2,521,865
Additions	-	-	-	242,679	242,679
Transfers from AICC	5,745	241,307	11,449	(258,501)	-
Net book value of disposals	(2,632)	(3,091)	(543)	-	(6,266)
Depreciation charge	<u>(13,554)</u>	<u>(125,314)</u>	<u>(16,925)</u>	-	<u>(155,793)</u>
Closing net book value	297,738	2,117,333	78,999	108,415	2,602,485
At 31 December 2005					
Cost	462,928	4,577,671	297,101	108,415	5,446,115
Accumulated depreciation	<u>(165,190)</u>	<u>(2,460,338)</u>	<u>(218,102)</u>	-	<u>(2,843,630)</u>
Net book value	<u>297,738</u>	<u>2,117,333</u>	<u>78,999</u>	<u>108,415</u>	<u>2,602,485</u>

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6 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

	<u>Land and buildings</u>	<u>Transportation system assets</u>	<u>Other fixed assets</u>	<u>Assets in course of construction</u>	<u>Total</u>
Opening net book value	297,738	2,117,333	78,999	108,415	2,602,485
Additions	-	-	-	184,261	184,261
Transfers from AICC	8,444	155,819	8,825	(173,088)	-
Net book value of disposals	(5,371)	(587)	(252)	-	(6,210)
Depreciation charge	<u>(13,898)</u>	<u>(128,947)</u>	<u>(18,016)</u>	<u>-</u>	<u>(160,861)</u>
Closing net book value	286,913	2,143,618	69,556	119,588	2,619,675
At 31 December 2006					
Cost	463,570	4,728,427	303,445	119,588	5,615,030
Accumulated depreciation	<u>(176,657)</u>	<u>(2,584,809)</u>	<u>(233,889)</u>	<u>-</u>	<u>(2,995,355)</u>
Net book value	<u>286,913</u>	<u>2,143,618</u>	<u>69,556</u>	<u>119,588</u>	<u>2,619,675</u>

The gross book value of fully depreciated assets still in use is RON 1,544,832 (2005: RON 1,470,703 and 2004: RON 1,359,848).

Public property assets

Included in the transportation system assets are property, plant and equipment which are part of the public property of the State and are subject to the concession agreement as follows:

Cost	Year ended 31 December 2006	Year ended 31 December 2005	Year ended 31 December 2004
1 January	2,686,874	2,686,874	2,736,495
Disposals	<u>-</u>	<u>-</u>	<u>49,620</u>
31 December	2,686,874	2,686,874	2,686,875
Depreciation			
1 January	2,089,017	2,029,300	1,996,184
Charge for the year	56,407	59,717	64,435
Impairment charge	-	-	18,301
Disposals	<u>-</u>	<u>-</u>	<u>(49,620)</u>
31 December	2,145,424	2,089,017	2,029,300
Net book value	<u>541,450</u>	<u>597,857</u>	<u>657,575</u>

TRANSGAZ SA

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

6 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

As detailed in Note 7, these assets are administrated by Transgaz SA. Public property assets can not be sold or disposed of by the Company.

In accordance with public property law (Law 213/1998) any new asset constructed by the Company which is part of the national gas transportation transfers to public property once it is fully depreciated.

The costs of dismantling and removing public property assets and restoring the site on which they are located are not an obligation of the Company.

Impairment

According to the Government Decision 1644/October 2004, public property assets with a statutory gross book value of RON 8,917 which were no longer used by the Company, were transferred to the private property of the State, with the view of either decommissioning or transferring to other entities. Any proceeds on disposal of state property are transferred to the State budget. Because at 31 December 2004 no actual decommissioning or transfer was made, the Company's management decided to book an impairment provision in amount of RON 18,301, being the restated carrying amount of the respective assets, on the basis they are no longer generating revenues for the Company. Subsequently the assets were retired.

7 SERVICE CONCESSION AGREEMENT

In May 2002, Transgaz SA has concluded a concession agreement with ANRM giving the Company the right to operate the major pipelines (trunk pipelines) of the national gas transportation system for a period of 30 years. Prior to the conclusion of this agreement, the pipelines were owned by Transgaz SA. All the modernisation or developments brought by the Company to the system are considered parts of the system and become property of the ANRM at the end of their useful life. The Company can not sell or otherwise dispose of any asset which is part of the pipeline system.

At the end of the contract, the public property assets existing at the time when the agreement was signed and all the investments made to the system will be returned to the ANRM free of charge, except for assets constructed by the Company and not fully amortised for which it will be compensated at the level of the net book value of the respective assets at the end of the concession period. The Company owns and will develop other assets that are not a direct part of the national gas pipeline transportation system, but represent complementary assets for the gas transportation operations. The ANRM has the option to buy these assets at the end of the concession agreement at fair value.

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7 SERVICE CONCESSION AGREEMENT (CONTINUED)

The main terms of the Concession Agreement are as follows:

- the Company has the right to directly operate the assets being the object of the Concession Agreement and to charge and collect the transit and transportation tariffs from its customers in exchange for the services provided; Transgaz SA is the only entity licensed to operate the major pipelines of the national gas transportation system, with no sub-concessions being allowed;
- any change in tariffs should be proposed by the Company to the ANRM and further approved by ANRGN;
- the Company is exempted from the payment of import duties for assets acquired in order to operate, improve or develop the system;
- on an annual basis, the Company should publish the available capacity of the system for the next year, by October 30;
- on an annual basis, customers' orders must be replied to by November 30, and ANRM should be informed of all the refusals decided by the Company's management;
- the Company has to maintain a specific service level (guaranteed through a minimum compulsory investment program for 2002 - 2006);
- royalties are paid as a percentage (5%) of gross revenue from operating the pipeline network (transportation and transit);
- all operating expenses for running the system are covered by the Company;
- the Company can cancel the contract by notifying the ANRM 12 months in advance;
- the ANRM can cancel the contract with 6 months advance notification; it has also the option to cancel the contract with a 30 days notification period, for "national interest" reasons; in such case, Transgaz SA will be paid compensation amounting to the average net profit for the past 5 years multiplied by the remaining life of the contract.

The Concession Agreement does not include an extension clause.

No changes in the terms of the Concession Agreement have occurred since June 2003.

TRANSGAZ SA

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8 INTANGIBLE ASSETS

	<u>Computer software</u>	<u>Intangibles in progress</u>	<u>Total</u>
At 31 December 2003			
Cost	16,311	7,009	23,320
Accumulated depreciation	<u>(10,137)</u>	<u>-</u>	<u>(10,137)</u>
Net book value	<u>6,174</u>	<u>7,009</u>	<u>13,183</u>
Year ended 31 December 2004			
Opening net book value	6,174	7,009	13,183
Additions	8,679	6,759	15,438
Disposals	-	(13,328)	(13,328)
Depreciation charge	<u>(3,794)</u>	<u>-</u>	<u>(3,794)</u>
Closing net book value	11,059	440	11,499
At 31 December 2004			
Cost	24,990	440	25,430
Accumulated depreciation	<u>(13,931)</u>	<u>-</u>	<u>(13,931)</u>
Net book value	<u>11,059</u>	<u>440</u>	<u>11,499</u>
Opening net book value	11,059	440	11,499
Additions	4,161	5,858	10,019
Disposals	-	(5,559)	(5,559)
Depreciation charge	<u>(5,410)</u>	<u>-</u>	<u>(5,410)</u>
Closing net book value	9,810	739	10,549
At 31 December 2005			
Cost	29,151	739	29,890
Accumulated depreciation	<u>(19,341)</u>	<u>-</u>	<u>(19,341)</u>
Net book value	<u>9,810</u>	<u>739</u>	<u>10,549</u>
Opening net book value	9,810	739	10,549
Additions	5,730	3,724	9,454
Disposals	-	(4,436)	(4,436)
Depreciation charge	<u>(4,436)</u>	<u>-</u>	<u>(4,436)</u>
Closing net book value	11,104	27	11,131
At 31 December 2006			
Cost	34,881	27	34,908
Accumulated depreciation	<u>(23,777)</u>	<u>-</u>	<u>(23,777)</u>
Net book value	<u>11,104</u>	<u>27</u>	<u>11,131</u>

TRANSGAZ SA

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(Expressed in RON thousand, unless otherwise stated)

9 AVAILABLE FOR SALE FINANCIAL ASSETS

Available for sale financial assets consist of unlisted equities in the following companies:

<u>Company</u>	<u>Activity</u>	<u>% Ownership</u>	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
Resial SA	manufacturing	68.16	18,116	18,116	18,116
Mebis SA	manufacturing	17.47	6,462	6,462	6,462
Wirom Gas SA	gas distribution and supply	0.02	3	2	1
Banca de Credit si Dezvoltare Romexterra SA	banking activity	-	-	1,158	1,158
Less provision for impairment of investments in Resial and Mebis			<u>(24,578)</u>	<u>(24,578)</u>	<u>(24,578)</u>
			<u>3</u>	<u>1,160</u>	<u>1,159</u>

Investment in Resial SA

The shares in Resial SA were received in December 2003 through enforced collection of receivables from Coloni Serv Com SA. Due to the absence of audited financial information prepared in accordance with IFRS, the investment is not consolidated and carried at cost less impairment provision at 100% of cost, which reflects Resial's financial condition (the company is in liquidation and Transgaz does not expect to recover any amounts on its investment).

At 31 December 2004 the Company also pledged a deposit of RON 1,000 as guarantee for a loan taken by Resial SA. A provision of 100% of this amount was also made by the Company (Note 21). During year ended 31 December 2005, the provision was reversed as the guarantee was executed during this financial period. The Company has no further obligations in respect of Resial.

TRANSGAZ SA

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

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9 AVAILABLE FOR SALE FINANCIAL ASSETS (CONTINUED)

Investment in Mebis SA

The shares in Mebis SA were received in February 2004 through forced collection of receivables from Coloni Serv Com SA. The investment is carried at cost less impairment provision at 100% of cost, which reflects Mebis's financial condition (the company is in liquidation and Transgaz does not expect to recover any amounts on its investment). The Company has no obligations in respect of Mebis SA.

Investment in Romexterra SA

During the year 2006 the Company has sold its investments in Romexterra bank towards PPF Investments for RON 2,218.

Investment in Wirom Gas SA

At 31 December 2003 the Company held 49.97% of the shares (and corresponding voting rights) in Wirom Gas SA, a joint-venture with Wintershall Erdgas Handelshaus GmbH (49.97%) and other parties (0.06%). In February 2004 the Company sold most of its shares in Wirom SA to Distrigaz Sud SA.

The joint-venture was not proportionally consolidated or equity accounted for the first two months of 2004 due to its immaterial impact on financial position and results of the Company; consequently, it was classified as an available-for-sale investment.

During year ended 31 December 2005, the Company increased its contribution to the share capital of Wirom GAS SA, in order to maintain the share of 0.02%.

10 INVENTORIES

	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
Spare parts and materials	38,245	41,195	43,753
Provisions for slow moving inventories	<u>(2,041)</u>	<u>(3,636)</u>	<u>(3,636)</u>
	<u>36,204</u>	<u>37,559</u>	<u>40,117</u>

TRANSGAZ SA

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(Expressed in RON thousand, unless otherwise stated)

11 TRADE AND OTHER RECEIVABLES

	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
Trade receivables	254,776	258,305	229,593
Advances from suppliers	14	3,531	3,965
VAT recoverable	392	1,228	8,417
Loan to Resial SA	2,235	3,068	2,432
Other receivables	3,375	2,006	1,099
Provision for impairment of receivables	(97,124)	(84,597)	(97,163)
Provision for impairment of receivables from Turnu (written off in 2006)	-	(29,314)	(13,286)
Provision for impairment of other loan to Resial SA	<u>(2,235)</u>	<u>(3,068)</u>	<u>(2,431)</u>
	<u>161,433</u>	<u>151,159</u>	<u>132,626</u>

As at 31 December 2006, RON 17,651 (31 December: RON 36,704 and 31 December 2004: RON 14,134) of net trade and other receivables are denominated in foreign currency, 77% in USD (2005: 91% and 2004: 100%) and 23% in EUR (2005: 9%).

Included in trade receivables are balances from related parties of RON 38,166 (31 December 2005: RON 36,957 and 31 December 2004: RON 67,829), as presented in Note 29.

Trade receivables have been pledged in favour of banks as collateral for bank loans as described in Note 15. The total amount of pledged receivables as at 31 December 2006 is RON 78,318 (31 December 2005: RON 57,260 and 31 December 2004: RON 58,643).

TRANSGAZ SA

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

12 CASH AND CASH EQUIVALENTS

	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
Cash at bank in RON	77,310	20,940	16,268
Cash at bank in foreign currency	1,711	45,061	38,377
Other cash equivalents	<u>238</u>	<u>185</u>	<u>149</u>
	<u>79,259</u>	<u>66,186</u>	<u>54,794</u>

As at 31 December 2006 cash at bank includes RON 1,027 (31 December 2005: RON 3,068 and 31 December 2004: RON 2,456) blocked deposits in foreign currencies and nil (31 December 2005: nil and 31 December 2004: RON 1,000) deposit pledged in favour of banks and as guarantee for a loan taken by Resial SA (Note 9).

The weighted average effective interest rate on short term bank deposits was 3.35% at 31 December 2006 (31 December 2005: 4.31% and 31 December 2004: 4.90%) and these deposits had an average maturity of 30 days.

For the purpose of the cash flow statement, the year end cash and cash equivalents comprise the following:

	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
Cash and cash equivalents	79,259	66,186	54,794
Less: Blocked cash accounts	(1,027)	(3,068)	(2,456)
Less: Bank overdrafts (Note 20)	<u>(17,293)</u>	<u>(33,148)</u>	<u>(29,953)</u>
	<u>60,939</u>	<u>29,970</u>	<u>22,385</u>

TRANSGAZ SA

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

13 SHARE CAPITAL

	<u>Number of ordinary shares</u>	<u>Share capital</u>
Statutory		
At 31 December 2003	10,363,087	103,630
Increase	<u>7,354</u>	<u>74</u>
At 31 December 2004	10,370,441	103,704
Increase	<u>9,879</u>	<u>99</u>
At 31 December 2005	10,380,320	103,803
Increase	<u>2,717</u>	<u>27</u>
At 31 December 2006	10,383,037	103,830
IFRS		
Hyperinflation adjustment to share capital cumulative to 31 December 2003		441,419
At 31 December 2004		<u>545,123</u>
At 31 December 2005		<u>545,222</u>
At 31 December 2006		<u>545,249</u>

The authorised number of ordinary shares in Transgaz SA is 10,383,037 (31 December 2005: 10,380,320 and 31 December 2004: 10,370,441) with a nominal value of RON 10 each. Each share carries one vote. The shareholders structure at 31 December 2006 is presented below:

	<u>Number of ordinary shares</u>	<u>Amount (RON)</u>	<u>Percentage (%)</u>
Romanian State, represented by			
Ministry of Economy and Commerce („MEC”)	8,825,989	88,260	85,004%
Fondul „Proprietatea”	<u>1,557,048</u>	<u>15,570</u>	<u>14,996%</u>
	<u>10,383,037</u>	<u>103,830</u>	<u>100.00%</u>

NOTES TO THE FINANCIAL STATEMENTS

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(Expressed in RON thousand, unless otherwise stated)

13 SHARE CAPITAL (CONTINUED)

In its statutory books, the Company has included in share capital certain revaluation differences for revaluations made prior to 31 December 2001. For the purposes of these financial statements prepared in accordance with IFRS, such increases have not been recognised as the hyperinflationary adjustments on fixed assets were recognised annually in the Statement of Income up to 31 December 2003. Consequently, in these financial statements the Company has only recorded share capital contributed in cash or kind, inflated from the date of the original contribution to 31 December 2003. The share capital increases which occurred after 1 January 2004 have been recognised in nominal terms as hyperinflation ceased after this date.

The increase in 2005 and 2006 relates to land which has been contributed to share capital by the Ministry of Economy and Commerce.

Dividends distribution

During year ended 31 December 2006, the Company has declared and distributed a dividend per share of RON 7.26 relating to prior year profit (2005:RON 0.39 per share, relating to 2002 profit previously retained; 2004 and 2003:nil).

14 PUBLIC PROPERTY RESERVE, LEGAL AND OTHER RESERVES

Public property reserve

A reserve corresponding to public property assets (Notes 3.4 and 5.7) was included as part of equity under the heading "Public Property Reserve" at the statutory value of the respective assets restated for inflation up to 1 January 2004.

Non distributable reserves

Legal reserve

In accordance with Romanian legislation and its Articles of Incorporation, the Company has to transfer five percent of its profits per statutory books to a statutory reserve which can accumulate up to 20% of the statutory share capital. The balance of the statutory reserve, which is not available for distribution at 31 December 2006, amounted to RON 20,766 (31 December 2005: RON 20,761 and 31 December 2004: RON 20,741).

TRANSGAZ SA

NOTES TO THE FINANCIAL STATEMENTS

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15 LONG TERM BORROWINGS

	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
IBRD loan	10,620	14,485	11,915
Gazprombank loans	126,293	193,841	219,624
Raiffeisen Bank loan	3,375	1,418	1,904
Efibanca loan	17,792	25,540	10,830
ABN Amro Bank loan	20,407	-	-
Less: current portion of loans	<u>(48,416)</u>	<u>(48,939)</u>	<u>(43,428)</u>
	<u>130,071</u>	<u>186,345</u>	<u>200,845</u>

IBRD loan

The loan from the International Bank for Reconstruction and Development ("IBRD" - RO 3723) was provided for the rehabilitation of the oil and gas sector in Romania under a Project Agreement signed on 1 June 1994.

As holding company of the Romgaz group of companies, the entire loan was nominally repayable by SNGN Romgaz, the predecessor company of Transgaz. However, in accordance with Government Decision 334/2000, following the year 2000 restructuring of the gas sector when Transgaz became a standalone entity, part of this borrowing was transferred to the newly created entities. The portion of the IBRD loan recognised by the Company is based upon an agreement concluded between the successor entities of SNGN Romgaz.

The Company also concluded a subsidiary loan agreement with the Ministry of Finance regarding its portion of this loan on 2 October 2001, and the original loan agreement between the Romanian Government and the IBRD has been amended to include the reorganisation of former Romgaz.

The loan is denominated in USD (the balances at 31 December 2006, 31 December 2005 and 31 December 2004 were USD 4,136 thousand and USD 4,661 thousand and USD 4,099 thousand respectively) and carries an interest rate of 0.5% over the cost of Qualified Borrowings as defined by the IBRD. The interest rate applicable in 2006 was approximately 5% (2005: approximately 5% and 2004: approximately 5%). Repayments are made twice a year. The principal and interest are repaid to the Ministry of Finance at least 15 days prior to the date of repayment by the Ministry of Finance to IBRD. Payments to Ministry of Finance may also be made in RON equivalent at the exchange rate at the date of payment plus a 5% refundable fee in order to protect the Ministry of Finance against foreign exchange losses and a 10% commission to the interest paid.

TRANSGAZ SA

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(Expressed in RON thousand, unless otherwise stated)

15 LONG TERM BORROWINGS (CONTINUED)

The loan was entirely drawn down and partially repaid by 31 December 2006.

The loan is secured by a deposit made by the Company in favour of the Ministry of Finance. The deposit is equal to the following instalment to be repaid. As at 31 December 2006 the deposit amounts to USD 400,000.

The maturity of the IBRD loan is set out bellow:

	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
Within 1 year	1,491	1,282	1,115
Between 1 and 2 years	1,604	1,379	1,199
Between 2 and 5 years	5,580	4,792	4,167
Over 5 years	<u>1,945</u>	<u>7,032</u>	<u>5,434</u>
	<u>10,620</u>	<u>14,485</u>	<u>11,915</u>

Gazprombank loan

The Company contracted two loans from Gazprombank for investment projects. Both loans from Gazprombank are denominated in USD and they were entirely drawn down by 31 December 2005.

First loan

On 24 November 1999, the predecessor Company contracted a loan from Gazprombank, in order to finance the first stage of the construction of a new gas transit pipeline in Dobrogea.

The loan is repayable in monthly instalments and bears an interest rate of 0.5% per month for the outstanding balance. The balance of the loan as at 31 December 2006 is USD 19,336 thousands.

The loan is collateralised by receivables from Gazexport under the gas transport contracts concluded with the Company, as well as any other receivables from Gazexport, in this order. The amount of the pledged receivables as at 31 December 2006 is RON 12,866 (31 December 2005 RON 15,382 and 31 December 2004 RON 14,134).

After the reorganisation of SNGN Romgaz SA the loan was taken over by Transgaz SA, the Company also being in charge of the related investment project (the Dobrogea transit pipeline).

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15 LONG TERM BORROWINGS (CONTINUED)

Second loan

The second loan agreement with Gazprombank was concluded on 8 February 2001 for partial financing of the Dobrogea pipeline.

The loan is repayable in monthly instalments. The loan bears an interest rate of 1 month LIBOR + 2% (penalty interest rate in case of late payments: 1 month LIBOR + 4%). The balance as at 31 December 2006 is USD 29,851 thousands.

The aggregate maturity of the Gazprombank loans is set out bellow.

	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
Within 1 year	33,855	40,977	38,326
Between 1 and 2 years	33,855	40,978	38,326
Between 2 and 5 years	58,583	111,886	114,978
Over 5 years	<u>-</u>	<u>-</u>	<u>27,994</u>
	<u>126,293</u>	<u>193,841</u>	<u>219,624</u>

Raiffeisen Bank loans

First loan

The first loan from Raiffeisen Bank was contracted in April 2003 to finance the acquisition of specific equipment for the gas transportation network, purchased from RMA Maschinen und Armaturenbau Keh. The interest rate applied is EURIBOR 3 months + 2% per year. The loan is guaranteed with the present and future receivables from Distrigaz Sud SA in amount of RON 45,008 as at 31 March 2006 (31 December 2005 RON 34,575, 31 December 2004 RON 37,763), a pledge on the bank accounts opened at the bank of RON 2,900 as at 31 March 2006 (2005: RON 2,388; 2004: RON 133) and a promissory note issues at sight for the whole amount of the loan. The loan has been completely repaid by 31 March 2006.

Second loan

The second loan from Raiffeisen Bank was contracted in September 2005 for financing the modernization of some of the Company's assets (i.e. SMG Isaccea II). The loan bears an interest rate of EURIBOR 1 month + 2% per year and is repayable in 8 quarterly instalments starting with October 2006.

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15 LONG TERM BORROWINGS (CONTINUED)

The maturity of the Raiffeisen Bank loan is set out bellow.

	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
Within 1 year	1,932	487	1,524
Between 1 and 2 years	1,443	533	380
Between 2 and 5 years	<u>-</u>	<u>398</u>	<u>-</u>
	<u>3,375</u>	<u>1,418</u>	<u>1,904</u>

Efibanca loans

The loans from Efibanca Spa, a company belonging to Banca Popolare di Lodi banking group, were contracted in June 2003, September 2004 and January 2005 to finance the acquisition of valves and related installation services from TYCO Valves&Controls ITALIA SRL and RMA Germany. The loans are denominated in EUR and bear an interest of 4.38%, 3.87% and 3.60% per annum, respectively. The repayment of each drawing is done in 10 bi-annual instalments. The balance as at 31 December 2006 is EUR 5,261 thousands.

The maturity of the Efibanca loans is set out bellow.

	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
Within 1 year	5,696	6,193	2,463
Between 1 and 2 years	5,696	6,193	2,463
Between 2 and 5 years	<u>6,400</u>	<u>13,154</u>	<u>5,904</u>
	<u>17,792</u>	<u>25,540</u>	<u>10,830</u>

ABN AMRO Bank Loan

The loan was contracted in December 2005 for financing the investments of the Company. The maximum amount of the credit facility is EUR 6,437 thousands.

The interest rate is EURIBOR one month + 0.95% if the ratio of Total Debt / EBITDA is less than 3 and EURIBOR one month + 1.5% if the ratio of Total Debt / EBITDA is greater than 3. The repayment will be made until 30 September 2010 in six monthly rates starting December 2006.

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15 LONG TERM BORROWINGS (CONTINUED)

The maturity of the ABN AMRO loan is set out below:

	Year ending <u>31 December 2006</u>	Year ending <u>31 December 2005</u>
Within 1 year	5,442	-
Between 1 and 2 years	5,442	-
Between 2 and 5 years	<u>9,523</u>	<u>-</u>
	<u>20,407</u>	<u>-</u>

Effective interest rate

Effective interest rate by category of loan can be summarized as follows:

	Year ending <u>31 December 2006</u>	Year ending <u>31 December 2005</u>	Year ending <u>31 December 2004</u>
Long term loans in USD	6.6%	5.2%	4.5%
Long term loans in EUR	4.4%	3.2%	4.3%

Fair value

The carrying amounts and fair values of long-term borrowings are as follows:

	Carrying amounts			Fair values		
	<u>31 December</u>			<u>31 December</u>		
	<u>2006</u>	<u>2005</u>	<u>2004</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>
IBRD	10,620	14,485	11,915	10,466	14,275	11,743
Gazprom	126,293	193,841	219,624	127,377	195,504	221,509
Raiffeisen	3,375	1,418	1,904	3,283	1,379	1,852
ABN	20,407	-	-	21,679	-	-
Efibanca	<u>17,792</u>	<u>25,540</u>	<u>10,830</u>	<u>17,916</u>	<u>25,717</u>	<u>10,905</u>
	<u>178,487</u>	<u>235,284</u>	<u>244,273</u>	<u>180,721</u>	<u>236,875</u>	<u>246,009</u>

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15 LONG TERM BORROWINGS (CONTINUED)

Fair value is determined based on the discounted value of the future cash flows, using a discount rate equal to the interest rate at which the management considers that the Companies could obtain similar borrowings, as at the balance sheet date.

16 DEFERRED INCOME

Deferred income consists of connection fees that are charged to customers for connecting them to the gas transportation network. The deferred income is released over the period in which related assets (connection pipes, gas flow regulator, counter) are depreciated.

17 LONG TERM TAX AND OTHER STATE PAYABLES

Long-term taxes payable in 2004 comprised various taxes payable to the State which were previously overdue and which were rescheduled in 2001 over a period of up to 5 years ending March 2006. In May 2005 the Company decided to fully repay the entire rescheduled tax amount.

The rescheduled tax liabilities accrued interest and penalties of 0.06% per day up to May 2005 which is equal to an effective rate of 21% per annum (2004: 22%).

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18 TAXATION

Income tax expense/(release)

	Year ended <u>31 December 2006</u>	Year ended <u>31 December 2005</u>	Year ended <u>31 December 2004</u>
Income tax expense - current	48,378	36,744	65,501
Deferred tax release - origination and reversal of temporary differences	(15,861)	(16,970)	(17,534)
Deferred tax release -effect of reduction in tax rate	-	-	<u>(103,191)</u>
Income tax expense/(release)	<u>32,517</u>	<u>19,774</u>	<u>(55,224)</u>

In 2006 and 2005, the Company accrued income taxes at the rate of 16% and in 2004 at the rate of 25% on profits computed in accordance with the Romanian tax legislation. Profit before taxation for financial reporting purposes is reconciled to tax expense as follows:

	Year ended <u>31 December 2006</u>	Year ended <u>31 December 2005</u>	Year ended <u>31 December 2004</u>
Profit before taxation	194,078	115,778	168,836
Theoretical tax charge at statutory rate of 16% (16% for 2005 and 25% for 2004)	31,052	18,524	42,209
Tax effect of items which are not deductible or assessable for taxation purposes:			
Non-taxable income	(7,435)	(3,612)	(4,370)
Non-deductible expenses	8,900	4,862	10,128
Effect of reduction in tax rate	-	-	<u>(103,191)</u>
Income tax expense /(release)	<u>32,517</u>	<u>19,774</u>	<u>(55,224)</u>

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18 TAXATION (CONTINUED)

Deferred tax

Deferred tax assets and liabilities are measured at the effective tax rate of 16% as at 31 December 2006, 31 December 2005 and 31 December 2004. The movement on the deferred income tax account is as follows:

	Year ended <u>31 December 2006</u>	Year ended <u>31 December 2005</u>	Year ended <u>31 December 2004</u>
At the beginning of the year	147,488	164,458	285,183
Release for the year	<u>(15,861)</u>	<u>(16,970)</u>	<u>(120,725)</u>
At the end of the year	<u>131,627</u>	<u>147,488</u>	<u>164,458</u>

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18 TAXATION (CONTINUED)

Deferred tax assets and liabilities and deferred tax expense/(income) in the income statement are attributable to the following items:

	31 December 2006	Movement	31 December 2005	Movement	31 December 2004	Movement (effect of change in tax rate differences)	31 December 2003
Deferred tax liabilities							
Restatement of property, plant and equipment	137,267	(15,758)	153,025	(16,685)	169,710	(103,011)	286,143
Impairment of property, plant and equipment	(2,928)	-	(2,928)	-	(2,928)	(180)	499
Other taxable temporary differences	<u>1</u>	<u>(74)</u>	<u>75</u>	<u>1</u>	<u>74</u>	<u>(2,928)</u>	<u>-</u>
	134,340	(15,832)	150,172	(16,684)	166,856	(103,191)	286,642
Deferred tax assets							
Accruals	778	82	696	74	622	-	298
Adjustments to inventories	103	(81)	184	78	106	-	(279)
Provision for employee benefits	<u>1,832</u>	<u>28</u>	<u>1,804</u>	<u>134</u>	<u>1,670</u>	<u>230</u>	<u>1,440</u>
	2,713	29	2,684	286	2,398	939	1,459
Net deferred tax liability	<u>131,627</u>	<u>(15,861)</u>	<u>147,488</u>	<u>(16,970)</u>	<u>164,458</u>	<u>(103,191)</u>	<u>285,183</u>

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NOTES TO THE FINANCIAL STATEMENTS

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18 TAXATION (CONTINUED)

The amounts shown in the balance sheet include the following:

	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
Deferred tax liabilities to be settled after more than 12 months	<u>125,828</u>	<u>141,074</u>	<u>157,605</u>

19 TRADE AND OTHER PAYABLES

	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
Trade payables	79,354	70,924	35,944
Suppliers of fixed assets	42,000	60,444	51,062
Payable to Ministry of Economy and Commerce (additional distribution)	51,718	45,483	-
Other taxes	24,498	16,185	8,993
Employees payable	10,079	7,980	8,190
Dividends	-	4,000	-
VAT payable	6,737	-	-
Other liabilities	<u>4,340</u>	<u>5,036</u>	<u>3,058</u>
	<u>218,726</u>	<u>210,052</u>	<u>107,247</u>

As detailed in the Statement of changes in the shareholders' equity, in 2005 the Ministry of Economy and Commerce has decided to charge the Company the equivalent of late payment interest for declared and unpaid dividends dating from the period 2000-2003. These penalties are in substance an additional distribution to shareholders, therefore the Company's management decided to record and present them as a movement in retained earnings. The majority shareholder of the Company has informed the management that the payment of the penalties will be deferred until further notice, allowing the Company use of the respective amount for continuing to develop the network.

As at 31 December 2006, RON 10,052 (31 December 2005: RON 12,702 and 31 December 2004: RON 20,269) of trade and other payables are denominated in foreign currency, mainly USD.

Included in trade payables are balances due to related parties of RON 54,242 (31 December 2005: RON 43,691 and 31 December 2004: RON 20,207), as presented in Note 29.

TRANSGAZ SA

NOTES TO THE FINANCIAL STATEMENTS

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20 SHORT TERM BORROWINGS

Short-term borrowings are analyzed as follows:

	<u>Currency</u>	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
1. BRD overdraft	RON	2,620	14,310	18,202
2. ABN AMRO Bank overdraft	RON	14,673	18,838	11,751
Current portion of long term loans (Note 15)		<u>48,416</u>	<u>48,939</u>	<u>43,428</u>
		<u>65,709</u>	<u>82,087</u>	<u>73,381</u>

1. BRD overdraft

BRD overdraft agreement was concluded in 2004 with a RON 20,000 ceiling. It was subsequently extended until 31 August 2007. The facility had a ceiling of RON 30,000 at 31 December 2006 and was secured with a pledge on receivables from the contract with Electrocentrale Bucuresti SA in amount of RON 20,444 as at 31 December 2006 (31 December 2005: RON 7,320, 31 December 2004: RON 6,746) and on cash accounts with BRD in amount of RON 458 as at 31 December 2006 (31 December 2005 RON 8,363, 31 December 2004 RON 16).

Interest rate is BUBOR + 0.5% p.a. The effective interest rate in 2006 was 8% (2005: 11% and 2004:20%).

2. ABN AMRO Bank overdraft

ABN AMRO Bank overdraft agreement was concluded in 2004 with a RON 20,000 ceiling. It was subsequently extended until 30 October 2007. The overdraft is secured by a general pledge over the Company's receivables. Interest rate is BUBOR + 0.5% p.a. The effective interest rate in 2005 was 8% (2005: 11% and 2004: 20%).

The carrying amount of short-term borrowings approximates their fair value.

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21 PROVISIONS FOR LIABILITIES AND CHARGES

	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
<i>Current provision</i>			
Provision for litigations	1,278	12,969	11,474
Provision for guarantees issued	<u>-</u>	<u>-</u>	<u>1,000</u>
	<u>1,278</u>	<u>12,969</u>	<u>12,474</u>

Legal claims

As at 31 December 2004 the Company recorded provisions in respect of the litigation with the "Gas Federation" trade union (Note 33). As at 31 December 2005 the provision for litigations was increased due to a new lawsuit with Petrom SA. In 2006 the Company lost the case against the union, paid the amount requested by the Company's union and used the respective provision.

The value of the gas benefit relating to year 2004, in amount of RON 10,347, has been paid to the employees in 2005 and the value of the benefit for 2005, in amount of RON 13,862, has been partially paid in 2005 (RON 4,883) and partially in 2006 (RON 8,978). The amount for the year 2006 in amount of RON 24,301 has been paid entirely during 2006. The social contributions corresponding to the gas benefits have been computed and charged to the income statement.

Provision for guarantees

As at 31 December 2004, the Company has recorded a provision in respect of guarantees issued by Transgaz for a loan taken by Resial SA, a susidiary (Note 9). In 2005, this provision has been used as the Company had to disburse the guarantee amount in 2005.

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NOTES TO THE FINANCIAL STATEMENTS

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(Expressed in RON thousand, unless otherwise stated)

21 PROVISIONS FOR LIABILITIES AND CHARGES (CONTINUED)

Movement in provision for liabilities and charges

	<u>Provision</u>
1 January 2004	-
Increase of provision	<u>12,474</u>
31 December 2004	12,474
Increase of provision	12,969
Used amounts	<u>(12,474)</u>
31 December 2005	12,969
Increase of provision	4,628
Used amounts	<u>(16,319)</u>
31 December 2006	<u>1,278</u>

22 PROVISION FOR EMPLOYEE BENEFITS

	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
<i>Non-current provision</i>			
Provision for employee benefits	<u>11,452</u>	<u>11,278</u>	<u>10,443</u>

Employee benefits

Under the collective labour contract, the Company is required pay to its employees at the time of their retirement a lump-sum amount equal to a multiplier of their gross salary depending on the employment period in the gas industry, working conditions, etc. This provision in respect of these liabilities has been computed based on the estimations of the an average salary of RON 1,740 as at 31 December 2006 (2005: RON 1,567, 2004: 1,400), an average number of 4 salaries to be paid at the time of the retirement, a negligible staff turnover and the time frame when the benefits are to be paid. The provision has been discounted to its present value by applying a discount factor based on the risk free interest rate (i.e. interest rate on government bonds).

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22 PROVISION FOR EMPLOYEE BENEFITS (CONTINUED)

Movement in provision for employee benefits

	<u>Provision</u>
1 January 2004	9,117
Unwinding of the discount	26
Increase of provision	<u>1,300</u>
31 December 2004	10,443
Unwinding of the discount	35
Increase of provision	<u>800</u>
31 December 2005	11,278
Unwinding of the discount	24
Increase of provision	<u>150</u>
31 December 2006	<u>11,452</u>

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NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

23 REVENUE

	Year ended <u>31 December 2006</u>	Year ended <u>31 December 2005</u>	Year ended <u>31 December 2004</u>
Revenue from domestic gas transportation services	620,811	510,248	434,774
Revenue from international gas transit services	212,667	219,546	242,316
Revenue from sales of gas	71,623	36,836	91,130
Revenue from other services	<u>659</u>	<u>558</u>	<u>557</u>
	<u>905,760</u>	<u>767,188</u>	<u>768,777</u>

Revenues from international gas transportation services are generated in Romania and result from services provided to international customers for transit of gas from the Russian Federation to the Balkan region.

24 OTHER INCOME

	Year ended <u>31 December 2006</u>	Year ended <u>31 December 2005</u>	Year ended <u>31 December 2004</u>
Reimbursement of interest overpaid to State Budget	1,342	6,905	627
Reimbursement of penalties for late payment	-	2,157	-
Sale of intangibles to SNGN Romgaz	18,052	-	-
Sale of investment	2,219	-	-
Other operating revenues	<u>7,584</u>	<u>4,315</u>	<u>4,800</u>
	<u>29,197</u>	<u>13,377</u>	<u>5,427</u>

TRANSGAZ SA

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

25 OTHER OPERATING EXPENSES

	Year ended <u>31 December 2006</u>	Year ended <u>31 December 2005</u>	Year ended <u>31 December 2004</u>
Impairment loss/(reversal) of impairment loss of current assets	10,100	4,099	(14,597)
Loss on disposal of fixed assets	6,446	7,743	6,371
Penalties	4,008	3,261	7,029
Utilities	3,409	2,903	2,157
Telecom	2,621	2,564	2,615
Bank and other commissions	1,414	1,391	864
Rent	769	594	812
Insurance premium	598	430	326
Bad debts written off	-	85	2,450
Charges in inventory of finished goods and work in progress	(165)	(1)	335
Impairment of property, plant and equipment	-	-	18,302
Other	<u>11,083</u>	<u>11,466</u>	<u>8,253</u>
	<u>40,283</u>	<u>34,535</u>	<u>34,917</u>

26 NET FINANCIAL INCOME/ (EXPENSE)

	Year ended <u>31 December 2006</u>	Year ended <u>31 December 2005</u>	Year ended <u>31 December 2004</u>
Foreign exchange gains	37,076	10,319	30,821
Foreign exchange losses	(5,463)	(18,944)	(8,710)
Interest income	1,703	2,606	2,872
Interest expense	(14,718)	(16,330)	(15,771)
Unwinding of the discount			
Provision for employee benefit	(24)	(35)	(26)
Other financial expenses	<u>(777)</u>	<u>-</u>	<u>-</u>
	<u>17,797</u>	<u>(22,384)</u>	<u>9,186</u>

TRANSGAZ SA

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27 NET CASH-FLOW FROM OPERATING ACTIVITY

	Year ended <u>31 December 2006</u>	Year ended <u>31 December 2005</u>	Year ended <u>31 December 2004</u>
Profit before taxation	194,078	115,778	168,836
<i>Adjustments for:</i>			
Depreciation and amortisation	165,297	161,203	154,524
Impairment loss of property, plant and equipment	-	-	18,302
(Profit)/Loss on disposal of fixed assets	(13,826)	7,743	6,371
(Release)/Provisions for liabilities and charges	(11,691)	495	12,474
Provision for employee benefits	150	800	1,300
(Release)/Provisions for debtors and inventories	10,100	4,099	(14,597)
Bad debts written off	-	85	2,450
Net interest expense	13,015	13,724	12,899
Effect of exchange rate changes on non-operating items	32,026	9,829	(25,640)
Operating profit before working capital changes	389,149	313,756	336,919
(Increase)/decrease in trade and other receivables	(20,225)	(23,101)	101,635
Decrease/(increase) in inventories	2,952	2,558	(2,756)
Increase/(decrease) in trade and other payables	<u>9,407</u>	<u>21,002</u>	<u>(20,923)</u>
Cash generated from operations	<u>381,283</u>	<u>314,215</u>	<u>414,875</u>

28 OTHER EMPLOYEE BENEFITS

According to the collective labour agreement, employees were entitled to 4,000 cubic meters of gas a year and starting with October 2006 the amount has been increased to 5000 cubic meters a year as benefit in kind or the equivalent cash amount computed at monthly medium price per cubic meter. The expense has increased primarily due to the increase in the price of natural gas but also due to the increase in employee numbers.

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29 TRANSACTIONS WITH RELATED PARTIES

Parties are considered to be related if one party has the ability to control the other party, to exercise significant influence over the other party in making financial or operational decisions, is under common control with another party, is a joint venture in which the entity is a venturer or is part of the key management personnel as defined by IAS 24 "Related Party Disclosure". In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

Related parties may enter into transactions, which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

The majority shareholder in the Company is the Romanian State through the Ministry of Economy and Commerce; the related parties presented below are majority owned by the Romanian State and thus presented as entities under common control.

No transaction with the Company's subsidiary, Resial SA, took place during 2004 and 2005. However, the Company has issued a guarantee in amount of RON 1,000 for a loan taken by Resial. A full provision was made for this amount as at 31 December 2004. The provision was reversed in 2005 after the Company paid the guarantee amount in 2005.

During the years ended 31 December 2006, 31 December 2005 and 2004 the following transactions were carried out with related parties (entities majority owned by the Romanian State) and the following balances were payable/receivable at the respective dates:

i) Revenues from related parties – services and gas sold

		<u>31 December</u> <u>2006</u>	<u>31 December</u> <u>2005</u>	<u>31 December</u> <u>2004</u>
	<u>Relationship</u>			
SNGN Romgaz	Entity under common control	51,843	44,124	135,609
Termoelectrica	Entity under common control	16,916	7,282	12,869
Electrocentrale				
Deva SA	Entity under common control	6,838	4,690	6,572
Electrocentrale				
Bucureşti SA	Entity under common control	93,609	70,588	67,043
Electrocentrale				
Galaţi SA	Entity under common control	15,219	6,778	-
BAT Mediaş	Entity under the control of key management personnel	<u>2</u>	-	-
		<u>184,427</u>	<u>133,462</u>	<u>222,093</u>

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29 TRANSACTIONS WITH RELATED PARTIES (CONTINUED)

ii) Receivables from related parties

	<u>Relationship</u>	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
SNGN Romgaz Termoelectrica	Entity under common control	68	-	890
(net of provision) Electrocentrale Deva SA	Entity under common control	15,207	28,246	58,839
Electrocentrale Bucureşti SA	Entity under common control	999	385	1,354
Electrocentrale Galaţi SA	Entity under common control	20,516	7,320	6,746
Grup Dezvoltare Reţele SA	Entity under common control	1,376	880	-
		-	126	-
		<u>38,166</u>	<u>36,957</u>	<u>67,829</u>

iii) Acquisitions of services from related parties (gas storage)

	<u>Relationship</u>	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
SNGN Romgaz	Entity under common control	<u>142,056</u>	<u>91,721</u>	<u>62,320</u>

iv) Acquisitions of services from related parties (other services)

	<u>Relationship</u>	<u>31 December 2006</u>	<u>31 December 2005</u>	<u>31 December 2004</u>
BAT Mediaş	Entity under control of key management personnel	<u>1,374</u>	<u>-</u>	<u>-</u>

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29 TRANSACTIONS WITH RELATED PARTIES (CONTINUED)

v) Payables to related parties (gas storage)

		<u>31 December</u> <u>2006</u>	<u>31 December</u> <u>2005</u>	<u>31 December</u> <u>2004</u>
	<u>Relationship</u>			
SNGN Romgaz	Entity under common control	<u>54,116</u>	<u>43,691</u>	<u>20,207</u>

vi) Payables to related parties (other services)

		<u>31 December</u> <u>2006</u>	<u>31 December</u> <u>2005</u>	<u>31 December</u> <u>2004</u>
	<u>Relationship</u>			
BAT Medias	Entity under common control	<u>126</u>	<u>—</u>	<u>—</u>

vii) Key management compensation

	<u>Year ended</u> <u>31 December 2006</u>	<u>Year ended</u> <u>31 December 2005</u>	<u>Year ended</u> <u>31 December 2004</u>
Salaries paid to key management	<u>1,758</u>	<u>1,480</u>	<u>1,371</u>

viii) Loan to related party

	<u>Year ended</u> <u>31 December 2006</u>	<u>Year ended</u> <u>31 December 2005</u>	<u>Year ended</u> <u>31 December 2004</u>
Loan to Resial SA	2,235	3,068	2,432
less provision for impairment of loan	<u>(2,235)</u>	<u>(3,068)</u>	<u>(2,432)</u>
	<u>—</u>	<u>—</u>	<u>—</u>

TRANSGAZ SA

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30 SEGMENT INFORMATION

The Company has three business operating segments which have different risks and benefits: international gas transit, domestic gas transportation and gas supply.

For the year ended 31 December 2006

	<u>Domestic gas transportation</u>	<u>International gas transit</u>	<u>Gas supply</u>	<u>Unallocated</u>	<u>Total</u>
External sales	620,811	212,667	71,623	659	905,760
Other unallocated income	<u>-</u>	<u>-</u>	<u>-</u>	<u>29,197</u>	<u>29,197</u>
Total revenue	620,811	212,667	71,623	29,856	934,957
Depreciation	123,980	37,630	-	3,687	165,297
Operating expenses other than depreciation	<u>490,103</u>	<u>19,449</u>	<u>71,488</u>	<u>83,827</u>	<u>593,379</u>
Operating income	6,728	155,588	135	13,830	176,281
Net financial revenue					<u>17,797</u>
Gross profit					194,078
Taxation					<u>(32,517)</u>
Net profit					<u>161,561</u>
Segment assets	1,919,968	692,566	9,128	286,043	2,907,705
Segment liabilities	2,261,192	331,617	-	314,896	2,907,705
Capital expenditure	169,367	1,708	-	2,013	173,088
Non-cash expenses other than depreciation	13,157	71,521	-	12	84,690

The assets presented for each segment comprise mainly tangible and intangible assets, inventory and receivable and exclude mainly the cash and bank accounts.

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30 SEGMENT INFORMATION (CONTINUED)

The liabilities presented for each segment consist of the operating liabilities and loans contracted by the Company for the acquisition of the assets for the respective segments.

The non-cash expenses other than depreciation are composed of the receivables impairment charge, the inventory impairment charge and the expense with the gas received from barter transactions and sold to customers.

The Company's secondary segment is structured based on the customers' location, domestic or external.

The transit activity is provided only for the external customers, while the transportation activity is provided for the domestic customers.

	<u>Domestic customers</u>	<u>External customers</u>	<u>Total</u>
Turnover	692,435	213,325	905,760
Other income			29,197

All the Company's assets are located in Romania. All the Company's activities are carried out in Romania.

The Company has receivables from foreign parties in amount of RON 16,433.

TRANSGAZ SA

NOTES TO THE FINANCIAL STATEMENTS

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30 SEGMENT INFORMATION (CONTINUED)

For the year ended 31 December 2005

	<u>Domestic gas transportation</u>	<u>International gas transit</u>	<u>Gas supply</u>	<u>Unallocated</u>	<u>Total</u>
External sales	510,248	220,103	36,836	1	767,188
Other unallocated income	<u>-</u>	<u>-</u>	<u>-</u>	<u>13,377</u>	<u>13,377</u>
	510,248	220,103	36,836	13,378	780,565
Depreciation expense	119,405	38,714	-	3,084	161,203
Operating expenses other than depreciation	<u>386,553</u>	<u>50,230</u>	<u>36,554</u>	<u>7,863</u>	<u>481,200</u>
Operating income	4,290	131,159	282	2,431	138,162
Net financial gain/(loss)					<u>(22,384)</u>
Gross profit					115,778
Taxation					<u>(19,774)</u>
Net profit					<u>96,004</u>
Segment assets	1,853,179	759,456	2,151	256,463	2,869,098
Segment liabilities	2,115,727	558,487	-	194,884	2,869,098
Capital expenditure	257,240	628	-	634	258,502
Non-cash expenses other than depreciation	3,463	36,554	-	-	40,017

The assets presented for each segment comprise mainly tangible and intangible assets, inventory and receivable and exclude mainly the cash and bank accounts.

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30 SEGMENT INFORMATION (CONTINUED)

The liabilities presented for each segment consist of the operating liabilities and loans contracted by the Company for the acquisition of the assets for the respective segments.

The non-cash expenses other than depreciation are composed of the receivables impairment charge, the inventory impairment charge and the expense with the gas received from barter transactions and sold to customers.

The Company's secondary segment is structured based on the customers' location, domestic or external.

The transit activity is provided only for the external customers, while the transportation activity is provided for the domestic customers.

	<u>Domestic customers</u>	<u>External customers</u>	<u>Total</u>
Turnover	547,083	220,104	767,187
Other income			13,376

All the Company's assets are located in Romania. All the Company's activities are carried out in Romania.

The Company has receivables from foreign parties in amount of RON 19,262.

TRANSGAZ SA

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

30 SEGMENT INFORMATION (CONTINUED)

For the year ended 31 December 2004

	<u>Domestic gas transportation</u>	<u>International gas transit</u>	<u>Gas supply</u>	<u>Unallocated</u>	<u>Total</u>
External sales	434,774	242,873	91,130	-	768,777
Other unallocated income	<u>-</u>	<u>-</u>	<u>-</u>	<u>5,427</u>	<u>5,427</u>
	434,774	242,873	91,130	5,427	774,204
Depreciation	111,499	38,140	-	4,885	154,524
Operating expenses other than depreciation	<u>343,564</u>	<u>20,416</u>	<u>89,415</u>	<u>6,635</u>	<u>460,030</u>
Operating income/(loss)	(20,289)	184,317	1,715	(6,093)	159,650
Net financial gain					<u>9,186</u>
Gross profit					168,836
Taxation					<u>55,224</u>
Net profit					<u>224,060</u>
Segment assets	1,805,167	792,412	18,493	145,990	2,762,062
Segment liabilities	1,888,934	459,515	-	413,613	2,762,062
Capital expenditure	295,216	31,532	-	4,524	331,272
Non-cash expenses other than depreciation	34,925	89,426	-	-	124,351

The assets presented for each segment comprise mainly tangible and intangible assets, inventory and receivable and exclude mainly the cash and bank accounts.

TRANSGAZ SA

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

30 SEGMENT INFORMATION (CONTINUED)

The liabilities presented for each segment consist of the operating liabilities and loans contracted by the Company for the acquisition of the assets for the respective segments.

The non-cash expenses other than depreciation are composed of the receivables impairment charge, the inventory impairment charge and the expense with the gas received from barter transactions and sold to customers.

The Company's secondary segment is structured based on the customers' location, domestic or external.

The transit activity is provided only for the external customers, while the transportation activity is provided for the domestic customers.

	<u>Domestic customers</u>	<u>External customers</u>	<u>Total</u>
Turnover	525,904	242,873	768,777
Other income			5,424

All the Company's assets are located in Romania. All the Company's activities are carried out in Romania.

The Company has receivables from foreign parties in amount of RON 14,134.

31 EARNINGS PER SHARE

Basic earnings per share are calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year.

	<u>Year ended</u> <u>31 December 2006</u>	<u>Year ended</u> <u>31 December 2005</u>	<u>Year ended</u> <u>31 December 2004</u>
Profit/(loss) attributable to equity holders of the Company	161,561	96,004	224,060
Weighted average to number of shares	10,382,584	10,374,557	10,363,700
Basic (loss)/earnings per share (RON per share)	15.56	9.25	21.62

32 SIGNIFICANT NON-CASH TRANSACTIONS

Mutual cancellations

Approximately 24% of accounts receivable were settled via non-cash transactions during the year ended 31 December 2006 (2005: 9% and 2004: 37%). The transactions represent mainly sale of products and services in exchange for raw materials and services or cancellation of mutual balances with customers and suppliers within the operating cycle.

Barter transactions

The barter transactions during 2006 were of RON 120,975 (2005: RON 172,248 and 2004: RON 89,415). These transactions represent gas received from Gazexport Russia in exchange for the gas transit services provided by the Company.

33 CONTINGENCIES, COMMITMENTS AND OPERATING RISKS

(i) Commitments

The Concession Agreement specifies that, at the end of the Agreement, ANRM has the right to receive back, free of any charge or encumbrance, property, plant and equipment with an estimated gross book value of RON 2,808,987, representing all public property assets existing at the time when the agreement was signed and all the investments which are to be done to the gas pipeline system, according to the investments programme set out in the Concession Agreement. The Company also has other obligations in respect of the concession agreement as described in Note 7.

(ii) Taxation

The Romanian taxation system has just undergone a process of consolidation and harmonisation with the European Union legislation. However, there are still different interpretations of the fiscal legislation. In various circumstances, the tax authorities may have different approaches to certain issues, and assess additional tax liabilities, together with late payment interest and penalties (accruing at a rate of approximately 36% p.a. in 2006, same for 2007). In Romania, tax periods remain open for 5 years. The Company's management considers that the tax liabilities included in these financial statements are fairly stated.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

33 CONTINGENCIES, COMMITMENTS AND OPERATING RISKS (CONTINUED)

(iii) Insurance policies

The Company holds no insurance policies in relation to its operations, product liability, or in respect of public liability. The Company has insurance policies for buildings and mandatory 3rd party liability insurance for its car fleet.

(iv) Environmental matters

Environmental regulations are developing in Romania and the Company has not recorded any liability at 31 December 2006 for any anticipated costs, including legal and consulting fees, site studies, the design and implementation of remediation plans, related to environmental matters. Management do not consider the costs associated with environmental issues to be significant.

(v) Legal proceedings

During the year, the Company was involved in a number of court proceedings (both as a plaintiff and a defendant). Except for the matter described below, the Company's management believes that the ultimate resolution of these matters will not have a material adverse effect on the amounts of operations or the financial position of the Company.

Following legal action taken in 2004 by the Gas Federation of Romania, a trade union, the Company was requested to pay an amount of RON 11,473 through decision no 94/2005 issued by Alba County Court of Law. This amount represents the value of gas that the Company should have distributed to employees based on the Collective Labour Agreement for 2004. The Company disagreed with this decision and filed an appeal to the Appeal Court, which was rejected in 2005. A provision of RON 11,473 was recorded in the Company accounts as at 31 December 2004. This provision was reversed during 2006 after the Company paid the amount requested by the union.

(vi) Government policy in the gas sector in Romania

As part of the ongoing process of restructuring of the gas sector in Romania, the Romanian Government and Parliament may continue to adopt new legislation, that impacts the sector in general, and the Company in particular.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

(Expressed in RON thousand, unless otherwise stated)

33 CONTINGENCIES, COMMITMENTS AND OPERATING RISKS (CONTINUED)

ANRGN (from 2007 ANRE) is an autonomous public body and establishes the gas transport tariffs charged by the Company. It is possible that the Agency might decide to implement changes in Governmental strategies in the gas sector which could lead to significant changes to the tariffs and hence significantly impact the Company's revenue.

It is not possible to establish at this stage the effects, if any, of future Government policy in the gas sector in Romania on the value of the assets and liabilities of the Company.

34 SUBSEQUENT EVENTS

Dividends

In April 2007 the Company declared dividends in amount of RON 121,385 thousands for 2006, (a dividend of RON 12 per share).