

ROMGAZ



Societatea Națională de Gaze Naturale Romgaz S.A. - Mediaș - România

NR. 7132 / 10.03.2014

TO: European Bank for Reconstruction and Development
Eric Rasmussen
Director Natural Resources

Subj: Answers requested related to the EGMS agenda

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Dear Sir,

Before replying to every question and request for clarification contained in the above-mentioned letter, we make a short presentation on the modality and the legal and formal framework under which Romgaz Board of Directors issued the endorsement of Romgaz conditional participation to the "Hidro Tarnita S.A." and "HVDCC Romania-Turkey S.A." project companies.

- i. Romgaz is a joint-stock company whose activity is governed and regulated by normative acts enforced as provided in the Constitution, organic laws (article 76 paragraph 1 of the Constitution of Romania) and other acts of normative nature with special applicability for companies. We principally refer to the provisions of Law No. 31/1990 on companies, as amended from time to time, the provisions of Emergency Government Ordinance no. 109/2011 on corporate governance of public companies, as amended from time to time by Emergency Government Ordinance no. 51/2013, the provisions of the Emergency Government Ordinance no. 79/2008 on economic and financial measures in connection with economic operators as amended by Law 203/2009 as amended from time to time, and to the company's Articles of Incorporation.

Moreover, in view of the fact that as of November 12, 2013 the shares issued by the Company are traded on the regulated market managed by S.C. Bursa de Valori București S.A. and that the shares issued by the Company are support for the GDRs issued by The Bank of New York Mellon with the agreement of the Company which are traded on the London Stock Exchange, the company complies with and applies the capital market legislation.

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- II. Romgaz corporate bodies are: General Meeting of Shareholders, Board of Directors and Director General. Romgaz has a one-tier management board, the Board of Directors. The Board of Directors delegated the management of the company to a Director General in accordance with the legal and statutory provisions in force and applicable, respectively. **The General Meeting of Shareholders is the supreme body of management and decision making of the Company and has the power to decide over any problems in connection with the Company's activity.**

In accordance with the express provisions contained in the Law 31/1990 on companies:

Article 117 par.(1) *Any time it is deemed necessary, the general meeting is called for gathering by the board of directors, or the directorate if applicable.*

Article 119 par (1) *The board of directors, or the directorate if applicable, calls the immediate gathering in general meeting upon the request of the shareholders holding together or individually at least 5 % of the share capital or a lesser percentage, in case the articles of incorporation provides for it and the request contains provisions within the area of competencies of the shareholders' meeting.*

- III. In accordance with Emergency Ordinance no. 109/2011 on corporate governance, the Romanian State through the Department for Energy (shareholding of 70.0071% of the share capital of Romgaz) is the tutelary authority of Romgaz (defined as public enterprise – commercial company).

As majority shareholder and tutelary authority the Department for Energy also has the following rights, obligations and powers in connection with governing a commercial company, specifically Romgaz as well (regulated by article 2 and 3 of Government Emergency Ordinance no. 109/2011):

- *exercises on behalf of the State the capacity as shareholder;*
- *may exercise, as shareholder, a determinant influence by reason of some clauses enabling the setting of the management strategy of the public enterprise;*
- ***to ensure the transparency of the State's shareholding policy in the company's where it exercises the competence as public tutelary authority;***
- *to monitor the exercise in economic and strategic conditions of the shareholding capacity in a public enterprise;*
- ***to monitor the compliance of the monitored company with economic efficiency and profitability principles;***

- IV. Within the presented applicable framework, the Department for Energy, through the General Direction for Privatization and Management of State Ownership in Energy requested to the Board of Directors on behalf of the Romanian State as shareholder holding 70.0071% of the share capital of Romgaz in letters no. 150120/January 16 2014 and no. 150370/February 07, 2014 registered with Romgaz under no. 1273/January 17, 2014 and no. 4140/February 07, 2014 to call for gathering of Romgaz Extraordinary General Meeting of Shareholders, having the following items on the agenda:

- the approval of Romgaz participation to the increase of the share capital of Hidro Tarnita SA by subscribing to 89,000 newly issued shares of 100 lei nominal value issued by Hidro Tarnita SA in accordance with the endorsement of the Board of Directors;
- approval for including in the 2014 budget draft the amounts required for paying the subscribed shares;

- the approval of Romgaz participation to the establishment of HVDCC Romania-Turkey S.A. Project Company by subscribing and paying the equivalent in lei of 2,000,000 shares of EUR1 nominal value;
- approval for including in the 2014 budget draft the amounts required for paying the subscribed shares issued by the HVDCC Romania-Turkey S.A. Project Company.

The Board of Directors has endorsed Romgaz participation to the share capital of Hidro Tarnita and of HVDCC Romania-Turkey S.A. Project Company, subject to the conditions contained in Resolution No.2/2014 and has fulfilled the legal obligation to call for gathering the GMS and to set the agenda as per the requirements of the company's majority shareholder.

With respect to the endorsement: Romgaz through its statutory bodies considers the projects which have potential for the company's development in terms of both its main scope of activity - hydrocarbon exploration and production – and its secondary scope of activity included in the company's charter. It directly reflects Romgaz option to become more dynamic and business-oriented once the private management was implemented and the company was listed.

Romgaz reviews on these development projects proposals are made by aligning the proposals to the company's development objectives, its economic viability and potential benefit considerations, the creation of plus value for its investors, the conformity with the applicable legislation and last but not least with the national energy strategy.

Against this background, Romgaz intends and is obliged to review any business opportunities it determines from the current activity of the company and **also from proposals made by its shareholders**. These proposals are considered in a transparent, objective and non-discriminatory manner in relation to the party submitting them for analysis.

Romgaz management considered and consulted all documents that the projects initiators were able to make available and prepared a point of view which was submitted to the Board of Directors for endorsement, and, according to the Resolution no. 2/2014, the Board of Directors agreed in principle to Romgaz participation to these projects subject to the imposed conditions. The Board of Directors endorsement in this form shall be reviewed and voted on during Romgaz GMS.

The decision of the Board of Directors to grant the endorsement is a statutory one; it has also been recorded in the minutes of the meeting, which contains the name of the participants, the order of deliberations, the decision made, the number of casted votes and the separate opinions.

The Board of Directors' endorsement is *de facto et de jure* consultative, it may support the decision-making process, and represents the authorized opinion expressed by the Board of Directors as competent body, but it is not conditional, does not oblige the body requiring it and can disregard it.

Please find below the specific answers:

- 1) ***How was it decided that Romgaz should be part of Hidro Tarnita project and the submarine interconnection cable project (jointly referred to as "the Projects")? Which is the authority responsible of the decision?***

a) Submarine Interconnection cable

The Governmental Memorandum dated December 16, 2013 stipulates under item IV Proposals the following:

"The **expedient** establishment of the Project Company "HVDCC Romania – Turcia S.A." – a Romania– Turkey joint venture company where each party holds 50%, responsible for the re-evaluation and the update of the feasibility study in line with the requirements of the Turkish partner, including the increase of export capacity from 800 to 1600 MW, as well as securing the financing, construction and operation of the project "Submarine interconnection cable 400KV Romania – Turkey".

The Project Company "HVDCC Romania – Turcia S.A." shall be incorporated as a joint stock company, in accordance with the Company Law no. 31/1990, republished, as amended or added from time to time, by subscription of an equal number of shares by the founding shareholders, namely CNTEE Transelectrica S.A., SN Nuclearelectrica S.A. , Societatea Complexul Energetic Oltenia S.A., S.C. Romgaz S.A., Societatea Hidroelectrică S.A., S.C. Electrica S.A. and S.C. Complexul Energetic Hunedoara S.A."

The same document stipulates under item III Current status of the project that:

"... the government program of Romania for 2013 – 2017 the project "Submarine interconnection cable 400KV Romania – Turkey" has been considered a priority project,...."

b) Hidro Tarnita project

The Governmental Memorandum dated October 16, 2013 stipulates under item IV Proposals the following:

"The expedient establishment of "Hidro Tarnița S.A." project company through the participation of 6 companies from the energy sector where the State holds an integral or a majority stake, namely: HIDROELECTRICA S.A., ELECTRICA S.A., NUCLEARELECTRICA S.A., ROMGAZ S.A., COMPLEXUL ENERGETIC OLTENIA S.A. and COMPLEXUL ENERGETIC HUNEDOARA S.A., as follows:

- as a first phase, Electrica S.A. and the Complexul Energetic Hunedoara S.A. shall establish the joint-stock company "Hidro Tarnița S.A." with the minimum equity capital required by law;
- in parallel, with respect to the other participating companies, the general shareholders' meetings shall be called for gathering in accordance with the applicable formalities for the purpose of approving their participation to the increase of the equity capital of "Hidro Tarnița S.A.", as a second phase.

In parallel, all six shareholders shall comply with the procedures provided in their respective articles of incorporation with respect to obtaining the approval of the Shareholders' Agreement on the increase of the equity capital of "Hidro Tarnița S.A." through cash contributions of EUR 2(two) million from each of the six shareholders as well as through in kind contributions of tangible and/or intangible assets, if the case may be, required for the implementation of the CHEAP Tarnița-Lăpuștești project.

2) **Who are the current/ future shareholders of the two project/future project companies? What is their role? Why is Romgaz the only oil & gas company from the consortiums?**

a) Submarine Interconnection cable

The shareholders of the future company shall be: CNTEE Transelectrica S.A., SN Nuclearelectrica S.A. , Societatea Complexul Energetic Oltenia S.A., S.C. Romgaz S.A., Societatea Hidroelectrica S.A., S.C. Electrica S.A. and S.C. Complexul Energetic Hunedoara S.A.

b) Hidro Tarnita project

The shareholders of the initial company are Electrica S.A. and the Complexul Energetic Hunedoara S.A. and the company shall be joined at a later stage by : HIDROELECTRICA S.A., ELECTRICA S.A., NUCLEARELECTRICA S.A., ROMGAZ S.A., COMPLEXUL ENERGETIC OLTENIA S.A. and COMPLEXUL ENERGETIC HUNEDOARA S.A..

Currently Romgaz is not a shareholder of Hidro Tarnita S.A.
Romgaz object of activity also includes power production.

3) **Please confirm whether or not CET Iernut is a non-core asset? Please confirm the validity of the following paragraphs from the IPO Prospectus: (i) "On 31 January 2013, Romgaz took over CTE Iernut thermal power electricity production plant ("CTE Iernut") from Electrocentrale Bucuresti S.A. ("Electrocentrale Bucuresti")...From a total capacity of 800 MW the Company estimates that 160 MW of such capacity will be utilized on average in 2013 (Prospectus English Version page 3); (ii) "...the Government approved in the past the acquisition by the Company of CTE Iernut in order to satisfy an outstanding debt owed to the Company by the owner of CTE Iernut" (English version page 40), (iii) "...CTE Iernut was transferred from Electrocentrale Bucuresti to the Company in exchange for settlement of Electrocentrale Bucuresti's debt owed to the Company in the amount of RON 653 million, owing from its inability to pay the Company for gas supplied to Electrocentrale Bucuresti. The Company recognized this asset in its books as being worth RON3.2 million. In addition, the Company undertook modernization of the plant, having a total value of RON 43.1 million."**

As per Romgaz's articles of incorporation power generation is a non-core activity (in Romanian: obiect de activitate secundar). As such, CET Iernut is a non-core asset.

For clarification purposes of the text included in the Prospectus and quoted in EBRD inquiry, please note that:

- the amount of RON 653 million has been constituted as a provision;
- the amount of RON 3.2 million represents the value of the land related to CET Iernut;
- the amount of RON 43.1 million represents the value of modernization investment made by Romgaz in relation to CET Iernut.

As such the total value of fixed assets of CET Iernut is of RON 46.3 million.

- 4) ***The preliminary feasibility studies for these Projects were done almost a decade ago. Have they been updated, and were they considered by Romgaz in considering proceeding?***

The feasibility study for Hydro Tarnita has been done in 2008.

The feasibility study for the submarine cable project has been done in 2011.

The executive management of Romgaz proposed to the Board, and the Board endorsed a staged approach of Romgaz's participation in the two projects. The project companies should deal with the updates of the studies as their first tasks.

The data and information provided in the current versions of the studies have been partially considered by Romgaz for the purpose of a preliminary analysis having as a main conclusion the necessity for the update of the studies by the project companies (established or to be established).

- 5) ***These Projects have not been pursued previously among other reasons for unacceptably low returns and lack of commercial rationale. How has this changed?***

As mentioned under item 1. above, the Governmental Memorandums have been issued in the last quarter of 2013. As such, Romgaz was not in the position to pursue such projects before the date of the Memorandums.

There was some consideration prior to this date especially with respect to Hydro Tarnita project also triggered by two Government Memorandums dated March 27, 2013 and September 4, 2013, by which it was decided that a project company shall be established having as shareholders Romanian companies in the energy sector.

- 6) ***What prompted the tight deadline in funding the update of the two feasibility studies?***

The tight deadline in funding has been triggered by the need to have the project companies established in and expedient manner, as mentioned in the Government Memorandums (see above).

- 7) ***What is the destination of the EUR 2 Million and RON 8.9 million? We demand a clear accountability for the use of these funds (i.e. number of employees of the two SPVs, the names and the CVs of the management, costs with salaries, rent, utilities, consultants, feasibility studies etc.)***

Romgaz' endorsement included in the Board Decision No. 2/2014 of February 10, 2014 includes the mechanism and conditions under which Romgaz will take part in the increase of share capital/initial share capital of the two project companies. The proposed approach is to have the contributions in stages and in line with the stages of the project and related expenditures of the project companies.

Details on the use of funds are not yet to the knowledge of Romgaz. However, this question shall find an answer as soon as the implementation plan (project performance chart) will be in

place, as requested under the conditions enumerated in the Board Decision mentioned in the above paragraph.

- 8) **Which are the companies that will carry out the new feasibility studies? How were they selected?**

It is our understanding that the new feasibility studies are to be carried out by companies selected by the project companies in accordance with legal provisions for procurement.

- 9) **Which are the companies that carried out the old feasibility studies? How were they selected?**

a) for Hydro-Tarnita: ISPH Bucuresti

b) for the submarine cable project: POYRY SwedPower AB

The owners of the studies are Transelectrica (for the submarine cable) and Hidroelectrica (for Hydro-Tarnita). As such, the selection procedures are not known to Romgaz.

Best regards,

Chairman of the Board

Aurora Negrut

Virgil Metea

Director General

