

REPORT

on proposal for amending the performance indicators included in the Directors Agreement

I. Directors Agreement and Governing Plan

By Resolution no 12 of **July 26, 2013**, The General Meeting of Shareholders, approved the form of **Director Agreement** to be concluded with the Directors of the Board.

Director Agreement also includes clauses concerning the revision/updating of the performance indicators, as follows:

- ⌘ *Article 4: "...The Director will execute all acts required.... in order to achieve the objectives and performance criteria established in Annex 1 to this document together with the other Directors of the Board, and/or as annually amended, as the case may be, within 30 days from the approval/amendment of the income and expenditures budget."*
- ⌘ *Article 9: "The Director undertakes, together with the other Directors, to fulfil the governing plan and GMS resolutions, in order to achieve the objectives and performance criteria established in Annex 1 to this Director Agreement. Performance criteria and objectives are applicable during the entire assignment of the Director, and the values of the performance indicators will be updated annually in accordance with the provisions of the income and expenditure budget."*

By Resolution no 16 as of **September 25, 2013**, The General Meeting of Shareholders approved the **Governing Plan of the company for the period 2013-2017**, presented and prepared by the Board of Directors.

The Governing Plan also provides the possibility to amend the performance indicators, mentioning the fact that the achievement of the indicators initially assumed by the directors is conditioned upon assignments undertaken by the state authorities, as follows:

- ⌘ *"The performance indicators provided in this plan, resulting from the strategic objectives and the action plan to be achieved for fulfilling such objectives, shall be reviewed in order to be approved by the General Meeting of Shareholders, if it is found that for reasons beyond the director's control, for external factors (the decline of the natural gas market and the electricity market, changes in the legal and regulatory frame etc.) or as a result of restating the financial statements in compliance with the International Financial Reporting Standards (IFRS) the objectives and the performance indicators cannot be fulfilled"- Summary of the Governing Plan (last paragraph);*
- ⌘ *"The fulfilment of the performance indicators is conditional upon:*
 - *Compliance with the country's commitment to gradually increase the Romanian market sale price for domestic gas production to reach the convergence with the Romanian market sale price for import gas until December 31, 2018. The Commitment has been undertaken by the Letter of Intent signed with the International Monetary Fund, and by the Memorandum of Understanding signed with the European Commission, integral part of the Precautionary Stand-By Arrangement signed with the International Monetary Fund and the European Commission;*

- ANRE compliance with legal provisions on adjusting the regulated income and underground gas storage tariffs.

.....
In case, other circumstances or events beyond Romgaz control require it, the Governing Plan shall be amended/modified/supplemented accordingly as regards the level of the performance indicators” – item 4.7 Performance criteria and objectives of the Governing Plan (page 76 – last paragraph);

Although, (1) the country’s commitment to gradually increase the Romanian market sale price was not met, (2) the Romanian Government initiated a series of fiscal regulations with a significant impact on the company’s performance and (3) the national gas consumption recorded a significant decrease, the company’s management fulfilled its performance criteria and objectives initially asumed until March 31, 2016, as shown in the table below:

	3 months	6 months	9 months	12 months
2014	112.21%	122.25%	112.18%	113.62%
2015	143.36%	126.64%	110.98%	103.38%
2016	101.97%	90.70%	88.34%	86.36%

II. Actions caried on as a result of contingencies which require the modification of performance indicators.

From the first year of the mandate, a number of contingencies arrised beyond the control of the board of directors or of the company’s management that impede the fullfilment of the objectives and performance indicators included in the Directors Agreement and Governing Plan, respectively, such as:

- ✍ non- compliance with the calendar related to the gradual increase of the market sale price for domestic gas production considered in the preparation and approval of the Governing Plan;
- ✍ fiscal regulations with a significant impact on the company’s performances, such as:
 - extending beyond December 31, 2014 the period for applying the windfall tax for gas producers as a result of price deregulation;
 - initiation of the tax on special constructions as of January 1, 2014, the so called “pole tax”
- ✍ reduced national gas consumption.

As a result, in accordance with the provisions of the Governing Plan and the Directors Agreement, the company’s Directors requested to shareholders to amend the calculation method of performance indicators included in the Directors Agreement. The request was substantiated under the Note no 13293 of May 16, 2016 presented to shareholders and discussed during the ordinary meeting of **June 16, 2016**.

Further the analysis of the substantiated requests within the note, the General Meeting of Shareholders approved under item 1 of Resolution no 5 as of June 16, 2016 “*the amendment of calculation method of performance indicators, namely by eliminating the effects of the influence of external factors that are beyond the control of the company’s management*”. The General Meeting of Shareholders approved under Item II of the same Resolution “*the*

conclusion of an Addendum to the Directors Agreement for amending the calculation method of performance indicators, namely by eliminating the effects of the influence of external factors that are beyond the control of the company's management", mandating the representative of the majority shareholder to sign the Addendum to the Directors Contract (item III).

Further the request of the Ministry of Energy, as a majority shareholder, the agenda of the Ordinary General Meeting of Shareholders of **August 11, 2016** was supplemented with the proposal for canceling the approvals issued by the GMS during the meeting held on June 16, 2016 concerning the amendment of calculation method of performance indicators, conclusion of an Addendum to the Directors Agreement and mandating the representative of the majority shareholder to sign it. GMS approved the requests formulated by the Ministry of Energy under the Resolution no 7 as of August 11, 2016.

On the Agenda of the Ordinary General Meeting of Shareholders of **November 15, 2016**, was included an item, for review and approval, namely *Report No. 25988 of October 5, 2016 on the proposal for amending the performance indicators included in the Directors Agreement*. The Board of Directors requested under this Report *"to set the performance indicators at the level of Budget indicators, as approved by the General Meeting of Shareholders under the Resolution No. 5 of June 16, 2016"*. The GMS did not approve under the Resolution No. 10 of November 15, 2016 *"the performance criteria and objectives in correlation with the budget of S.N.G.N. ROMGAZ S.A. as approved under Resolution No. 5/2016"*.

III. The effects of canceling the provisions of GMS Resolution No. 5/2016 related to performance indicators

In accordance with the provisions of Article 9, paragraph (1) letter c) of Government Ordinance no 26 as of August 26, 2013 on strengthening the financial discipline at the level of economic operators where the state or the administrative-territorial units are sole or majority shareholders or hold directly or indirectly a majority participation, *for the substantiation of the income and expenditures budget the following are taken into consideration: "the specific performance criteria and quantified objectives on reducing the outstanding payments and debts, reducing the losses, increasing the profit, revenue and labour productivity as well, as provided in the mandate contracts established in connection with the governing strategy of the Board of Directors/Supervision Commission and governing plan of the directors/members of economic operators directorate"*.

As a result, the income and expenditure budget for the year 2016 has been prepared taking into consideration the amendment of calculation method of performance indicators, namely by eliminating the influence of the external factors that are beyond the control of the company's management. The income and expenditure budget was subject to the shareholders analysis during the meeting of June 16, 2016 (Item IV on the agenda), when Item 1 on the same Agenda concerned the approval of the amendment of calculation method of performance indicators.

The General Meeting of Shareholders approved at the meeting of June 15, 2016 the amendment of the performance indicators calculation method (Item I), the conclusion of an Addendum of the Directors Agreement including the amendment from Item I (Item II) and the mandating of the majority shareholder representative to sign the Addendum of the Directors Agreement (Item III), as well as the Income and Expenditure Budget as it was presented by the company's management, respectively by taking into consideration the amendment of the performance indicators calculation method (Item IV).

Due to the fact that by Resolution No. 7/August 11, 2016 of the General Meeting of Shareholders the approvals included in Items I, II and III of Resolution No. 5/ June 16, 2016

were revoked, we consider that, along with the revocation, the directors have no longer performance indicators.

IV. Request

Whereas:

- The provisions of the Directors Agreement which offer the possibility to an annual update of the performance indicators value;
- The approval by the General Meeting of Shareholders from June 16, 2016 to amend the performance indicators calculation method, to conclude an Addendum of the Directors Agreement and to mandate a representative of the majority shareholder to sign the Addendum of the Directors Agreement;
- The approval by the General Meeting of Shareholders of the Income and Expenditure Budget for 2016 which was substantiated taking into account the amendment of the performance indicators calculation method.

The Income and Expenditure Budget basically represents the main instrument for programming the financial results as well as the necessary funds, the budget's elaboration and performance, based on the principles of maximum efficiency and financial equilibrium. The role of the Income and Expenditure Budget is to reflect the modality of formation, administration and use of financial means and to ensure the provision of the information necessary to substantiate the decisions regarding the company's management.

At the same time, the Income and Expenditure Budget may be considered a complex of actions materializing in a final document expressing the efficiency of the general activity of the company by cumulating the income, expenses and results of a financial year. Consequently, the Income and Expenditure Budget appears as a system of correlated annexes reflecting the objective of the economical-financial strategy of the company.

The Income and Expenditure Budget is drawn up, based on the substantiation of each indicator in its smallest detail, by the company's management and after that it is analysed and endorsed by the Board of Directors, analysed for approval by shareholders during the General Meeting of Shareholders, according to the legal provisions in force¹ and the company's Articles of Incorporation².

Once approved by shareholders, the Income and Expenditure Budget indicators are the tasks of the Board of Directors and the company's management. Consequently, the accomplishment of the Income and Expenditure Budget indicators should go hand in hand with the remuneration system of the board of directors and the company's management.

- Revocation by the GMS on August 11, 2016 of the previous resolution regarding the amendment of the performance indicators calculation method, the conclusion of an

¹ According to the provisions of Article 4, paragraph (l) letter d) of the Government Ordinance No.26/August 21, 2013 as amended by Government Ordinance No. 11/January 27, 2016, the income and expenditure budgets of economic operators are approved by „the Resolution of the General Meeting of Shareholders [...] in the case of economic operators whose shares are admitted to trading on a regulated market [...]”

² According to the provisions of Article 4 letter d) of the company's Articles of Incorporation, the Ordinary General Meeting of Shareholders is empowered to ”establish the Income and Expenditure Budget, for the next financial year”.

Addendum of the Directors Agreement and the mandating of the representative of the majority shareholder to sign it.

- GMS did not approve the proposal related to setting the performance indicators at the level of Budget indicators, therefore the amendment of the performance indicators calculation was not approved,

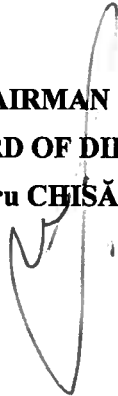
we propose a new approach as far as regards the application of the provisions of Article 9 of the Directors Agreement on the modification of the performance criteria and objectives, as follows:

- Amendment of the calculation method, as presented in Chapter 4.7 of the Governing Plan approved by Resolution No. 12/July 26, 2013 of the General Meeting of Shareholders, modification of performance criteria in order to substitute the reporting base represented by the average for the previous three years with quarterly allocation afferent to the Income and Expenditure Budget;
- Establishing the performance indicators at Income and Expenditure Budget level which should be approved by GMS.

In this respect, in order to eliminate the effects of the revocation of Resolution No. 5/2016 of the GMS provisions regarding the performance indicators, we hereby submit the following, when applying the provisions of Article 9 of the Directors Agreement, to analysis and approval:

- **Amendment of the calculation method of the performance indicators weighing coefficients as provided above, as well as the amendment of the Governing Plan, in this respect;**
- **Approval of the performance criteria and objectives as presented in Annex 1 to this Report.**

**CHAIRMAN OF
THE BOARD OF DIRECTORS
Dumitru CHISĂLIȚĂ**



Annex 1

**Performance indicators and criteria
(according to the Income and Expenditure Budget)**

Item no.	Indicator	M. U.	Performance criterion	Weighing factor	3 months 2017	6 months 2017	9 months 2017	Year 2017
0	1	2	3	5	6	7	8	9
1.	EBITDA	RON thousand	increasing	0.25	738,857	1,092,836	1,394,525	1,925,007
2.	Revenue	RON thousand	increasing	0.20	1,370,558	2,074,364	2,716,967	3,801,946
3.	Labour productivity	RON/person	increasing	0.10	218.03	329.37	430.92	602.53
4.	OPEX to Ron 1,000 operating income	RON	decreasing	0.10	555.44	632.74	674.16	653.21
5.	Geological resources	million m ³	increasing	0.10	650.00	1,400.00	2,100.00	2,500.00
6.	Natural gas production decline		maintaining	0.15	1,337	2,468	3,488	4,751
7.	Outstanding payments	RON thousand	maintaining	0.10	0	0	0	0

CHIEF FINANCIAL OFFICER

Andrei BOBAR

