

REPORT ON THE OPERATION OF THE AUDIT COMMITTEE OF THE BOARD OF DIRECTORS OF GAS NATURAL SDG, S.A. DURING 2017.

This is a free translation of a Spanish language document which has been provided for purposes of convenience. In case of discrepancies, the Spanish version shall prevail. Gas Natural Fenosa shall not be responsible for any deviations between the translation and the Spanish language document

In accordance with Recommendation No. 36 of the Unified Code of Good Governance (version 2015), the Board of Directors shall annually evaluate, among other aspects, the quality and efficiency of its operation and its Committees. To this end, the various Committees shall submit their own evaluations to the Board. It must be highlighted that for this financial year, in accordance with said recommendation, the Board has had assistance in performing said evaluation from Ramón y Cajal Abogados, as an independent adviser.

In accordance with the foregoing, the present report relating to the operation of the Audit Committee of the Board of Directors of GAS NATURAL SDG S.A. is issued in accordance with the following considerations and conclusions.

In terms of its operation, the Audit Committee is subject, in addition to applicable legal and statutory rules, to its own internal standard, i.e. the organizational and operational Regulations of the Board of Directors and its Committees (hereinafter “RBD”), approved at the meeting of 24 March 2004, whose object is the regulation of these Governing Bodies, establishing for that purpose the principles of its organization and operation, the rules governing its legal and statutory activity and its supervisory and control regime.

The latest version of the RBD is that of 21 September 2016, which was duly reported in the first General Shareholders’ Meeting to be held after said date.

To disseminate the RBD and make it publicly available, it has been registered in the Mercantile Registry of Madrid, and is permanently published on the Company’s website (www.gasnaturalfenosa.com).

During the 2017 financial year the Audit Committee has held 10 meetings.

The Audit Committee has acted within its powers, adopting as many resolutions and issuing as many reports as are necessary or as have been expressly requested thereto.

The composition of the Audit Committee adheres to, in terms of the structure and typology of its members, the principles that prevail in the field of corporate governance.

The Audit Committee is composed of seven (7) Directors and one (1) Non-Board Member Secretary.

At 31 December 2017 the arrangement of positions in the Audit Committee was as follows:

			Member since
Chairman:	Mr Ramón Adell Ramón (*)	Independent	20/04/2012
Board Members-Directors:	Mr Enrique Alcántara-García Irazoqui	Nominee	21/09/2016
	Mr Xabier Añoveros Trías de Bes	Independent	21/09/2016
	Ms Cristina Garmendia Mendizábal	Independent	21/09/2016
	Ms Helena Herrero Starkie	Independent	21/09/2016
	Mr Rajaram Rao	Nominee	21/09/2016
	Mr Luis Suárez de Lezo Mantilla	Nominee	28/01/2011
Secretary:	Mr Manuel García Cobaleta		

(*) Mr Ramón Adell Ramón was appointed as Chairman of the Audit Committee by agreement of the Board on 28 November 2014. The provisions of the Articles of Association (Art. 51 bis) state that the Chair of said Committee may serve a maximum consecutive term of four years, although

they may be re-elected one year after having relinquished their position as Chair. Therefore, Mr Ramón Adell Ramón's term as Chairman shall expire on 28 November 2018.

The profile of each of the members can be consulted on the Company's website www.gasnaturalfenosa.com, (Shareholders and Investors – Corporate Governance – Governing Bodies – Composition of the Board of Directors of GAS NATURAL SDG, S.A.).

In another vein, it is worth mentioning that the Committee absenteeism during the 2017 financial year has been minimal and indispensable (7.14%), as is clear from the following table of absences:

For the present purposes, absenteeism is considered to be the absence of the member from the corresponding Committee, regardless of whether or not they have delegated their representation to another member.

DIRECTORS	AUDIT COMMITTEE 10 MEETINGS
Mr Ramón Adell Ramón	-
Mr Enrique Alcántara-García Irazoqui	2
Mr Xabier Añoveros Trías de Bes	-
Ms Cristina Garmendia Mendizábal	-
Ms Helena Herrero Starkie	1
Mr Rajaram Rao	-
Mr Luis Suárez de Lezo Mantilla	2

Ordinarily, in cases where there has been a failure to attend, the absent Director will have delegated their representation and vote to another member of the Committee.

The Secretariat of the Committee convened meetings in advance of that established in the RBD, following instructions from the Chairman and provided the information and documentation that was available and which was considered appropriate or relevant to the topics to be addressed.

The meetings of the Committee took place at the registered office of the Company, located at Plaça del Gas nº 1, Barcelona and Avda. de San Luis nº 77, Madrid.

The discussions at the meetings were extensive and rich in content, with the active participation of the Directors, and with all resolutions unanimously adopted by those attending the sessions.

The Company's senior executives were specifically invited to certain meetings in order to outline matters relating to their Management Boards, or to answer questions on any competency-related issues posed by the board members.

The internal auditor has attended five (5) meetings of the Committee, as has the external auditor.

Pursuant to Article 51 bis of the Articles of Association and Article 32 of the Board Regulations, the Audit Committee has the powers set out in legislation and those that are commissioned by the Board of Directors, whether of a general or specific nature.

Article 529 *quaterdecies* of the Corporate Enterprises Act specifies that the Audit Committee shall have at least the following duties:

- a) Informing the General Meeting of Shareholders on issues that arise with regard to those matters for which the committee holds terms of reference and, in particular, with regard to

the results of the audit, explaining how this has contributed to the integrity of financial reporting and the function that the committee has carried out in that process.

- b) Supervising the efficacy of the company's internal control, internal auditing and risk management systems, as well as discussing with the accounts auditor any significant weaknesses of the internal control system detected during the audit. All this must be performed without jeopardising the auditor's independence. To this end, and where appropriate, recommendations or proposals may be forwarded to the governing body along with the corresponding deadline for follow-up.
- c) Supervising the process of compiling and submitting the compulsory financial information and presenting recommendations or proposals to the governing body targeted at safeguarding its integrity.
- d) Forwarding proposals for selection, appointment, re-election and replacement of the accounts auditors to the Board of Directors, taking responsibility for the screening process, pursuant to the provisions set out in Articles 16, sections 2, 3 and 5, and 17.5 of Regulation (EU) 537/2014 of 16 April. Furthermore, setting the contractual conditions for the auditor and receiving regular information from the auditor with regard to the performance of the audit plan, and guaranteeing the auditor's independence in the performance of its duties.
- e) Establishing the appropriate relationships with the external auditor to receive information on those issues that could jeopardise their independence, to be scrutinised by the committee, and any others related to the accounts auditing procedure. Furthermore, its functions include the authorisation of services other than those that are banned, under the terms set out in Article 5, section 4, and 6.2.b) of Regulation (EU) 537/2014 of 16 April, and the provisions set out in section 3, chapter IV, heading I, Law 22/2015 of 20 July, on Accounts Auditing, concerning the structure of independence, as well as those other communications set out in accounts auditing legislation and audit standards. Under all circumstances, every year the committee must receive the declaration of the auditor's independence with regard to the entity or entities directly or indirectly related to the company, as well as detailed and individualised information on any additional services rendered and the corresponding fees received by the external auditor or by the persons or entities related to this party, pursuant to the provisions set down in accounts auditing regulations.
- f) Issue annually, prior to the issuance of the audit report, a report in which an opinion will be expressed on whether the independence of the auditors of accounts or audit companies is compromised. In all cases, this report must contain a reasoned assessment of the provision of each and every one of the additional services referred to above, considered on an individual basis and as a whole, separate from the legal auditing and with regard to the structure of independence or with regard to accounts auditing regulations.
- g) Informing the Board of Directors beforehand with regard to all issues provided for under Law, the Articles of Association and the Board Regulations, and in particular concerning:
 - 1. The financial reporting that the company must regularly disclose;
 - 2. the creation or acquisition of shares in entities with special purposes or domiciled in countries or territories that are considered tax havens and
 - 3. transactions with associated parties.

Through a resolution of the Board of Directors of 27 November 2015, and pursuant to the 2015 Good Corporate Governance Recommendations from the National Securities Market Commission (CNMV), the Audit Committee was commissioned with the following duties:

- Drawing up the report on the auditor’s independence.
- Drawing up the report on performance of the Audit Committee.
- Drawing up the report on related-party transactions.
 - Drawing up the report on corporate responsibility. Said reports will be published on the Company’s website sufficiently in advance of the General Shareholders’ Meeting.
- Ensuring that the Board of Directors seeks to present the accounts to the General Meeting of Shareholders without reservation or exception in the Audit Report and, in any exceptional case, both the Chairman of the Audit Committee and the auditors should clearly explain to shareholders the content and scope of said reservations or exceptions.
- In relation to the control and reporting systems:
 - Supervising the preparation and completeness of the financial information concerning the company and, if appropriate, the group, checking due compliance with the governing regulations, the proper delimitation of the consolidation criteria and the correct application of accounting criteria.
 - Ensuring independence of the unit that assumes the internal audit function; approving the work plans and guidelines, making sure that its activities are mainly focused on relevant risks for the company; receiving periodic information on its activities; and verifying that senior management take into consideration the conclusions and recommendations of its reports. Making proposals to the Chairman of the Board of Directors with regard to the selection, appointment, re-election and removal from office of the party responsible for the internal audit service, and proposing the budget for that service. The final decision lies with the Chairman of the Board of Directors.
 - Setting up and supervising a mechanism that enables employees to communicate any significant irregularities, especially those related to finance and bookkeeping, and to do so in a confidential manner and, if considered suitable, anonymous.
- In relation to the external auditor:
 - In the case of the resignation of the external auditor, it should examine the circumstances leading to the said resignation.
 - Ensure that the remuneration of the external auditor does not compromise its quality or its independence.
 - Verify that the company notifies the change of auditor to the CNMV as a relevant event and attach a declaration on the possible existence of disagreements with the outgoing auditor and, if there are any disagreements, the content thereof.
 - Ensure that the external auditor holds an annual meeting with the full Board of Directors to report on the work carried out and the evolution of the accounting situation and of the company’s risks.
 - Ensure that the company and the external auditor observe current standards on the provision of services other than auditing services, the limits to the auditor’s business concentration and, in general, the other standards established to guarantee the independence of auditors.
- Call any of the company’s employees or managers, and also have them appear without the presence of any other executive.

- Analyse and report to the Board of Directors with regard to the economic conditions and the accounting impact and, more particularly, where appropriate, on the exchange ratio, with regard to structural and corporate modification operations which, because of their nature or amount, are of particular relevance. Transactions shall be considered to have such relevance when the net value exceeds 25% of the assets shown on the last approved balance sheet of the company.
- With regard to supervision of compliance with the corporate governance rules, the codes of conduct and the corporate responsibility policy:
 - Supervision of compliance with the internal codes of conduct and the corporate governance rules of the company.
 - Supervision of the communication strategy and relations with shareholders and investors, including small and medium shareholders.
 - Regular assessment of the appropriateness of the company's corporate government system, to ensure that it complies with its mission of fostering social interest and takes into consideration, as appropriate, the legitimate interests of remaining stakeholders.
 - Revision of the Company's corporate responsibility policy, ensuring it is oriented towards the creation of value.
 - Monitoring of the corporate responsibility strategy and practices and assessment of the degree of compliance therewith.
 - Supervision and evaluation of the processes for conducting relations with the different stakeholders.
 - Assessment of everything concerning the Company's non-financial risks, including operational, technological, legal, social, environmental, political and reputational risks.
 - Coordination of the process for reporting non-financial and diversity information, in accordance with the applicable regulations and international reference standards.

Subsequently, on 29 January 2016, the Board of Directors agreed to entrust the Appointments and Remuneration Committee with the tasks related to Corporate Social Responsibility.

Within its powers, the audit Committee has debated, examined or adopted decisions or issued reports on, among other things, the following (while ensuring due confidentiality regarding certain matters):

- Conclusions of the External Audit of the Individual and Consolidated Annual Accounts of GAS NATURAL FENOSA for 2016.
- Update of lawsuits and disputes.
- Activities of the Compliance Evaluation Committee.
- Crime Prevention Model.
- Evolution of the 2016 Internal Audit Plan.
- Treasury Stock.
- Proposals for contracting the External Auditor for services other than the auditing of accounts.
- Report on compliance of the Internal Code of Conduct in matters relating to the Securities Market.
- Report on compliance of the Board Regulations and of its Committees during the 2016 financial year.
- 2016 Annual Financial Report.

- Proposal to the Board, for submission to the General Meeting, on the appointment of the External Accounts Auditors of GAS NATURAL S.D.G. S.A. and its Consolidated Group companies for the financial year 2017.
- GAS NATURAL CAPITAL MARKETS.
- Report on the Group's tax situation.
- Activities of the Code of Ethics Committee.
- 2017 Budget for the Internal Audit Unit.
- 2016 Annual Report on the functions and activities of the Audit Committee.
- 2016 Annual Report on the functions and activities of the Audit Committee.
- 2016 Annual Report on related-party transactions.
- Annual Corporate Governance Report 2016.
- Related-party transactions.
- Intermediate management declaration for the 1st quarter of 2017.
- 2017 Corporate Risk Map.
- Evaluation of the Internal Control System on Financial Reporting (SCIIF).
- Half-Yearly Financial Report.
- Analysis of the CNMV Technical Guide 3/2017.
- Intermediate management declaration for the 3rd quarter of 2017.
- Adoption of NIIF 9 Financial Instruments.
- Technical Guide to Auditing Public Interest Entities.
- Proposed schedule and topics to be addressed in the Committee during 2018.
- Safety, Health and Environment Policies of GAS NATURAL FENOSA and main activity indicators for 2017.

Furthermore, as a result of the relations with the Auditor, from the analysis of the contracting carried out, other than for the auditing service and related services, and from the written confirmation of the Auditor regarding their independence, this Committee states that no incident has been identified regarding the independence of PricewaterhouseCoopers in the delivery of its services, both with regard to that concerning the work of the auditor itself and in any services provided in addition to auditing and related services.

Additionally, during the 2017 financial year the Committee proceeded to perform a detailed analysis of the different recommendations included in the Technical Guide 3/2017 on the Audit Committees of Public Interest Entities approved by the National Securities Market Commission (CNMV) on 27 June 2017. The conclusions of said analysis were presented to the Board of Directors in December 2017, and the Board confirmed that a large number of said recommendations were already being followed in practice, requesting that explicit mention be made of this fact. Furthermore, as regards the functions and competencies of the Committee, it was concluded that it would be suitable to maintain these in the terms established by the Capital Companies Act, to guarantee the distribution of powers established by the legislator.

In conclusion, it can be stated that during the 2017 financial year the Audit Committee has operated as expected; in particular, it must be highlighted that, as reflected in the independent adviser's report, no deficiencies have been detected that require any special action or that specifically affected the Audit Committee, fully exercising, without interference, its powers with total respect for the law and the rules of the organization and operation of its own RBD.

Madrid, 8 January 2018.
The Audit Committee of GAS NATURAL SDG, S.A.