



**SOCIETATEA NAȚIONALĂ DE TRANSPORT
GAZE NATURALE "TRANSGAZ" SA MEDIAȘ**
Capital social: 117 738 440,00 LEI
ORC: J32/301/2000; C.I.F.: RO13068733
P-ța C. I. Motaș nr. 1, cod: 551130, Mediaș, Jud. Sibiu
Tel.: 0040 269 803333, 803334; Fax: 0040 269 839029
http://www.transgaz.ro; E-mail: cabinet@transgaz.ro



No. 13550/23 March 2017

Submitted for approval in the OGMS of 27/28 April 2017

REPORT on the approval of the revenue and expense budget for 2017 and of the estimations for 2018 - 2019

SUMMARY

The draft revenue and expense budget for 2017 and the estimations for 2018-2019 were approved in the Board of Administration meeting of 24 March 2017.

The substantiation of the draft was based on the programmes for NTS design, maintenance, rehabilitation, supply of materials and spare parts; programmes for the provision of services; the provisions of the Collective Labour Contract; the legislation in force; based on the quantities of gas estimated to be transmitted and the expected capacity bookings.

* thousand RON *

No.	ITEM	2016 REB	Estimated in 2016	2017 REB
0	1	2	3	4
1.	TOTAL REVENUE, of which:	1.752.011	2.034.216	2.205.866
	<i>2016 REB comparison</i>		16,11%	25,90%
	<i>Estimated in 2016 comparison</i>			8,44%
1.1.	Operating revenue before the construction activity according to IFRIC 12	1.723.159	1.883.155	1.577.348
1.2.	Revenue before the construction activity according to IFRIC 12	0	118.884	597.692
1.3.	Financial revenue	28.852	32.177	30.826
2.	TOTAL COST	1.282.386	1.312.881	1.834.295
	<i>2016 REB comparison</i>		2,38%	43,04%
	<i>Estimated in 2016 comparison</i>			39,72%
2.1.	Operating costs	1.278.581	1.184.314	1.226.595
2.2.	Cost of assets constructed according to IFRIC 12	0	118.884	597.692
2.3.	Financial costs	3.805	9.683	10.007
3.	GROSS PROFIT	469.625	721.335	371.571
	<i>2016 REB comparison</i>		53,60%	-20,88%
	<i>Estimated in 2016 comparison</i>			-48,49%
4.	Tax on profit	72.149	125.625	59.742
5.	NET PROFIT	397.476	595.710	311.829

No.	ITEM	2016 REB	Estimated in 2016	2017 REB
	2016 REB comparison		49,87%	-21,55%
	Estimated in 2016 comparison			-47,65%

PROPOSAL:

The approval of the draft revenue and expense budget for 2017 and of the estimations for 2018 - 2019, according to the applicable Articles of Incorporation of Transgaz, Chapter IV, Art.15, paragraph (3), letter c).

General considerations regarding REB preparation

Considering GO 26/21 August 2013, as further amended and supplemented, *‘on strengthening the financial discipline at the level of the economic operators where the state or the territorial administrative units are unique or majority shareholders or hold a majority directly or indirectly’*, regulating:

- Art. 6, paragraph (1[^]1) *The economic operators under Art.4, paragraph (1), letter d), whose shares are accepted to trade on a regulated market, as well as their affiliates submit, according to the law the revenue and expense budget and the substantiation annexes, prepared according to the applicable laws, to the General Meeting of the Shareholders, for approval, following the prior consulting of the trade unions, and publishes the revenue and expense budget including the amount for the current year within 60 days from the entering into force of the annual law on the state budget or from the date of approval of the village, town, Bucharest district, County, Bucharest local budgets, as appropriate.*
- Art. 7, paragraph (1) *annually, the state budget law establishes salary policy objectives on which economic operators base revenue and expense budget indicators.*
- Art. 9, paragraph (1) *Economic operators consider, without limitation the following when substantiating the revenue and expense budget:*
 - a) Compliance with the Government's and administrative-territorial units' policy on improving the economic and financial performance of the operators;*
 - b) compliance with the salary policy objectives set by the annual state budget law;***
 - c) the specific performance criteria and the quantified objectives for the reduction of payments and outstanding debts, the reduction of losses, the increase in profit and turnover and the labour productivity growth provided in the mandate contracts, stable in relation to the management strategy of the Board of Administration//Supervisory Board and the management plan of the directors / members of the directorate of economic operators.***

for the substantiation of the Revenue and Expense Budget of SNTGN Transgaz SA it is necessary to comply with the Government's policy on enhancing the economic and financial performance and of the salary policy objectives approved under the State Budget Law.

The Revenue and Expense Budget for 2017 is substantiated compliant with the provisions of:

- Law 6/16 February 2017 of the state budget for year 2017;
- GO 26/21 August 2013, *'on strengthening the financial discipline at the level of the economic operators where the state or the territorial administrative units are unique or majority shareholders or hold a majority directly or indirectly'*; as further amended and supplemented,
- GO 11/27 January 2016 *'amending and supplementing GO 26/2013 on strengthening the financial discipline at the level of the economic operators where the state or the territorial administrative units are unique or majority shareholders or hold a majority directly or indirectly'*;
- Ministry of Public Finance Order 20/7 January 2016 *'on the form and structure of the revenue and expense budget and of the annexes for the substantiation of the budget'*;
- ANRE Order 32/21 May 2014 *on the approval of the Gas Transmission Regulated Revenue, Total Revenue and Regulated Tariff Setting Methodology*;
- ANRE Order 31/6 July 2016 *on the amendment and supplementing of the methodology for setting the regulated revenue, the total revenue and the regulated tariffs for the gas transmission activity, approved by the ANRE Order 32/21 May 2014*;
- Regulation EU 312/2014 *establishing a Network Code on Gas Balancing of Transmission Networks*;
- ANRE Order 160/2015 *amending and supplementing the Network Code for the National Gas Transmission System, approved by ANRE President Order 16/2013*;
- Companies' Law 31/1990, *republished, as further amended and supplemented*.

The draft revenue and expense budget for 2017 was submitted for consultation to the trade unions and the financial management control according to Government Resolution 1.151/2012 approving the Methodological rules on the organization and exercise of the financial management control.

Expense substantiation was based on the following:

- estimated inflation ratios and/or exchange rates projected according to the **Medium-term forecast for the period 2016-2020 - the winter forecast of the National Commission for Prognosis**, for those costs which by their nature have an approximately linear evolution;
- technical regulations in force;
- programme for NTS modernization and development (Investments), design, maintenance and rehabilitation, supply of materials and spare parts;
- service providing programs (security and safety, training, consulting, etc.);
- normative acts that are in force regarding legislated costs (contribution to social insurance, health insurance, unemployment benefit; transmission licence fee, royalty for the concession of the transmission system, etc.).
- costs of social activities under the Collective Labour Contract.

Under Art. 1 of GEO 8/2009 on granting holiday vouchers approved as amended and supplemented by Law 94/2014, stipulating that 'As of the entering into force of this emergency ordinance, for the recovery and maintenance of the working capacity of the employees, the employers hiring personnel under an individual labour contract may legally grant vouchers, hereinafter referred to as holiday vouchers' correlated with the provisions of the CLC in force, regarding the substantiation of the 2017 REB and of the estimations for 2018-2019, no holiday voucher costs were substantiated and were taken into account the rights of the employees in line with art 189 of the current Collective Labour Contract in force regarding the partial settlement of tickets for rest and treatment.

For 2017, the granting of holiday vouchers up to the maximum limit according to Art. 1, paragraph (4) of GEO 8/2009 on granting holiday vouchers approved as amended and supplemented by Law 94/2014, *'The maximum limit of the amounts which may be granted to employees as holiday vouchers represent the value of 6 gross national minimum base salaries guaranteed for an employee, in a fiscal year'*, would lead to costs about three times higher than the expenditure provided for the partial settlement of the tickets for rest and treatment according to the CLC.

- technological consumption costs were established based on:
 - an estimate of the specific consumption in the gas compressor stations, technological loss due to discharge as a result of new pipe couplings and planned repairs, differences due to measurement errors, etc.;
 - a purchase price of gas from domestic production for the technological consumption under the average price related to the year 2016 (71.27);
- costs of purchase of gas for NTS balancing according to ANRE Order 160/2015 amending and supplementing the Network Code for the National Gas Transmission System, approved by ANRE President Order 16/2013 and ANRE Order 1/18.01.2016;
- the expense related to the tax on the monopoly - according to Art. 15 of GEO 99/2016 on measures related to salaries of the personnel paid from public funds, the prorogation of terms, and fiscal and budgetary measures providing *'The period under Art. 6 of Government Order 5/2013 on the establishment of special tax measures of the natural monopoly activities in the electricity and natural gas domains, as further amended, shall be extended until 31 December 2017, included'*;
- The following were considered at the substantiation of the personnel costs:
 - compliance with the Collective Labour Contract in force in the Company and the individual labour contract applicable;
 - a basic salary indexation by 1,4 % starting from October 2017 in line with the provisions of art. 146 of the Collective Labour Contract;
 - Hiring new staff for the new 210 jobs created for BRUA and Moldova projects, whose salary fund will be settled in part from the funds received from the European Union and which will be cancelled after the completion of the projects. The funds provided for this purpose in the amount of RON 18 861, thousand were assigned to staff salary costs, being the kind employed for business expansion, art. 59 (1) letter c of Law no. 6/2017 of the state budget. RON 7,544 thousand of this amount will be reimbursed from the funds received from the EU for the achievement of these projects.

- Fixed-term employment of personnel on 80 positions in 2017. Such positions will be occupied mainly by experts and advisers needed for the operating and analysis activities regarding the structure of the gas market consumptions and of the European funds granting necessary for the implementation of the projects for the upgrading of the NTS and related facilities. For these 80 position having an employment duration of 10 months in 2017 salary cost funds amounting to RON 4.129,4 thousand were foreseen;
- the amounts necessary for the granting of the vouchers in nominal value of RON 9,57, in the first quarter 2017, RON 12 in the second and third quarter 2017 and RON 15 in the fourth quarter 2017. This increase is in line with the provisions of Law 218/2016 amending Law 142/1998 on the granting of meal vouchers;
- expenses incurred on behalf of an employee related to voluntary pension schemes, up to an amount representing the RON equivalent of 400 EUR in a fiscal year, for each participant, in line with the collective labour agreement in force, art. 62, par (4);
- cost of voluntary health insurance premiums up to an amount representing the RON equivalent of EUR 250 in a fiscal year;
- expenses representing the participation of employees in the Company's profit under G.O. 64/2001 on profit distribution in national companies, companies publicly owned or controlled and the autonomous regies, as further amended and supplemented corroborated with art. 141 of the Collective Labour Contract in force within the company;
- a fund of RON 7.912,8 thousand for compensations regarding the continuation of employee redundancy on some positions which will be eliminated as a result of the organizational redesigning of some of the Company's activities. This fund was calculated for an estimated number of 150 employees, according to Art. 47 of the CLC. The provision of these funds represents an increase in the cost of personnel in the short term, but in the long term it is intended the obtaining of advantages by reducing the costs with the relevant employees, employed under individual labour contracts for an indefinite period of time.

Revenue substantiation was determined considering:

- the gas quantities estimated to be transmitted (including the quantities transmitted for storage) and the capacity booking estimated for 2017 – 2019;
- the gas quantities estimated to be procured for the physical balancing of the National Transmission System;
- The regulated transmission tariffs approved by the ANRE under Order 39/10 August 2016 on the approval of the regulated revenue, total revenue and transmission tariffs for the transmission of gas through the National Transmission System for the period 1 January 2017 - 30 September 2017, and for the period 1 October 2017 - 31 December 2019 based on the methodology approved by ANRE Order 32/2014 modified by ANRE Order 31/2016;
- The value of the international gas transmission service was estimated according to the existing contracts concluded with Gazprom Export Ltd for the pipeline sections 2 and 3;
- Based on the transmission capacities estimated for section 1 and of the regulated transmission tariffs approved by NERA by Order no 43 dated 24 August 2016 on the approval of the total revenue and of the transmission tariffs for the gas transmission activity related to the Isaccea 1 – Negru Voda 1 transmission pipelines.

The assumptions at the basis of the substantiation of the economic and financial indicators for the period 2017-2019 are as follows:

No.	Item	MU	2017	2018	2019
1.	Annual inflation ratio	%	1,4	2,5	2,3
2.	Rate of exchange	RON/EUR	4,46	4,44	4,42
3.	Rate of exchange	RON/USD	4,21	4,15	4,09
4.	Gas quantity transmitted (including storage injection)	MWh	123.536.826	123.536.826	123.536.826
5.	Average transmission tariff	RON/MWh	9,05	7,47	9,00
6.	Technological consumption procurement price	RON/MWh	71,27	71,27	71,27

Based on these assumptions the following economic and financial indicators resulted:

Thousand RON

No.	Indicators	2017 REB	Estimated for 2018	Estimated for 2019
1.	TOTAL REVENUE, of which:	2.205.866	2.907.885	2.383.430
1.1	Operating revenue before the construction activity according to IFRIC 12	1.577.348	1.386.245	1.585.779
1.2	Revenue from the construction activity according to IFRIC 12	597.692	1.488.055	759.374
1.3	Financial revenue	30.826	33.584	38.276
2.	TOTAL COST, of which:	1.834.295	2.640.629	1.947.762
2.1	Operating cost before the construction activity according to IFRIC 12	1.226.595	1.138.853	1.174.706
2.2	Cost of assets constructed according to IFRIC 12	597.692	1.488.055	759.374
2.3	Financial cost	10.007	13.720	13.681
3.	GROSS PROFIT	371.571	267.256	435.668
4.	TAX ON PROFIT	59.742	40.425	67.569
5.	NET PROFIT	311.829	226.831	368.099

The evolution of the economic and financial indicators during the estimated period is influence by:

- the commissioning of investment objectives;
- the progress National Transmission System rehabilitation and maintenance works;
- the evolution of the costs regarding procurement of gas for technological consumption;

Profit distribution was determined taking into account the provisions of G.O. 64/2001 on profit distribution in national companies, companies publicly owned or controlled and the autonomous regies, as further amended and supplemented and of the specifications approved by MPF Order 144/2005 approving the Specifications for the determination of the amounts subject to profit distribution according to G.O. 64/2001 on profit distribution in national companies, companies publicly owned or controlled and

the autonomous regies, approved as amended by Law 769/2001, as further amended and supplemented as follows:

- no amounts were distributed to legal reserves as they are currently constituted under the quota of 20% of the share capital, according to Art.183, paragraphs (1) and (2) of Law 31/1990, as further amended and supplemented, and the share capital is not expected to change;
- employees participation in the profit was determined within the limit of the monthly average base salary estimated per employee in the year for which the participation is granted, per average number of employees, obtained in the ended financial year;
- dividends to shareholders were determined according to MPF Order 144/2005, by applying 50% to remaining net profit after its recompletion with the amount of the cost representing the participation in profit, with which it was affected the gross profit before taxation;
- retained earnings for setting up own financing sources, was determined as the difference between the net profit to be distributed and the profit proposed to be allocated according to GO 64 / 2001.

The analysis of the 2017 REB economic and financial indicators as compared to the 2016 estimations

The 2017 REB indicators compared to the 2016 estimations are as follow:

thousand RON

No.	Item	Estimated in 2016	2017 REB	Variation
0	1	2	3	4=3/2-1
1.	TOTAL REVENUE, of which:	2.034.216	2.205.866	8,44%
1.1.	Operating revenue	1.883.155	1.577.348	-16,24%
1.2.	Revenue from the construction activity according to IFRIC 12	118.884	597.692	402,75%
1.3.	Financial revenue	32.177	30.826	-4,20%
2.	TOTAL COST, of which:	1.312.881	1.834.295	39,72%
2.1.	Operating cost	1.184.314	1.226.595	3,57%
2.2.	Cost of constructed assets according to IFRIC 12	118.884	597.692	402,75%
2.3.	Financial cost	9.683	10.007	3,35%
3.	GROSS PROFIT	721.335	371.571	-48,49%
4.	TAX ON PROFIT	125.625	59.742	-52,44%
5.	NET PROFIT	595.710	311.829	-47,65%

I. The revenue from the operation activity before the construction activity according to IFRIC 12 amounting to **RON 1.577.348 thousand** is lower by **RON 305.807 thousand** as compared to the 2016 estimated revenue, which is a decrease by 16,24%, mainly due to:

- The decrease of the revenues from the international gas transmission activity by **RON 4.529 thousand** due to the fluctuations in the exchange rate of the currency provided in the contracts concluded with Gazprom Export Ltd. And to the regulation of the transmission on the pipeline Isaccea 1 – Negru Voda 1 in line with the provisions of NERA Order no 34/2016 regarding the

Methodology for transmission capacity booking and setting gas transmission tariffs related to the gas transmission services through the gas transmission pipelines Isaccea – Negru Voda;

- the decrease of the revenue from gas transmission by **RON 241.848 thousand**, due to two factors:
- the decrease of the volumetric component by **RON 63.343 thousand** on account of the estimated quantities to be transmitted in 2017 lower than the ones transmitted in 2016;
 - the decrease of the capacity booking component by **RON 178.505 thousand** on account of the invoicing of the amount of the surplus of booked capacity in 2016 amounting to RON 143.132 thousand in line with NERA Order no. 1/18.01.2016, NERA Order no. 14/30.03.2016, NERA Order no 160/26.11.2016 and NERA Order no 39/10.08.2016 (revenues which are not present in the following years) and of the decrease of the booked capacity by RON 116.067.730 MWh on account of the reduction of the level of gas transmission tariffs for short term capacity booking products.
- the decrease of other operating revenue by **RON 58.380 thousand** due to the revenues related to the prescription of the delay penalties for the late payment of some dividends in 2000-2003 achieved in 2016, which are not found in the revenue of the following years.
- The decrease in the revenues from the NTS balancing by **RON 1.050 thousand** on account of the decrease of the quantity of gas meant for balancing the NTS.

Regarding the annual evolution of revenue from gas transmission:

Gas transmission is regulated by the National Energy Regulatory Authority (ANRE). According to the methodology for setting the regulating revenue, the costs savings of the transmission operator in a gas year and the additional revenue obtained in a gas year diminish the regulated revenue approved in the following gas years. In other words, the more effective the company is in reducing costs, the more the revenues from gas transmission will be reduced in the coming gas years.

According to ANRE Order 32/21 May 2014 *on the approval of the Gas Transmission Regulated Revenue, Total Revenue and Regulated Tariff Setting Methodology* the following are also considered at the determination of the annual regulated revenue:

- the correction component of the total revenue for the previous years;
- the correction component of the technological consumption for the previous years;
- the efficiency gain redistribution component obtained by the transmission operator in the first year of the regulatory period by the transmission system users in the first year of the following period (the savings obtained by the transmission operator regarding some cost items as compared to the levels approved by ANRE must be kept by the transmission operator over a period of 5 years; then they are redistributed to users by the diminishing of the annual regulated revenue with these savings).

All these provisions of the methodology may determine the reduction of the revenues from the transmission activity and hence the charges related to them with beneficial effects upon the users of the transmission system.

The application of the provisions of the methodology mentioned above determined, to a large extent, the decrease in revenues from gas transmission in 2017 compared to the level achieved in 2016.

Thus the regulated revenue approved for the period 1 October 2016 - 30 September 2017 recorded decreases mainly on account of savings on gas purchase costs related to technological consumption in the third and the fourth years of the third regulatory period (1 July 2014 - 30 September 2016) in the amount of RON **33.585** thousand and the recalculation of the total income for the years 2–4 based on the performed inflation.

The estimated revenue from the gas transmission activity for 2017, according to the tariffs approved by ANRE for the period 1 October 2016 - 30 September 2017 the estimated charges based on existing regulations for the fourth quarter of 2017 is RON 1.118.506 thousand, by RON 241.848 thousand less compared with 2016 preliminary.

Considering the above, we believe that the provisions of the Instructions for completing the REB approved by Order no. 20 /08.01.2016 of the Ministry of Finance, Annex 6 par.II.6 that *'the total revenue and expense is estimated, so the index related to the increase in total expenses usually does not exceed the total income growth index'* cannot be applied in the situation of Transgaz whose activity is regulated at a rate of approx. 80%.

EU Regulation 312/2014 establishing a network code on the gas transmission networks balancing provides uniform balancing rules at European level, reflecting the specific needs of the transmission system and take into account the levers of the operators for balancing the transmission systems. According to the Regulation mentioned above the role of the system operator is to perform balancing activities based on non-discriminatory market principles through the purchase/sale of natural gas quantities required for balancing. The system operator does not record gains or losses as a result of conducting the balancing activity.

The provisions of the Regulation mentioned above are taken over in the ANRE Order no.16/2013 on the approval of the Network Code for the National Gas Transmission System modified by ANRE Order no.160 /2015, which states in Article 83 (2) that *'to ensure the safe operation of the NTS, the TSO should have enough gas for system balancing as natural gas stored in pipelines and/or as balancing gas stored in underground storages, and to take NTS balancing actions including by conducting sales and/or purchasing transactions for the natural gas quantities required to balance the system in a transparent, non-discriminatory manner, by using market mechanisms'*.

When estimating the quantity of gas destined for NTS balancing, the quantities of gas purchased for the physical balancing of the NTS in 2016 were considered. This gas will be purchased in 2017 according to the needs in order to balance fluctuations in gas flow and to maintain the pressure values in order to enable the safe and efficient operation of the NTS.

II. Operating expenses before the construction activity according to IFRIC12 amounting to RON 1.225.348 thousand are by RON 41.034 thousand higher than the preliminary ones related to 2016, which represents their increase by 3,46%, determined mainly by:

- a) overriding in the following expense elements:

1. expenses with the services executed by third parties higher by **RON 91.373 thousand**;
2. the cost of gas procurement for NTS balancing higher by **RON 244 thousand** according to ANRE Order no.16/2013 approving the Network Code for the National Gas Transmission System modified by ANRE Order no.160/2015. Because according to the provisions of EU Regulation 312/2014 the system operator does not record gains or losses as a result of conducting balancing activities the revenues and expenses related to such activities were grounded in the draft of the revenue and expenses budget in the same amount.
3. Personnel salary expenses higher by RON **22.360** thousand mainly on account of the provision in 2017 of the funds for the payment of the salaries of the personnel to be employed for the BRUA and Moldova projects;
4. other material expenses and auxiliary materials higher by **RON 33.916 thousand**;

b) Economies especially in the following expense elements:

1. The cost related to the technological consumption lower by RON **4.445** thousand, due to the lower gas quantity as compared to 2016 by 5% (62.365 MWh);
2. Other operation related expenses lower by **RON 97.617 thousand**, mainly due to the adjustment of the provisions for the depreciation of current assets;
3. Expenses related to the royalty for the NTS concession lower by **RON 24.638 thousand** on account of the decrease of the revenue from gas transmission;

Financial expenses higher by **RON 324 thousand** because of the increase in the expenses related to the currency exchange rate differences.

III. The gross result estimated for 2017 is of **RON 371.571 thousand**, by RON 349.765 thousand (-49%) lower than the preliminary one for 2016.

IV. The tax on profit was calculated taking into account:

- ☞ The influence of the provisions for risks and expenses and of the provisions for the depreciation of current assets;
- ☞ The influence of the expenses related to the participation of the employees to the profit related to 2016 and of the rights related to the mandate contract to be paid in the following year;
- ☞ The social expenses exceeding the legal deductibility limit (Law 227/2015 - Tax Code Art. 25 (3) b) of 5% applied on the value of the wage bill;
- ☞ Sponsorship expenses granted within the legal limit (Law 227/2015 - Tax Code Art. 25 (4) let. i) of 0,5% of the turnover, but not more than 20% of the tax on profit.

Planning the investment financial effort related to 2017-2019

The total expenses for investment include funds for NTS development and modernization works, the amounts necessary for the repayment rates on loans employed by the company to finance the

investments which were not covered from own sources and the amounts required for the payment of guarantees related to the removal from the statute of agricultural land.

The sources for financing investment expenses are:

- Own sources including the amortization and the amounts distributed from the net profit to finance investments according G.O. no. 64/2001 regarding profit distribution to national societies, national companies and companies owned or majority state owned, as well as the autonomous administrations, as amended and supplemented;
- Amounts resulting from the absorption of European funds;
- Unused own resources from previous years and other sources.

The investment expenses were determined based on:

- The modernization and development investment program for 2017 and estimates for the period 2018-2019;
- The design software for investment works for 2017;
- The 10 years national transmission system development program.

A sustainable development of the transmission infrastructure in Romania requires an extensive investment program to enable the compliance of the National Transmission System (NTS) with the transmission and operating requirements of the European gas transmission network.

Considering the growing dependency of the European Union on gas imports coupled with the constantly increasing demand and the decrease of the domestic production ensuring the security of gas supply constitutes a need.

Taking into account the perspective of the implementation of some new projects aimed at the diversification of gas transmission routes from the Caspian Sea region towards Central Europe, as well as some new off-shore gas sources in the Black Sea Transgaz aims at achieving a new gas transmission corridor to ensure the recovery of gas volumes from these sources on the Romanian and European market and the possibility of permanent bi-directional gas flow in the interconnections with Bulgaria and Hungary.

The development of the National Gas Transmission System in Romania on the corridor Bulgaria-Romania-Hungary-Austria (BRUA) - execution works Phase 1 which is part of the project - 'Gas pipeline from Bulgaria to Austria via Romania and Hungary' (PCI - 7.1.5 – on the first PCI list) consists in the construction of a new gas transmission pipeline to connect the new Technological Node Podișor to the Gas Metering Station Horia in the Podișor – Corbu – Hurezani – Hațeg – Recaș – Horia direction with an average length of approximately 528 km and a diameter Dn 800.

By the implementation of the BRUA project Phase 1 the following objectives will be reached:

- The diversification of gas supply sources of European countries,
- The transmission to the Central European markets of the gas reserves in the Caspian region,
- Ensuring in the Bulgaria direction a transmission capacity of 1.5 bcm/year;
- The development of a transmission capacity in the Hungary direction of 1.75 bcm/year;
- The security of gas supply to Romania by access to new gas sources.

This transmission pipeline will allow in the future the interconnection to the pipelines with the potential supply sources of liquefied gas at the Black Sea shore (AGRI Project) and the Black Sea gas.

For this project, by the application form submitted to the European Commission on 10.12.2015, a financial aid was sought through the CEF mechanism, amounting to 50% of the eligible investment costs.

In the meeting dated 19.01.2016 of the CEF-Energy Coordination Committee, the European Union allocated **EUR 179.3 million** for the execution of the first stage of the project proposed by Transgaz according to the first PCI List /2013 `Gas pipeline from Bulgaria to Austria via Romania and Hungary`, with the name - according to the Development Plan of the National Gas transmission System 2014 - 2023 (TYNDP) - `Development on the territory of Romania of the National Gas transmission Systems along the corridor of the transmission pipeline Bulgaria - Romania - Hungary - Austria` - (abbreviated BRUA) - the first stage.

On September 9, 2016, in Budapest, Transgaz signed with the representatives of the European Commission, the Grant Agreement through the Connecting Europe Facility related to the pipeline route through Romania on the transmission corridor Bulgaria-Romania-Hungary-Austria (BRUA). By means of this Agreement Transgaz receives a grant amounting to **EUR 179.32 million** for the implementation of the BRUA Project Phase I.

The financing of the total investment cost was provided to be ensured from own sources (amounts from the net profit and depreciation) European funds and bank loans.

The progress in the implementation of major investment projects of Transgaz SA, requires the performance of parallel steps to ensure the financing of the 10-year National Transmission System development plan. In the years 2017-2019 the company aims at attracting funds from the banking system to complement the necessary financing.

The synthesis of the investment expenditure for the period 2017-2019 as well as their financing is indicated below:

** thousand RON **

No.	Item	2017	2018	2019	Total
					2017-2019
0	1	2	3	4	5=2+3+4
I.	Investment expenses, of which:	712.157	1.523.376	776.277	3.011.811
1.1.	Investments	704.141	1.515.957	764.574	2.984.672
1.2.	Capitalized interest	223	7.419	11.703	19.345
1.3.	Loan repayment	0	0	0	0
1.4.	Guarantees for the lands	7.794	0	0	7.794
II.	Financing sources, of which:	1.244.992	1.523.376	776.277	3.011.811
2.1.	Own sources, of which:	286.653	262.509	337.980	887.141
	-amounts from the net profit	149.903	107.361	177.995	435.259
	- amortization	136.750	155.147	159.985	451.882
2.2.	European funds	8.367	265.473	242.245	516.085
2.3.	Bank loans	66.900	462.560	188.258	717.718
2.4.	Receipts from the guarantees for the lands			7.794	7.794
2.5.	Surplus/deficit from previous years	883.072	532.834	0	883.072
III.	SURPLUS/DEFICIT(II-I)	532.834	0	0	0

Other additional information

1. The substantiation of the remunerations related to the non-executive and executive members of the Board of Administration

The amounts related to the mandate contract of the director general/executive administrator were determined based on the remunerations set in the mandate contract and in the provisions of GEO no.109/30 November 2011 *on corporate governance of public enterprises, as amended and supplemented*, and it is a fixed monthly allowance and an annual variable remuneration component. The annual variable remuneration component to the mandate contract of the Director general /executive administrator consists of the annual bonus for the performance indicator on EBITDA + the annual bonus for the performance indicator on operating expenses excluding depreciation + the annual bonus for the performance indicator on investments.

The amounts related to the mandate contract of the non-executive administrators (a total of 4 contracts) were determined based on the remunerations set in the mandate contracts and the provisions of GEO 109/30 November 2011 *on corporate governance of public enterprises, as amended and supplemented*, and it is a fixed monthly allowance and an annual variable remuneration component. The annual variable remuneration component to the mandate contracts of non-executive administrators is made of the annual bonus for the performance indicator on EBITDA + the annual bonus for the performance indicator on operating expenses excluding depreciation + the annual bonus for the performance indicator on investment.

The variable remuneration of the Director General and of the Board of Administration was approved by Resolution No. 9 of 23 September 2013 of the Ordinary General Meeting of Shareholders, Article 2 respectively with the approval of the contract template that is to be concluded with the members of the Board of Administration of Transgaz SA, as approved by the majority shareholder Romanian State represented by the Ministry of Finance and published on the website of TRANSGAZ SA by address nr.5917/28.08.2013.

The payment of the Bonus for the performance indicator 'EBITDA' is made in four equal instalments payable quarterly during the fiscal year and the adjustment shall be made according to the results actually achieved in that particular year within 30 days from the date of approval by GMS of the audited annual financial statements, the TRUSTEE will repay the full value of the bonus if the performance indicator in question is not fulfilled.

The payment of the bonuses for the performance indicator on 'Operating expenses (excluding depreciation)' and for the performance indicator on 'Investment' is made **within 30 days from the date of approval by the general meeting of shareholders** of the audited annual financial statements for the year for which those respective bonuses were determined.

2. The substantiation of the economic-financial indicators which are facing a significant increase as compared to the same period of the previous year

The expenses related to goods and services were forecasted by **49,22%** higher. The main causes which determined this increase are:

- The increase of the expenses related to the purchase of the gas required for NTS balancing according to ANRE Order no.16/2013 approving the Network Code for the National Gas Transmission System modified by ANRE Order no.160 / 2015. In estimating the quantity of gas necessary to balance the NTS the quantities of gas purchased for NTS physical balancing in 2016 were considered. These quantities of gas will be purchased in 2017 according to the needs in order to balance the fluctuations in gas flow and pressure to maintain the values that enable safe and efficient operation of the NTS.
- The increase of the expenses related to consumables by 85, 48% and of the expenditure related to materials and inventory objects by 411, 88%. These expenses were set according to the schedule for supply of materials and spare parts needed for maintenance works, repairs, interventions and special operations and materials for the normal activity. At the substantiation of this program the material stocks estimated for the end of 2016 and the procurement contracts in progress were considered;
- The increase of energy and water related expenses (12,46%) due to the increase in electricity consumption because of a connection to the power supply network of the new objectives that will be put into operation (technology nodes, SCADA system, metering regulating stations);
- The increase of the expenses related to the maintenance and repair by RON 70.329 thousand (808,24%) due to the increase of the maintenance program by approximately RON 63.000 thousand for 2017. The program for the scheduled repairs to pipelines for 2017 includes mainly: the works started and unfinished provided in the relevant program of 2016, the works included in the program of 2016 but which were not promoted to execution (mainly due to the lack of the execution documentation or permits) and the new works proposed as a result of events/anomalies /incidents occurred during the previous years and that need to be resolved in 2017. All the works were initiated as a necessity by the design themes underlying the execution based on the technical projects or evaluation reports related to pipes diagnostic methods (external or intelligent pigs). Out of the works proposed for the works program, most of them are substantiated by projects endorsed by the T.E.C of Transgaz;
- The increase in expenses with the commissions and fees by 449,19%. These expenses consist mainly of expenses for legal advice (RON 2.700 thousand), representing consultancy, assistance and the legal representation of a law firm with international expertise in the Community competition law, approved by the Resolution of the EGMS no 6/2016 and consultancy, assistance and the legal representation needed to implement the European regulations in force and future incidence in the company's business, the implementation of rules relating to the financing of energy infrastructure by CEF mechanism and providing legal expertise in international and European regulations, approved by the EGSM Decision no.2 / April 29, 2014;
- Increase in banking and similar expenses (633.33%) on account of costs payable to the European Bank for Reconstruction and Development amounting to RON 1,784 thousand prior to the grant of a loan to finance major investment projects;
- increased expenditure on maintenance and operation of computer technology (40.45%) due to supplementation of platform GMOIS maintenance costs and inclusion in the proposed budget of programming services of information systems and user software;

- The increase in other expenses with services performed by third parties (59,87%) substantiated based on the program for other services performed by third parties.

We would like to mention that the programs for NTS upgrading and development (Investments) design, maintenance and NTS rehabilitation, materials and spare parts supply and the program related to other services performed by third parties, which substantiated the abovementioned expenses were approved by the Board of Administration.

Transgaz employs bank loans in the period 2017 - 2019 for financing projects in the development plan, which is why, in accordance with IAS 23 'Borrowing Costs', the company capitalized interest and expense attributable to those loans.

According to the provisions of Transgaz' Articles of Incorporation, in force, Chapter IV, art 15, par 3, letter c), **we would like to kindly ask the General Meeting of the Shareholders to approve the revenue and expense budget for 2017 and the estimates for 2018-2019**, according to the provisions of GO no. 26 on 21 August 2013, art. 4, par. 1, letter d).

Enclosures:

- The revenue and expense budget for 2017 and the estimates for 2018-2019: Annex no.1*;
- The detailing of the economic-financial indicators provided in the revenue and expense budget and their split by quarters: Annex no 2*,
- The execution rate of the total revenues: Annex no.3*;
- The investment program and sourcing of investment funding: Annex no.4*;
- Means to improve the gross result and the reduction of outstanding payments: Annex no. 5*;
- The revenue and expense budget for 2017: Annex no. 6.

***Note: Annexes 1 – 5 will not be made public**

Chairman of the Board of Administration
Ion Sterian

Economic operator: S.N.T.G.N. Transgaz S.A. Medias
 Headquarters: 1 C.I. Motas Sq., Medias
 VAT number: RO 13068733

REVENUE AND EXPENSE BUDGET
for 2017

RON thousand

		INDICATORS	Row no.	REB 2017
0	1	2	3	4
I.		TOTAL REVENUE (row1=row2+row5a+row5+row6)	1	2,205,866
	1	Tota operating revenue before the construction activity according to IFRIC 12	2	1,577,348
		a) subsidies according to the applicable laws	3	
		b) transfers according to the applicable laws	4	
	2	Revenue from the construction activity according to IFRIC12	5a	597,692
	3	Financial revenue	5	30,826
	4	Extraordinary revenue	6	
II		TOTAL EXPENSE (row7=row8+row20+row20a+row21)	7	1,834,295
	1	Operating expense before the construction activity according to IFRIC12, of which:	8	1,226,595
		A. Expense with goods and services	9	369,981
		B. Expenses with taxes, charges and similar	10	210,859
		C. Expense with personnel, of which:	11	424,336
		C0 Salary-related costs (row13+row14)	12	322,425
		C1 Salary costs	13	282,101
		C2 Bonuses	14	40,324
		C3 Other personnel expense, of which:	15	7,913
		Compensation expense related to employees layoffs	16	7,913
		C4 Expense on mandate contract and other governing and control bodies, commissions and committees	17	4,543
		C5 Insurance and social security, special funds and other legal obligations expense	18	89,455
		D. Other operating costs	19	221,420
	2	Cost of assets built according to IFRIC12	20a	597,692
	3	Financial costs	20	10,007
	4	Extraordinary costs	21	
III		GROSS RESULT (profit/loss)	22	371,571
IV		TAX ON PROFIT	23	59,742
V		ACCOUNTING PROFIT REMAINING AFTER THE DEDUCTION OF THE TAX ON PROFIT, of which:	24	311,829
	1	Legal reserves	25	
	2	Other reserves representing tax incentives provided according to the law	26	
	3	Covering accounting losses in the previous years	27	
	4	Establishment of own financial sources for the projects cofinanced by foreign loans as well as establishment of the sources necessary for the capital repayments, interest payment and other costs related to these foreign loans	28	
	5	Other assignments provided by law	29	

		INDICATORS	Row no.	REB 2017
0	1	2	3	4
	6	Accounting profit left after the deduction of the amounts in row 25, 26, 27, 28 and 29.	30	311,829
	7	Employees share to the profit within the limit of 10% of the net profit, but no more than the level of an average monthly salary of the economic operator during the reference financial year	31	12,024
	8	Minim 50 % payments to the State or local budget, for the autonomous companies, or dividends for the national companies or the entirely or partially owned-by the state companies, of which:	32	161,927
	a)	- dividends to the state budget	33	94,743
	b)	- dividends to the local budget	33a	
	c)	- dividends to other shareholders	34	67,184
	9	Profit not assigned for the destinations provided at row 31 - row 32 is assigned to other reserves and it is an own financing source	35	149,903
VI		INCOME FROM EUROPEAN FUNDS	36	
VII		ELIGIBLE COSTS FROM EUROPEAN FUNDS, of which:	37	
	a)	material costs	38	
	b)	salary costs	39	
	c)	service supply costs	40	
	d)	publicity costs	41	
	e)	other costs	42	
VIII		INVESTMENT FUNDING SOURCES, of which:	43	1,244,992
	1	Budget allocations	44	
		Budget allocations regarding payment of commitments from the previous years	45	
IX		INVESTMENT COSTS	46	704,364
X		SUBSTANTIATION DATA	47	
	1	No. of personnel estimated at the end of the year	48	4,686
	2	Total average no. of employees	49	4,679
	3	Average monthly income per employee (RON/person) determined based on the salary costs*)	50	5,282
	4	Average monthly income per employee determined based on the salary costs (RON/person) (row13/row49)/12*1000	51	5,024
	5	Labour productivity in units of value per total average personnel in current prices (RON/person) (row 2/row 49)	52	337
	6	Labour productivity in physical units per total average personnel (physical units/person)	53	0.0000
	7	Total costs at RON 1000 total income (row 7/row 1)x1000	54	832
	8	Outstanding payments	55	0
	9	Outstanding debt	56	255,126

DIRECTOR GENERAL,
Petru Ion Vaduva

		INDICATORS	Row no.	REB 2017
0	1	2	3	4

CHIEF FINANCIAL OFFICER,
Marius Lupean