

## **BOARD OF NOMINEES ANNUAL REPORT FOR 2017**

### **I. THE ROLE OF THE BOARD OF NOMINEES**

#### **INTRODUCTION:**

The Board of Nominees of Fondul Proprietatea SA (the “**Fund**” / “**Fondul Proprietatea**”) is a body created in accordance with the Fund’s Constitutive Act and with Article 224 para. (4) of National Security Commission’s Regulation no. 15/2004, which does not have an equivalent correspondence in the corporate body structure regulated by the Companies’ Law (“*For concluding the administration contract in case of an investment firm which is not self-managed, and also for verifying the unrolling of this contract, the general shareholding can appoint representatives*”).

The Board of Nominees consists of members appointed by the Ordinary General Shareholders’ Meeting (“**OGM**”) for a mandate of three (3) years, which upon expiry is automatically extended until the next OGM.

The members of the Board of Nominees shall be the persons designated by the Fund’s shareholders (and may themselves be shareholders) and shall hold adequate experience and qualifications to decide (if necessary, by assistance of an independent consultant) whether the transactions proposed by the Fund Manager, which require the approval of the Board of Nominees, are carried out for the benefit of the shareholders. The Board has a diligence and loyalty duty to the Fund, acting in the best interests of its shareholders.

The Board of Nominees shall meet at least quarterly. The convening of the meeting shall be made by the chairman of the Board of Nominees (selected by the members thereof), by a member of the Board of Nominees or by the Fund Manager. The meeting of the Board of Nominees shall assemble within 7 (seven) days of convening. The resolutions of the Board of Nominees shall be passed statutorily with a quorum representing the majority of the total members thereof, with the vote of the majority of the voting rights held by the members of the Board of Nominees.

According to the Constitutive Act, the main duties of the Board of Nominees are:

- (1) Following the information received from the Alternative Investment Fund Manager (“**AIFM / Fund Manager**”) with regard to the summoning of the ordinary and/or extraordinary general meeting of the shareholders requests, if it deems necessary, the insertion of supplementary matters in the text of the calling notice of the general meeting of shareholders;
- (2) Receives from the Alternative Investment Fund Manager the information in connection with the answers to the written requests submitted before the date of the general meeting of the shareholders, by the shareholders on topics regarding Fondul Proprietatea’s activity;
- (3) Receives from the Alternative Investment Fund Manager the annual financial statements, the annual activity report presented by the Alternative Investment Fund Manager and the financial auditors’ report, before being made available to the shareholders and analyses them, being able to

formulate an opinion to be presented to both the Alternative Investment Fund Manager and the general meeting;

(4) Receives from the Alternative Investment Fund Manager for analysis the annual report and the management policy of Fondul Proprietatea and presents an opinion to the Alternative Investment Fund Manager and to the general meeting of the shareholders regarding such;

(5) Receives from the Alternative Investment Fund Manager for analysis the yearly income and expenditure budget before it is submitted to the approval of the general meeting of shareholders and presents an opinion to the Alternative Investment Fund Manager and to the general meeting of the shareholders regarding such;

(6) Receives from the Alternative Investment Fund Manager for analysis the strategy in accordance with the Fondul Proprietatea's investment policy before to be submitted to the approval of the general meeting of the shareholders and presents an opinion to the Alternative Investment Fund Manager and to the general meeting of the shareholders;

(7) Receives from the Alternative Investment Fund Manager for analysis and approves the framework for carrying out Fondul Proprietatea's operations, as well as any other Fondul Proprietatea's regulations issued by Alternative Investment Fund Manager according to legal provisions in force, capital market rules and regulations;

(8) Receives from the Alternative Investment Fund Manager for analysis the proposal to the ordinary general meeting of the shareholders for the conclusion of the financial audit agreement and presents an opinion to the Alternative Investment Fund Manager and to the general meeting of the shareholders;

(9) Reviews on a regular basis the investment policy of Fondul Proprietatea and presents an opinion to the Alternative Investment Fund Manager and to the general meeting of the shareholders as any time it deems necessary, but in any case, at least once a year to the annual ordinary meeting;

(10) Receives the report of the internal auditor and presents an opinion to the Alternative Investment Fund Manager and to the general meeting of the shareholders;

(11) Monitors the following, based on information and reports received from the Fund Manager:

- the list of all portfolio investments and percentage breakdown by each investment type;
- a list of major transactions occurring in the Fondul Proprietatea portfolio for the period under review;
- the total profit of the portfolio and comparison of profit with the appropriate market benchmark;
- comparison of the obtained profit with the initial objective;
- the extent of compliance with the investment policy, including, specifically, the degree to which any performance objectives set out therein are achieved, as well as any variations and actions taken to achieve such objectives and improve investment results;
- the performance evaluation report.

The Board of Nominee shall draft and present to the general meeting of the shareholders an annual report regarding the monitoring activity performed or a monitoring report for another period agreed by the general meeting of shareholders;

(12) Represents the general meeting of the shareholders in relation with the Alternative Investment Fund Manager from the communication point of view between the two corporate bodies, except for the cases expressly regulated by this constitutive act as a direct communication between the general meeting and the Alternative Investment Fund Manager;

(13) Verifies the report of the Alternative Investment Fund Manager and the exercise of the permanent monitoring over the management of Fondul Proprietatea by the Alternative Investment Fund Manager, and verifies if the operations carried on by the Alternative Investment Fund Manager are in compliance with the applicable law, the constitutive act and/or with any relevant decision of the general meeting of the shareholders;

(14) Under the conditions of art. 13 paragraphs (11) and (14) calls upon the general meeting of the shareholders;

(15) Participates to the meetings of the general shareholders' meetings and presents in this meeting reports in all cases provided by this constitutive act or with regard to any issue it deems to be relevant for the shareholders;

(16) Proposes to the general meeting of the shareholders the prior approval or rejection of the execution of contracts for acquiring, selling, exchanging or for creating pledges, having as subject non-current assets of Fondul Proprietatea, whose value exceeds, individually or cumulatively during a financial year, 20% of the total value of the non-current assets, less receivables;

(17) Recommends to the General Meeting of the Shareholders the termination of the management agreement for the case when the Board of Nominees is considered is to the benefit of the shareholders.

(18) Recommends to the general meeting of the shareholders on any other issues the Board of Nominees is considered relevant to the shareholders.

(19) Following the proposal of the Alternative Investment Fund Manager, recommends to the Extraordinary General Meeting of the Shareholders the appointment of the public offer intermediary, as well as on its remuneration, when it will become necessary that such a company be appointed related to the admission to trading of Fondul Proprietatea.

(20) Approves the delegation by the Alternative Investment Fund Manager of certain activities. The delegation shall be effective in accordance with the legal provisions in force.

(21) Is responsible for monitoring the Alternative Investment Fund Manager performance of the Investment Management Agreement.

The Constitutive Act also includes regulatory provisions with respect to the conflict of interest and confidentiality responsibilities of the members of the Board of Nominees.

Furthermore, the Board of Nominees will decide, within a reasonable period of time, upon any request submitted by the Fund Manager so as to permit the Fund Manager to perform its obligations.

### ***SHORT PRESENTATION OF THE BOARD OF NOMINEES' ACTIVITY FOR 2017:***

#### **Composition of the Board of Nominees**

The structure of the Board of Nominees as at 31 December 2017 was the following:

<b>Name</b>	<b>Position</b>	<b>Mandate until</b>
Mr Sorin-Mihai Mîndruțescu	Chairman	30 September 2019
Mr Mark Gitenstein	Member	30 September 2019
Mr Julian Rupert Francis Healy	Member	5 April 2018
Mr Steven Cornelis van Groningen	Member	14 April 2018
Mr Piotr Rymaszewski	Member	5 April 2018

During 2017 there were no changes in the structure of Board of Nominees.

#### **Meetings & Relevant Decisions**

In accordance with the provisions of Article 16 of the Constitutive Act of the Fund adopted by the Extraordinary General Shareholders Meeting Decision no. 5 of 29 November 2010 and the provisions of Chapter III of the Regulation for organization and functioning of the Board of Nominees approved by the Board of Nominees' Decision no. 2 of 14 October 2010, as subsequently amended, there were fourteen (14) meetings of the Board of Nominees in 2017, as follows:

- 17 January 2017 - conference call (Members of the Board joining the conference call: Mr. Sorin Mîndruțescu – Chairman, Mr. Julian Healy, Mr. Steven van Groningen, Mr. Piotr Rymaszewski and Mr. Mark Gitenstein);
- 14 February 2017 – meeting (Members of the Board joining the meeting: Mr. Sorin Mîndruțescu – Chairman, Mr. Julian Healy, Mr. Steven van Groningen and Mr. Mark Gitenstein);
- 3 March 2017 – meeting (Members of the Board joining the meeting: Mr. Sorin Mîndruțescu – Chairman, Mr. Julian Healy, Mr. Steven van Groningen, Mr. Piotr Rymaszewski and Mr. Mark Gitenstein)
- 22 March 2017 – conference call (Members of the Board joining the conference call: Mr. Julian Healy – Chairman; Mr. Steven van Groningen, Mr. Piotr Rymaszewski);
- 24 April 2017 – meeting (Members of the Board joining the meeting: Mr Sorin Mîndruțescu – Chairman, Mr Julian Healy, Mr Steven van Groningen, Mr Piotr Rymaszewski and Mr Mark Gitenstein);
- 11 May 2017 – conference call (Members of the Board joining the conference call: Mr. Sorin Mîndruțescu – Chairman, Mr. Julian Healy and Mr. Mark Gitenstein);
- 31 May 2017 – conference call (Members of the Board joining the conference call: Mr. Sorin Mîndruțescu – Chairman, Mr. Julian Healy, Mr. Steven van Groningen, Mr. Piotr Rymaszewski and Mr. Mark Gitenstein);
- 27 June 2017 – meeting (Members of the Board joining the meeting: Mr. Sorin Mîndruțescu – Chairman, Mr. Julian Healy, Mr. Steven van Groningen, Mr. Piotr Rymaszewski and Mr. Mark Gitenstein);

- 11 August 2017 – conference call (Members of the Board joining the conference call: Mr. Sorin Mîndruțescu – Chairman, Mr Julian Healy, Mr Piotr Rymaszewski and Mr Mark Gitenstein);
- 5 September 2017 – meeting (Members of the Board joining the meeting: Mr. Sorin Mîndruțescu – Chairman, Mr. Julian Healy, Mr. Steven van Groningen, Mr. Piotr Rymaszewski and Mr. Mark Gitenstein)
- 26 September 2017 – meeting (Members of the Board joining the meeting: Mr. Sorin Mîndruțescu – Chairman, Mr. Julian Healy, Mr. Piotr Rymaszewski and Mr. Mark Gitenstein);
- 26 October 2017 – meeting (Members of the Board joining the meeting: Mr. Sorin Mîndruțescu – Chairman, Mr. Julian Healy, Mr. Steven van Groningen, Mr. Piotr Rymaszewski and Mr. Mark Gitenstein);
- 14 November 2017 – conference call (Members of the Board joining the conference call: Mr Sorin Mîndruțescu – Chairman, Mr. Julian Healy and Mr. Mark Gitenstein);
- 15 December 2017 – meeting (Members of the Board joining the meeting: Mr Julian Healy - Chairman, Mr. Steven van Groningen, Mr. Piotr Rymaszewski and Mr. Mark Gitenstein).

During 2017, the Board of Nominees issued a total number of sixty-six (66) resolutions. Among such, the most important ones referred to:

- ✓ The approval of amending the Internal Regulations of the Board of Nominees of Fondul Proprietatea SA;
- ✓ The approval of amending the Expense Reimbursement Internal Policy of Fondul Proprietatea SA;
- ✓ The approval of the Anti-Bribery and Corruption Code of Conduct for the Board of Nominees of Fondul Proprietatea SA;
- ✓ The approval of the costs related to signing different arrangements for rendering various services to the Fund, including extension of loan agreement, independent financial advisory and investment banking services, new provider for the redesign of the Fund’s website etc.;
- ✓ The approval of the waiver for the selection of different providers with respect to the activity performed by Fondul Proprietatea SA;
- ✓ The approval of the convening notices in relation to the General Shareholders Meetings held during 2017 and beginning of 2018;
- ✓ The approval of updating the procedure for organising the Fund’s general shareholders’ meetings;
- ✓ The prior approval of the decrease of the subscribed share capital of the Fund (either through the reduction of the par value of the Fund’s shares involving cash distributions to the Fund’s shareholders or pursuant to the cancellation of own shares acquired by the Fund within the buyback programmes);
- ✓ The prior approval of the buyback programmes of the own shares issued by the Fund;
- ✓ The prior approval of the Fund’s Sole Director Annual Report for 2016;
- ✓ The prior approval of the net profit allocation registered for the financial year 2016;
- ✓ The prior approval of the renewal of the mandate of Franklin Templeton International Services S.à r.l., as the alternative investment fund manager and sole director of Fondul Proprietatea S.A. for another two (2) years term starting with 1 April 2018 (“New Mandate”)
- ✓ The prior approval of the key commercial terms of the New Mandate of FTIS, as the alternative investment fund manager and sole director of Fondul Proprietatea S.A. for another two (2) years term starting with 1 April 2018;

- ✓ The prior approval of the terms along with the execution before 1 March 2018 of the new Management Agreement by and between Fondul Proprietatea S.A. and Franklin Templeton International Services S.À R.L. covering the New Mandate (as defined by OGM Resolution no. 3 of 26 September 2017);
- ✓ The prior approval with respect the continuation of the current mandate of FTIS as the Fund's Alternative Investment Fund Manager and Sole Director, as per the provisions of the Management Agreement in force;
- ✓ The prior approval of the new Investment Policy Statement of Fondul Proprietatea;
- ✓ The prior approval of Fondul Proprietatea's 2018 budget;
- ✓ The prior approval of appointing Deloitte Audit SRL as the financial auditor of the Fund for 2017-2019 and of the costs related to signing the audit contract;
- ✓ The approval of reimbursement of the expenses incurred by Franklin Templeton Investment Management Ltd. United Kingdom Bucharest Branch on behalf of Fondul Proprietatea.

## **II. THE OPINION OF THE BOARD OF NOMINEES REGARDING ANNUAL REPORT FOR THE YEAR END 31 DECEMBER 2017:**

### ***ANNUAL ACTIVITY REPORT PRESENTED BY THE FUND MANAGER***

This section provides an overview on the main elements of the Fund's financial position and performance for the period ended 31 December 2017.

#### **Statement of Financial Position**

<b>RON million</b>	<b>31 December 2017 Audited</b>	<b>31 December 2016 Audited</b>
Cash and current accounts	19.2	5.8
Deposits with banks	1,276.7	305.3
Treasury bills	46.3	781.4
Government bonds	195.9	328.6
Equity investments	9,278.2	9,992.2
Other assets	10.7	20.8
<b>Total assets</b>	<b>10,827.0</b>	<b>11,434.1</b>
Payables	15.2	27.1
Other liabilities	21.6	21.0
<b>Total liabilities</b>	<b>36.8</b>	<b>48.1</b>
Total equity	10,790.2	11,386.0
<b>Total liabilities and equity</b>	<b>10,827.0</b>	<b>11,434.1</b>

The short term assets of the Fund included term **deposits with banks**, **government bonds** and **treasury bills** issued by the Ministry of Public Finance of Romania. All instruments are denominated in RON and have maturities of up to one year.

The overall increase in liquidity assets in 2017 is mainly due to the cash inflows from the disposal of portfolio companies (mainly in the subsidiaries of Electrica and part of OMV Petrom SA) in amount of RON 1,231.3 million and the dividends collected from portfolio companies during the period in amount of RON 737.6 million, net of tax. These were netted off mainly by the cash outflows in respect of the return of capital to shareholders (RON 910.5 million) and for funding the own shares acquired within the seven, eight and nine buy-back programmes (RON 819.2 million).

The net decrease of **equity investments** of RON 714.0 million for the year ended 31 December 2017 is mainly due to the disposal of certain portfolio companies (total impact RON 1,247.3 million), which was offset by the net increase of RON 172.5 million in the value of unlisted equity investment following the **updated** valuations as at 31 December 2017 and by the increase in value of equity investments, mainly OMV Petrom SA (increase in share price of 9.6%).

### Statement of Comprehensive Income

RON million	2017 Audited	2016 Audited
Gross dividend income	740.4	353.1
Net realised gain / (loss) from disposal of non-current assets held for sale	330.6	(127.5)
Net unrealised gain/ (loss) from equity investments at fair value through profit or loss	222.8	(377.8)
Net gain on disposal of equity investments classified as available for sale	38.5	926.0
Reversal of impairment losses on receivables, net	36.4	17.9
Interest income	11.9	7.9
Net realised gain from equity investments at fair value through profit or loss	(1.4)	-
Impairment losses on equity investments classified as available for sale	(8.0)	(122.4)
Other income/ (expenses), net*	0.9	(0.5)
<b>Net operating income/ (loss)</b>	<b>1,372.1</b>	<b>676.7</b>
Administration fees recognized in profit and loss	(63.0)	(70.6)
Other operating expenses	(34.5)	(61.5)
<b>Operating expenses</b>	<b>(97.5)</b>	<b>(132.1)</b>
Finance costs	(0.2)	(0.3)
<b>Profit/ (Loss) before income tax</b>	<b>1,274.4</b>	<b>544.3</b>
Income tax expense	15.5	(97.3)
<b>Profit/ (Loss) for the year</b>	<b>1,289.9</b>	<b>447.0</b>
Other comprehensive income	(85.4)	100.7
<b>Total comprehensive income for the year</b>	<b>1,204.5</b>	<b>547.7</b>

\* Other items of income/ (expense), net included mainly the net loss from revaluation of government securities through profit or loss, net foreign exchange gain / (loss) and other operating income/ (expenses).

**Gross dividend income** for the year ended 31 December 2017 comprised the dividend income earned from the Fund's portfolio companies, mainly from Hidroelectrica SA (RON 206.6 million), OMV Petrom SA (RON 106.8 million), CN Aeroporturi Bucuresti SA (RON 43.0 million), Electrica Furnizare SA (RON 34.8 million), Electrica Distributie Transilvania Nord SA (RON 22.1 million),

Electrica Distributie Muntenia Nord SA (RON 19.3 million) and Electrica Distributie Transilvania Sud SA (RON 21.7 million).

The increase of gross dividend income compared with 2016 relates to the special dividends distributed in September – December 2017 by state controlled entities, namely Hidroelectrica SA and CN Aeroporturi Bucuresti SA, in amount of RON 130.6 million, and RON 40 million respectively.

**The net realised gain from disposal of non-current assets held for sale** for the year end 31 December 2017 is represented by:

- The net gain on disposal of Electrica subsidiaries in amount of RON 345.1 million, representing the difference between the proceeds from disposals (RON 752.0 million) and the carrying values of the equity investments as at disposal date (RON 752.0 million), plus the net unrealised gain related to the investments disposed, recycled from other comprehensive income to profit or loss upon their derecognition (RON 345.1 million)
- the difference between the total proceeds from the disposal of the partial sale of OMV Petrom SA holding (RON 399.9 million) and the fair value at the reclassification date of the non-current assets held for sale disposed of (RON 414.4 million).

The **net unrealised gain from equity investments at fair value through profit or loss** for 2017 of RON 222.8 million was mainly generated by OMV Petrom SA, as a result of the positive evolution of the share price for this company during the year end 31 December 2017 (RON 176.5 million, share price increase of 9.6%).

The **net gain on disposal of equity investments classified as available for sale** represents the difference between the proceeds from disposals and the carrying amount of the equity investments as at disposal date, plus the net unrealised gain related to these investments transferred from other comprehensive income to profit or loss upon their derecognition.

During 2017, the Fund sold its entire holdings in Oil Terminal SA, Banca Transilvania SA and Cetatea SA and part of its holding in BRD Groupe Societe Generale SA. The **net gain on disposal of these equity investments classified as available for sale** was RON 38.5 million, representing the difference between the gross proceeds from disposals (RON 74.9 million) and the carrying values of the equity investments as at disposal date (RON 74.4 million), plus the net unrealised gain related to these investments disposed, recycled from equity (other comprehensive income) to profit or loss upon their derecognition (RON 38.0 million).

The **reversal of impairment losses** for 2017 relates mainly to the receivable for the unpaid share capital amounts from the Romanian State represented by the Ministry of Public Finance. Following the reduction of the nominal value of the Fund's shares from RON 0.85 to RON 0.57 (registered on 24 March 2017) and from RON 0.57 to RON 0.52 (registered on 16 June 2017), the receivable for the unpaid amounts and the related impairment adjustment decreased accordingly, generating a positive impact in the profit or loss account of RON 36.4 million.

In performing the impairment test for the available for sale equity investments, the Fund considers all relevant factors, such as: significant or prolonged decline in fair value below cost, market and industry conditions, to the extent that they influence the recoverable amount of the equity investment, financial conditions and near-term prospects of the issuer, any specific adverse events that may influence the issuer's operations and recent losses of the issuer. **Impairment losses on equity investments classified as available for sale** caption for year ended 31 December 2017 relates to the holding in Posta Romana (RON 8.0 million).

The total **administration fees** expenses in 2017 included the base fee of RON 46.8 million (in 2016: RON 46.8 million) and the distribution fee for return of capital of RON 16.2 million (in 2016: RON



23.8 million out of which RON 13.5 million represented distribution fee related to the buy-backs). Starting 2017, the distribution fee related to buy-backs is recognised directly in equity together with the underlying shares (RON 15.1 million). This change was not applied retrospectively as the effect on the comparative amounts is not significant. The higher distribution fee in 2017 compared to 2016 was due to the fees invoiced for the higher distributions made available to the Fund's shareholders in 2017, respectively for the special return of capital performed in March 2017 of RON 0.05 per share for which the payment started on 27 March 2017.

The **other comprehensive income** mainly comprised the changes in fair value of equity investments classified as available for sale, net of related deferred tax, where applicable. As at 31 December 2017, the change in fair value of these equity investments is of RON 315.8 million and the decrease in the fair value reserve due to the disposal of the equity investments available for sale during the year, is of RON 383.1 million, mainly generated following the disposal of Electrica subsidiaries.

**The Board of Nominees has reviewed the financial information and related statements set out above and is satisfied that they correctly reflect in all material aspects the activity of the Fund during 2017.**

### ***FINANCIAL REPORT OF AUDITORS***

The Board of Nominees has reviewed Deloitte's audit report, which is presented together with the statutory financial statements. The Board has had the opportunity to discuss the report in detail with Deloitte.

The audit opinion has an extended new form, following the requirements of the new audit standards adopted and it contains an unqualified audit opinion on the Fund's annual financial statements as at 31 December 2017.

The key audit matters included in the audit report are: Valuation of equity investments.

### **Profit appropriation proposal**

As per the statutory financial statements prepared in accordance with the IFRS, the Fund recorded a net profit for the financial year ended 31 December 2017 of RON 1,289,896,039. In accordance with the Companies law, the Fund is obliged to make transfers to the legal reserves until those reserves reach a value equivalent to 20% of the value of the issued share capital of Fondul Proprietatea. Following the 2017 transfer of RON 64,494,802, the value of those reserves is RON 330,578,801 (representing 7.09% of the issued share capital as at 31 December 2017).

The Fund's Sole Director proposal, subject for GSM approval in accordance with the legislation in force, for the appropriation of the net accounting profit for the 2017 financial year in an amount of RON 1,289,896,039 is as follows:

- RON 64,494,802 to legal reserve
- RON 591,087,324 to dividends;
- RON 634,313,913 remains available to the Fund's shareholders under retained earnings.

### Coverage of the Negative Reserve balance incurred during 2017 Financial Year

The Fund recognises the treasury shares (repurchases of own shares and/ or GDRs) at trade date as a deduction to shareholders' equity (in an equity reserve account). Treasury shares are recorded at acquisition cost, including brokerage fees and other transaction costs directly related to their acquisition. Upon completion of all legal and regulatory requirements, the treasury shares are cancelled and netted off against the share capital and other reserves.

At the cancellation date, only a reallocation between the equity accounts is booked, without any impact on profit or loss or an additional total shareholders' equity decrease (as compared to the acquisition impact). A negative reserve (equity element) arises upon cancellation of the shares acquired in a buy-back programme, if the acquisition value (trade price and related costs) is higher than the nominal value.

During 2017, the nominal value decreased below the acquisition price starting on 24 March 2017 when the share capital decrease according to 31 October 2016 GSM was registered at Trade Registry. All subsequent acquisitions in the buy-back programmes (respectively 7th, 8th and 9th buyback programmes) were made at an acquisition price higher than the nominal value.

The table below shows the negative reserve arising on the cancellation of treasury shares from 29 November 2017:

		<b>Buy-back program 7</b>
Number of shares cancelled during 2017	(1)	739,398,468
Total acquisition costs (including brokerage fees and other transaction costs) (RON)	(2)	682,500,639
Less the impact of the Fund's share Nominal Value decrease during 2017 (RON) <sup>1</sup>	(3)	(41,939,847)
Accounting value of the cancelled treasury shares as at 29 Nov 2017 (the cancellation date) (RON)	(4) = (2)+(3)	640,560,792
Correspondent Nominal Value at the cancellation date (NV = RON 0.52/ share) (RON)	(5) = (1)*NV	384,487,203
<b>Negative equity reserve arising on the partial cancellation of shares acquired during the 7<sup>th</sup> buy-back (RON)</b>	<b>(6) = (5)-(4)</b>	<b>(256,073,589)</b>

<sup>1</sup> For shares cancelled and in balance at the date of Fund's share nominal value decrease in 2017: 1) 99,398,468 shares at 24 March 2017 and 2) 739,398,468 shares at 16 June 2017

Article 75 from Norm 39/2015 mentions that the negative balance arising on out of the cancellation of equity instruments may be covered from the retained earnings and other equity elements, in accordance with the resolution of the General Shareholders Meeting.

### 2017 BUDGET COMPARED TO ACTUAL RESULTS

The Board of Nominees asked the Fund Manager to analyse the significant variances in the main categories of income and expenses of Fondul Proprietatea S.A. by comparing the budget for the year ended 31 December 2017 (approved by shareholders on 31 October 2016) to the audited actual results for the same period.

The result of this analysis has been reviewed by the Board of Nominees, which is satisfied with the explanations given for any significant variances.

Together with the approval of 2017 Budget in October 2016, the shareholders granted the Fund Manager the power to:

- exceed the expenses budgeted for administration fees;
- exceed the expenses budgeted for commissions and fees (FSA fees and Depository bank fees), to the extent arising from the Fund's actual average NAV, the value of assets under custody and/ or volume of portfolio and buy-backs trades in 2017 being higher than the ones assumed in the 2017 Budget;
- incur on behalf of the Fund all expenses necessary (e.g. intermediary fees of brokers or investment banks, market authorities' fees, lawyers, public notaries, other advisors costs, as well as other related expenses, commissions or fees) related to the execution of acquisitions and disposals of equity investments or participation in share capital increases of portfolio companies;
- incur on behalf of the Fund all expenses related to the buy-back of the Fund's shares or the equivalent global depository receipts corresponding to shares of the Fund and their subsequent cancellation (after the approval by shareholders), under any buy-back programme approved by shareholders;
- incur on behalf of the Fund any expenses related to bank loans/ credit facilities contracted by the Fund, with Board of Nominees approval;
- incur on behalf of the Fund any expenses related to the potential change of the fund manager and sole administrator of the Fund (expense incurred by the Board of Nominees);
- incur on behalf of the Fund any expenses resulting from the implementation of any regulation applicable to the Fund.

even if this will result in exceeding the total expenses approved in the 2017 Budget.

A detailed breakdown of the figures has been included in **Annex 1**. As certain categories of income and expenses cannot be budgeted (such as foreign exchange gains and losses, revenues and expenses from impairment adjustments, fair value changes, gains or losses and other expenses related to disposal of financial instruments, or other items of income/ expense), the income and expenses have been split into "budgeted" and "non-budgeted" categories.

## **Results**

### ***Net result***

The *actual net profit* of the Fund for the year end 31 December 2017 was RON 1,289.9 million, 469% higher as compared to the budgeted profit of RON 226.7 million. The main contribution to the profit recorded in 2017 was the gross dividend income, which increased compared to the budget due to OMV Petrom SA decision to distribute dividends in 2017 (RON 106.8 million) and due to higher dividends distributed by Hidroelectrica SA (RON 206.6 million) as well as due to the special dividends in amount of RON 186.1 million distributed by state controlled entities starting with September 2017 (mainly from Hidroelectrica SA and CN Aeroporturi Bucuresti SA).

A significant contribution to the profit recorded during 2017 were also the positive net change in the fair value related to equity investments classified at fair value through profit or loss, mainly OMV Petrom SA, as a result of the positive evolution of the share price of this company during the period (increase of 9.6%) and the net gain on disposal of Electrica SA subsidiaries.

***Income from current activity***

The actual gross dividend for 2017 in amount of RON 740.4 million is 122% higher than budgeted amounts. The budgeted amounts were prepared based on discussions and specific assumptions during August 2016 while the actual amounts are impacted by the Romanian State one-off decisions made during 2017: a 90% dividend pay-out ratio and special dividends distributions.

The table below presents details of the main differences, by portfolio company:

<b>Portfolio company</b>	<b>Actual net dividend</b>	<b>Budgeted net dividend</b>	<b>Variance</b>	<b>Reason for variance</b>
Hydroelectrica SA	337,188,756	134,644,266	202,544,491	Increase of dividends in 2017 due to the increase of 2016 profit, due to the Government decision to pay out a minimum of 90% of the 2016 profits and due to the special dividends approved by the company (RON 130.6 million).
OMV Petrom SA	106,763,221	-	106,763,221	The 2017 budgeted figures were estimated to be nil due to the fact that that the company incurred a loss in 2015. The actual figures in 2017 were impacted by the 2016 profit and by the company dividend policy to distribute a minimum of 30% of its 2017 profit.
CN Aeroporturi Bucuresti SA	82,955,766	27,413,948	55,541,818	Increase of dividends in 2017 due to the increase of 2016 profit, due to the Government decision to pay out a minimum of 90% of the 2016 profits and to pay special dividends (RON 40.0 million).
<b>TOTAL</b>	<b>526,907,743</b>	<b>162,058,214</b>	<b>364,849,530</b>	

In addition, the Fund's actual results include an amount of RON 619.8 million of *non-budgeted income*, related to:

- *Net gain on disposal of equity instruments* in amount of RON 367.7 million, generated mainly by the sale of the entire holdings in the subsidiaries of Societatea Energetică Electrica SA ("Electrica");
- the *net unrealised gain from financial instruments at fair value through profit or loss* in amount of RON 215.8 million mainly generated by OMV Petrom SA, as a result of the positive evolution of the share price for this company during 2017 (RON 176.5 million, share price increase of 9.6%).

During the year the Fund also sold its entire holding in Oil Terminal SA, Primcom SA, Banca Transilvania SA and part of its holdings in BRD Societe Generale and OMV Petrom.

Interest income arose from deposits with banks and from short-term government securities held until the end of the year and amounted to RON 11.9 million, while the budget included a nil assumption.

The net reversal of impairment adjustments and provisions, in amount of RON 28.4 million represents net impairment release related to the receivable for unpaid shares of the Romanian State, following

the reduction of the nominal value of the Fund's shares on 24 March 2017 and on 16 June 2017, net of the impairment loss booked in December 2017 for the Fund's holding in Posta Romana SA.

*Other non-budgeted income* category mainly includes the amounts reimbursed by The Bank of New York Mellon from the fees collected from GDR holders in amount of RON 7.3 million.

***Expenses from current activity***

During 2017, the *actual expenses from current activity* of RON 97.6 million are lower than the budgeted expenses of RON 106.9 million.

*The other non-budgeted expenses* in amount of RON 8.6 million, include expenses related to the disposal of portfolio holdings, mainly fees related to OMV Petrom sale during 2017 (e.g. brokerage and Bucharest Stock Exchange fees).

If we exclude the *non-budgeted expenses*, the *actual expenses from current activity* are lower than the budget by RON 17.9 million (17%).

The actual *third party service providers' expenses* during the period are lower by RON 14.8 million compared to the budgeted figure. A detailed breakdown of this category is shown in **Annex 1**.

The main component of this category relates to the *administration fees* starting with 2017, the *distribution fee related to buy-back programmes* is recognised directly in other comprehensive income (equity) together with the underlying shares.

The total administration fees for the period are presented below:

	<b>Budgeted</b>	<b>Actual</b>	<b>Comments</b>
<b>Recognised in Profit and Loss</b>	<b>68,155,575</b>	<b>63,049,843</b>	
Base fee	41,005,356	46,780,186	The base fee was higher during 2017 due to a higher Fund's average price compared to the one used in the budget assumptions.
Distribution fee for buy-back programmes	10,827,000		
Distribution fee Return of capital	16,323,219	16,269,657	
<b>Recognised in Other comprehensive income</b>	<b>-</b>	<b>15,062,391</b>	
Distribution fee for buy-back programmes	-	15,067,165	The higher distribution fee was due to the higher distributions made available to the Fund's shareholders (mainly determined by the Tender offer from March 2017).
<b>TOTAL administration fees</b>	<b>68,155,575.00</b>	<b>78,117,008</b>	

*Income tax* in amount of RON 15.5 million represents the deferred tax asset related to fiscal loss carried forward and recognised in profit and loss to offset the increase of the deferred tax liability generated by the available for sales equity investments and recorded to other comprehensive income (equity).

The average actual Fund's NAV during year ended 31 December 2017 was lower than the average NAV used in the 2017 Budget assumptions, and had a positive influence mainly on *Commissions and fees expenses (include FSA fees)* and *Bank fees and distribution to shareholders fees (including Depositary fees)*.

The *other third party service providers' expenses* include mainly portfolio holding valuation, costs related to the FSA's regulatory requirements and portfolio related expenses (market studies, due diligence).

### **III. PORTFOLIO INVESTMENT OF THE FUND:**

#### ***BOARD OF NOMINEES OPINION REGARDING THE INVESTMENT POLICY OF THE FUND AND THE DEGREE OF COMPLIANCE WITH THE INVESTMENT POLICY AND ANY CHANGES AND ACTIONS THAT LEAD TO TARGETTED RESULTS***

The investment objective of the Fund is the maximization of returns and per-share capital appreciation via investments mainly in Romanian equities and equity-linked securities. Details of the investment policy can be found in the Investment Policy Statement and Constitutive Act.

**The Board of Nominees believes that the Fund Manager was in compliance during 2017 with the applicable investment policy adopted by the Fund.**

#### ***BOARD OF NOMINEES OPINION REGARDING THE PORTFOLIO INVESTMENT AND THE PERCENTAGE ACCOMPANYING EACH TYPE OF INVESTMENT AT THE END OF 2017***

The Board of Nominees holds frequent and detailed discussions on managing the Fund to maximize shareholder value. This includes developing a consistent approach for appropriate actions aimed at reducing the discount at which the Fund's shares are traded on the Bucharest Stock Exchange. In particular, the Board is supportive of the implementation of various Discount Control Mechanism techniques including buyback programmes, tender offers, the return of capital and dividends to shareholders, because the Fund's shares are trading at a deep discount. The Board also discusses at its meetings with the Fund Manager the potential strategies for unlocking the value of the individual unlisted investments. The Board has an Audit and Valuation Committee, part of the role of which is to consider on a regular basis the appropriate valuation methodology for valuing the individual unlisted investments.

#### ***BOARD OF NOMINEES OPINION REGARDING THE SIGNIFICANT TRANSACTIONS OF THE FUND FOR 2017***

The Board of nominees considers that the most significant portfolio transactions during 2017 were consistent with maximizing returns for the Fund's shareholders. The most significant transactions of the Fund within the investment portfolio during 2017 were:

- In September the Fund sold 1,454,000,000 shares in OMV Petrom SA through an accelerated book building offer at an agreed selling price of RON 0.2750 / share, the gross proceeds of the transaction amounting to RON 399,850,000;
- In November the Fund sold its entire holdings in the subsidiaries of Societatea Energetică Electrica SA ("Electrica") in amount to RON 752,031,841 and its details are described below:
  - Electrica Furnizare SA was sold to Electrica and Societatea Filiala de Întreținere și Servicii Energetice Electrica Serv SA for an aggregated selling price of RON 167,079,881;

- Societatea de Distribuție a Energiei Electrice Transilvania Nord SA was sold to Electrica and Societatea de Distribuție a Energiei Electrice Muntenia Nord SA for an aggregated selling price of RON 201,702,667;
- SDDEE Muntenia Nord SA was sold to Electrica and Societatea de Distribuție a Energiei Electrice Transilvania Sud SA for an aggregated selling price of RON 209,744,928;
- SDEE Transilvania Sud SA was sold to Electrica and SDEE Transilvania Nord S.A. for an aggregated selling price of RON 173,504,365.

During November 2017, the Fund also collected the outstanding balance of the dividends in amount of RON 97.9 million distributed by the Electrica subsidiaries.

- During the year the Fund also sold its entire holdings in Oil Terminal SA, Primcom SA, Cetatea SA, Banca Transilvania SA and part of its holdings in BRD Societe Generale.

#### ***BOARD OF NOMINEES OPINION REGARDING KEY PORTFOLIO VALUATIONS DURING THE PERIOD***

At year end, valuation updates were prepared for 16 unlisted holdings, representing 99.7% of the total unlisted portfolio, with the assistance of KPMG Advisory. The valuation reports were prepared in accordance with the International Valuation Standards and the biggest increase compared to 31 December 2016 occurred for Hidroelectrica (RON 182.0 million). The full list of valuation reports impact for 2017 is included in Annex 2.

In terms of listed holdings, the most significant impact relates to OMV Petrom's share price, which had a positive evolution during the year with an increase of 9.6% (net positive impact during the period of RON 176.5 million).

At the end of 2017 the Fund assessed whether there is objective evidence of impairment for both listed and unlisted holdings. In performing the impairment test for the available for sale equity investments, the Fund considers all relevant factors, such as: significant or prolonged decline in fair value below cost, market and industry conditions, to the extent that they influence the recoverable amount of the equity investment, financial conditions and near-term prospects of the issuer, any specific adverse events that may influence the issuer's operations and recent losses of the issuer.

The only impairment losses booked by the Fund for year ended 31 December 2017 relates to the holding in Posta Romana (RON 8.0 million).

#### **IV. BOARD OF NOMINEES OPINION REGARDING THE ANNUAL REPORT OF THE INTERNAL AUDITORS AND THE ANNUAL COMPLIANCE REPORT**

The Board of Nominees has reviewed the internal audit report prepared by Fondul Proprietatea's internal auditor, BDO and been informed about the internal audit performed by FTI, for the year 2017.

The overall objective of the report of the internal auditors was to assess whether the key risks relating to Fondul Proprietatea's operations are being managed in an appropriate manner and in compliance with applicable regulatory requirements and FTI policies and procedures.

The report has not identified any major deficiencies regarding the design and effectiveness of controls which were subject to the internal audit work.

The Board of Nominees received and reviewed the Annual Compliance Report prepared by the local compliance officer, addressing the management of the compliance risk within the company / fund. The compliance report covered the activities performed by Franklin Templeton Investment Management Limited UK Bucharest Branch and Fondul Proprietatea S.A. in respect of compliance with applicable local rules and regulations and internal procedures.

No material compliance exceptions have been reported in 2017.

**In the opinion of the Board of Nominees, both the Annual Report of the Internal Auditors and the Annual Compliance Report have been prepared to an adequate standard.**

## **V. THE GENERAL EVALUATION OF THE ACTIVITY OF THE FUND MANAGER FOR 2017**

The most notable activities during 2017 included:

- Completion of the fourth tender offer of 640 million shares (370.7 million in the form of shares and 269.3 million in the form of GDRs), at a purchase price of RON 0.91 per share and the USD equivalent of RON 45.50 per GDR, executed in order to accelerate the seventh buy-back programme;
- Gross special distribution of RON 480.5 million to shareholders through the reduction of the nominal value of the Fund's shares from RON 0.62 per share to RON 0.57 per share;
- Completion of the seventh buy-back programme for 830.2 million shares. The total value of the programme excluding transaction costs was RON 744.5 million, and the average share price was RON 0.8967 per share;
- Gross distribution of RON 443.5 million to shareholders through the reduction of the nominal value of the Fund's shares from RON 0.57 per share to RON 0.52 per share;
- Successful placement of 1.454 million shares held in OMV Petrom SA (2.6% of the total shares issued by the company and 20.4% of the Fund's holding in the company), via an accelerated bookbuilding process on the BVB;
- Disposal of the entire holdings in the Electrica subsidiaries for a total value of the transaction of RON 752.0 million. The Fund also collected the outstanding balance of dividends in amount of RON 97.9 million distributed by Electrica subsidiaries;
- Completion of the eight buy-back programme for 141.9 million shares. The total value of the programme excluding transaction costs was RON 122.3 million, and the average share price was RON 0.8624 per share;
- Start of the ninth buy-back programme for a maximum number of shares and/or equivalent GDRs corresponding to the Fund's shares computed so that inclusive of all the outstanding treasury shares (acquired during this programme and/or previous ones) will not exceed 20% of



the issued share capital at the relevant time, which represents a total of 1,866.9 own shares as of 31 December 2017;

- Continued efforts to promote the Fund and raise its visibility, as well as the visibility of the Romanian capital market, the local companies (listed or candidates for being listed), and of Romania in general, in the key financial centers in the United States of America, Europe, and the Middle East;
- Record high participation from foreign institutional investors and analysts at the Romania Investor Days in London, and Fondul Proprietatea Analyst and Investor Days in Bucharest;
- Key shareholders' approvals during 2017:
  - The return of capital of RON 0.05 per share to shareholders, as proposed by the Sole Director;
  - The approval of a new mandate of FTIS as Alternative Investment fund manager and Sole Director of Fondul Proprietatea, starting 1 April 2018 and its key commercial terms;
  - Approval of the ninth buy-back programme to repurchase a maximum number of 20% of the issued share capital at the relevant time.

## **VI. RECOMMENDATIONS FOR SHAREHOLDERS:**

In view of the proposed points of the agenda of the annual GSM, the Board of Nominees would like to recommend to shareholders that they approve all the proposals of the Fund Manager submitted to this meeting.

Please note that this report is the annual report of the board of Nominees prepared on the basis of Article 17 of the Constitutive Act of Fondul Proprietatea SA.

**Mr. Sorin-Mihai MÎNDRUȚESCU, Chairman**

**Mr. Steven Cornelis van GRONINGEN, Member**

**Mr. Piotr RYMASZEWSKI, Member**

**Mr. Julian Rupert Francis HEALY, Member**

**Mr. Mark Henry GITENSTEIN, Member**

**Annex 1**  
**2017 Budget versus Actual Results**

	Budget 2017	Actual 2017	Variance	
	RON	RON	RON	%
<b>I INCOME FROM CURRENT ACTIVITY</b>	<b>333,600,492</b>	<b>1,372,052,057</b>	<b>1,038,451,565</b>	<b>311%</b>
<b>Budgeted income</b>	<b>333,600,492</b>	<b>752,280,482</b>	<b>418,679,990</b>	<b>126%</b>
Gross dividend income	333,600,492	740,360,617	406,760,125	122%
Interest income	-	11,919,865	11,919,865	100%
<b>Non-budgeted income</b>	<b>-</b>	<b>619,771,575</b>	<b>619,771,575</b>	<b>n/a</b>
Net gain on disposal of equity instruments	-	367,693,958	367,693,958	n/a
Net unrealised gain from financial instruments at fair value through profit or loss	-	215,831,742	215,831,742	n/a
Reversal of impairment adjustments and provisions, net	-	28,378,838	28,378,838	n/a
Net foreign exchange gains	-	570,507	570,507	n/a
Other income	-	7,296,530	7,296,530	n/a
<b>II EXPENSES FROM CURRENT ACTIVITY</b>	<b>106,903,852</b>	<b>97,645,041</b>	<b>(9,258,811)</b>	<b>-9%</b>
<b>Budgeted expenses</b>	<b>106,903,852</b>	<b>89,020,434</b>	<b>(17,883,418)</b>	<b>-17%</b>
Third party service providers' expenses	87,692,763	72,868,226	(14,824,537)	-17%
Commissions and fees expenses (include FSA fees)	11,036,492	10,496,761	(539,731)	-5%
Investors relations expense	2,237,168	1,410,074	(827,094)	-37%
Other expenses	1,420,712	488,773	(931,939)	-66%
Board of Nominees & special administrators remunerations	1,200,000	1,200,000	-	0%
PR expenses	1,027,164	920,648	(106,516)	-10%
Bank fees and distribution to shareholders fees (including Depository fees)	955,505	786,394	(169,111)	-18%
Amortisation expenses	644,660	288,180	(356,480)	-55%
Insurance expenses	334,905	221,640	(113,265)	-34%
Social security contributions	252,000	245,075	(6,925)	-3%
Rent expenses	78,113	70,265	(7,848)	-10%
Expenses with utilities	24,370	24,398	28	0%
<b>Non-budgeted expenses</b>	<b>-</b>	<b>8,624,607</b>	<b>8,624,607</b>	<b>n/a</b>
Finance costs	-	152,997	152,997	n/a
Other expenses	-	8,471,610	8,471,610	n/a
<b>III GROSS PROFIT/ (LOSS)</b>	<b>226,696,640</b>	<b>1,274,407,016</b>	<b>1,047,710,376</b>	<b>462%</b>
IV.Income tax	-	15,489,023	15,489,023	n/a
<b>V. NET PROFIT/ (LOSS)</b>	<b>226,696,640</b>	<b>1,289,896,039</b>	<b>1,063,199,399</b>	<b>469%</b>
<b>VI CAPITAL EXPENDITURE</b>	<b>493,196</b>	<b>495,977</b>	<b>2,781</b>	<b>1%</b>
Intangible assets	493,196	495,977	2,781	1%

**2017 Budget vs. Actual - Detail of Third Party Services Providers' Expenses**

	<b>Budget</b>	<b>Actual</b>	<b>Variance</b>	
	<b>2017</b>	<b>2017</b>	<b>RON</b>	<b>%</b>
	<b>RON</b>	<b>RON</b>	<b>RON</b>	
<b>Third party service providers' expenses</b>	<b>87,692,763</b>	<b>72,868,226</b>	<b>(14,824,537)</b>	<b>-17%</b>
Administration fees	68,155,575	63,049,843	(5,105,732)	-7%
Legal and litigation assistance	10,608,273	6,579,540	(4,028,733)	-38%
GSM organisation	1,071,000	627,983	(443,017)	-41%
External audit	453,450	334,767	(118,683)	-26%
Tax compliance & tax advisory expenses	523,412	450,514	(72,898)	-14%
Software maintenance and support fees	478,179	162,608	(315,571)	-66%
Trade Register and Official Gazette expenses	261,800	256	(261,544)	-100%
Internal audit	187,425	178,500	(8,925)	-5%
Other third party service providers' expenses	5,953,649	1,484,215	(4,469,434)	-75%

Note: The administration fees amounting to RON 63 million reported under actual amounts include only the amounts recognised in profit or loss during the period. The total administration fees for 2017 amount to RON 78 million and additional details are included on page 13 of this report.

**Annex 2**

**Table of unlisted holdings valuation at 29 December 2017 versus 31 December 2016**

	Portfolio company name	Value in 29 Dec	Value in 31 Dec	Impact on Total	29 Dec 2017
		2017 NAV	2016 NAV	NAV	NAV vs. 31 Dec 2016 NAV %
		(RON Million)	(RON Million)	(RON Million)	
1	Hidroelectrica SA	3.566,00	3.384,00	182,00	5,40%
2	CN Aeroporturi Bucuresti SA	774,00	761,00	13,00	1,70%
3	E-Distributie Banat SA	545,00	599,90	(54,90)	-9,20%
4	Engie Romania SA	472,00	453,40	18,60	4,10%
5	E-Distributie Muntenia SA	419,00	449,40	(30,40)	-6,80%
6	E-Distributie Dobrogea SA	342,00	380,20	(38,20)	-10,00%
7	Societatea Nationala a Sarii SA	233,00	181,00	52,00	28,70%
8	CN Administratia Porturilor Maritime SA	230,00	216,00	14,00	6,50%
9	ENEL Energie Muntenia SA	61,00	70,30	(9,30)	-13,20%
10	ENEL Energie SA	57,00	75,50	(18,50)	-24,50%
11	Posta Romana SA	35,00	43,00	(8,00)	-18,60%
12	Complexul Energetic Oltenia SA	32,00	-	32,00	100,00%
13	Zirom SA	26,80	25,50	1,30	5,10%
14	Aeroportul International Timisoara - Traian Vuia SA	22,00	3,60	18,40	511,10%
15	Aeroportul International Mihail Kogalniceanu - Constanta SA	2,40	1,70	0,70	41,20%
16	Plafar SA	2,00	2,20	(0,20)	-9,10%
	<b>TOTAL</b>	<b>6.819,20</b>	<b>6.646,70</b>	<b>172,50</b>	<b>2,60%</b>

Note: The table does not include Electrica SA subsidiaries, which were sold in November 2017