

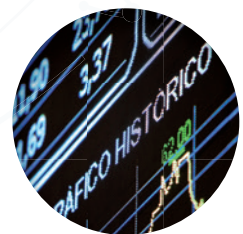
Gas Natural SDG
2016 Annual
Report



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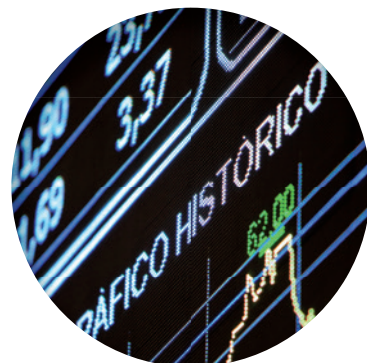
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Audit Report



This version of our report is a free translation of the original, which was prepared in Spanish. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation

INDEPENDENT AUDITOR'S REPORT ON ANNUAL ACCOUNTS

To the Shareholders of Gas Natural SDG, S.A.:

Report on the Annual Accounts

We have audited the accompanying annual accounts of Gas Natural SDG, S.A., which comprise the balance sheet as at December 31, 2016, and the income statement, statement of changes in equity, cash flow statement and related notes for the year then ended.

Directors' Responsibility for the Annual Accounts

The company's Directors are responsible for the preparation of these annual accounts, so that present fairly the equity, financial position and financial performance of Gas Natural SDG, S.A., in accordance with the financial reporting framework applicable to the entity in Spain, as identified in Note 3 to the accompanying annual accounts, and for such internal control as Directors determine is necessary to enable the preparation of annual accounts that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these annual accounts based on our audit. We conducted our audit in accordance with legislation governing the audit practice in Spain. This legislation requires that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the annual accounts are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the annual accounts. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the annual accounts, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the annual accounts in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the presentation of the annual accounts taken as a whole.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

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Opinion

In our opinion, the accompanying annual accounts present fairly, in all material respects, the equity and financial position of Gas Natural SDG, S.A. as at December 31, 2016, and its financial performance and its cash flows for the year then ended in accordance with the applicable financial reporting framework, and in particular, with the accounting principles and criteria included therein.

Report on Other Legal and Regulatory Requirements

The accompanying Directors' Report for 2016 contains the explanations which the Directors consider appropriate regarding Gas Natural SDG, S.A.'s situation, the development of its business and other matters and does not form an integral part of the annual accounts. We have verified that the accounting information contained in the Directors' Report is in agreement with that of the annual accounts for 2016. Our work as auditors is limited to checking the Directors' Report in accordance with the scope mentioned in this paragraph and does not include a review of information other than that obtained from the company's accounting records.

PricewaterhouseCoopers Auditores, S.L.



Iñaki Goiriena Basualdu

February 10, 2017

Balance Sheet of Gas Natural SDG, S.A.

(million euros)	31/12/16	31/12/15
Non-current assets	29,993	29,907
<i>Intangible assets (Note 7)</i>	195	272
Goodwill	190	272
Other intangible assets	5	–
<i>Property, plant and equipment (Note 8)</i>	153	179
Land and buildings	140	167
Plant and other property, plant and equipment	13	12
<i>Long-term investments in Group companies and associates (Note 9)</i>	29,443	29,308
Equity instruments	13,688	14,613
Loans to companies	15,755	14,695
<i>Long-term investments (Note 10)</i>	74	15
Equity instruments	5	5
Derivatives	59	1
Other financial assets	10	9
Deferred income tax assets (Note 19)	128	133
Current assets	2,084	2,739
<i>Trade and other receivables (Note 11)</i>	670	701
Trade receivables	145	95
Group companies and associates	368	400
Sundry receivables	153	192
Current income tax assets	–	10
Public Administrations	4	4
<i>Short-term investments in Group companies and associates (Note 9)</i>	883	730
Loans to companies	816	727
Other financial assets	67	3
<i>Short-term investments (Note 10)</i>	27	63
Other financial assets	27	63
Short-term prepayments and accrued expenses	2	1
<i>Cash and cash equivalents (Note 12)</i>	502	1,244
Cash at banks and in hand	502	1,089
Other cash equivalents	–	155
Total assets	32,077	32,646

Balance Sheet of Gas Natural SDG, S.A.

(million euros)	31/12/16	31/12/15
Net equity (Note 13)	13,444	13,285
Shareholders' equity	13,431	13,298
Capital	1,001	1,001
Authorised capital	1,001	1,001
Share premium	3,808	3,808
Reserves	7,898	7,873
Legal and statutory	300	300
Other reserves	7,598	7,573
Treasury shares	(13)	–
Profit for the year	1,067	1,024
Interim dividend	(330)	(408)
Adjustments for changes in value	13	(13)
Hedging operations	13	(13)
Non-current liabilities	14,626	15,114
Long-term provisions (Note 14)	467	481
Long-term post-employment obligations	285	283
Other provisions	182	198
Long-term borrowings (Note 15)	3,300	3,159
Borrowings from financial institutions	3,190	2,983
Derivatives	93	161
Other financial liabilities	17	15
Amounts owing to group companies and associates falling due in more than one year (Note 17)	10,627	11,239
Deferred income tax liabilities (Note 19)	231	234
Long-term accruals	1	1
Current liabilities	4,007	4,247
Short-term borrowings (Note 15)	297	621
Borrowings from financial institutions	270	187
Derivatives	15	14
Other financial liabilities	12	420
Amounts owing to group companies and associates falling due in less than one year (Note 17)	3,000	2,891
Trade and other payables (Note 18)	710	735
Trade payables	242	247
Payables with group companies and associates	311	254
Sundry payables	93	196
Personnel (outstanding remuneration)	23	22
Current tax liabilities	24	–
Other amounts payable to Public Administrations	17	16
Total net equity and liabilities	32,077	32,646

Income Statement of Gas Natural SDG, S.A.

(million euros)	2016	2015
Net turnover (Note 20)	5,062	5,640
Sales	3,088	3,640
Income from equity instruments of Group companies and associates (Note 9)	1,560	1,542
Income from marketable securities and other financial instruments of Group companies and associates	414	458
Supplies (Note 21)	(3,118)	(3,647)
Consumption of goods	(3,113)	(3,641)
Raw materials and other consumables	(5)	(6)
Other operating income (Note 24)	444	361
Supplementary income and other operating income	443	359
Operating grants released to the income statement	1	2
Personnel costs (Note 22)	(201)	(191)
Wages, salaries and related expenses	(152)	(143)
Social Security	(34)	(33)
Provisions	(15)	(15)
Other operating expenses (Note 23)	(337)	(365)
External services	(330)	(326)
Taxes	(2)	(2)
Impairment loss and variation in trade provisions	(5)	(8)
Other current operating expenses	–	(29)
Amortisation expense (Notes 7 and 8)	(94)	(92)
Impairment and results on disposals of fixed assets	(139)	(109)
Gain/(loss) on disposals of tangible fixed assets (Note 8)	36	–
Impairment and losses from equity instruments of Group companies and associates	(206)	(106)
Gain/(loss) on disposals of equity interests in Group companies and associates (Note 9)	31	(3)
Operating profit	1,617	1,597
Financial income	30	29
Negotiable securities and other financial instruments	30	29
In third parties	30	29
Financial expenses	(664)	(698)
Borrowings from group companies and associates	(569)	(580)
Borrowings from third parties	(95)	(118)
Variation in fair value of financial instruments	(1)	2
Investments	(1)	2
Net exchange gains / losses	1	(13)
Net financial income (Note 25)	(634)	(680)
Profit before tax	983	917
Income tax (Note 19)	84	107
Profit for the year	1,067	1,024
Basic and diluted earnings per share in Euros	1.07	1.02

Statement of Changes in Net Equity of Gas Natural SDG, S.A.

A) Statement of income and expense recognised

(million euros)	2016	2015
Profit for the year	1,067	1,024
Income and expense recognised directly in net equity	20	(4)
Cash flow hedges	24	(9)
Actuarial gains and losses and other adjustments (Note 14)	3	4
Tax effect (Note 19)	(7)	1
Releases to income statement	8	8
Cash flow hedges	10	11
Tax effect (Note 19)	(2)	(3)
Total income and expense recognised in net equity	1,095	1,028

B) Statement of Total Changes in Net Equity

(million euros)	Share capital	Share premium	Reserves	Treasury shares	Profit or loss brought forward	Profit for the year	Interim dividend	Adjustments for changes in value	Grants, donations and bequests received	Total
Balance at 01/01/2015	1,001	3,808	8,145	-	-	1,083	(397)	(14)	3	13,629
Adjustments for changes in accounting policy (Note 4)	-	-	(451)	-	-	-	-	-	-	(451)
Adjusted balance at 01/01/2015	1,001	3,808	7,694	-	-	1,083	(397)	(14)	3	13,178
Total recognised revenues and expenses	-	-	3	-	-	1,024	-	1	-	1,028
Operations with partners or owners										
<i>Dividend distribution (Note 14)</i>	-	-	-	-	(512)	-	(408)	-	-	(920)
Trading in treasury shares	-	-	2	-	-	-	-	-	-	2
Reductions due to business combinations	-	-	-	-	-	-	-	-	(3)	(3)
Other variations in net equity (Note 4)	-	-	174	-	512	(1,083)	397	-	-	-
Balance at 31/12/2015	1,001	3,808	7,873	-	-	1,024	(408)	(13)	-	13,285
Total recognised revenues and expenses	-	-	2	-	-	1,067	-	26	-	1,095
Operations with partners or owners										
Dividend distribution (Note 14)	-	-	-	-	(593)	-	(330)	-	-	(923)
Trading in treasury shares (Note 14)	-	-	-	(13)	-	-	-	-	-	(13)
Other variations in net equity (Note 14)	-	-	23	-	593	(1,024)	408	-	-	-
Balance at 31/12/2016	1,001	3,808	7,898	(13)	-	1,067	(330)	13	-	13,444

Statement of cash flows of Gas Natural SDG, S.A.

(million euros)	2016	2015
Profit/(loss) for the year before tax	983	917
Adjustments to results	(1,112)	(1,163)
Fixed asset depreciation (<i>Notes 7 and 8</i>)	94	92
Impairment adjustments	211	114
Change in provisions	6	39
Profit/(loss) on write-offs and disposals of fixed assets	(36)	–
Profit/(loss) on write-offs and disposals of financial instruments	(31)	3
Financial income	(2,004)	(2,029)
Financial expenses	664	698
Gains/(losses) on exchange	(1)	13
Change in fair value of financial instruments	1	(2)
Other income and expenses	(16)	(91)
Changes in working capital	28	(463)
Inventories	–	–
Debtors and other receivables	10	(128)
Other current assets	(1)	1
Creditors and other payables	19	(336)
Other cash flows from operating activities	1,529	1,662
Interest paid	(640)	(669)
Dividends received	1,560	1,542
Interest collected	447	493
Income tax collections/(payments)	162	296
Cash flows from operating activities	1,428	953

Statement of cash flows of Gas Natural SDG, S.A. (continued)

(million euros)	2016	2015
Amounts paid on investments	(2,071)	(1,634)
Group companies and associates	(2,047)	(1,623)
Property, plant and equipment	(16)	(10)
Other financial assets	(8)	(1)
Amounts collected from divestments	1,639	866
Group companies and associates	1,571	865
Property, plant and equipment	66	–
Other financial assets	2	1
Cash flows from investing activities	(432)	(768)
Collections and payments equity instruments	(13)	–
Acquisition of own equity instruments	(13)	–
Collections and payments financial liability instruments	(394)	(838)
Issued	6,347	4,873
Bank borrowings	801	287
Payables to Group companies and associates	5,546	4,583
Other payables		3
Repayment/redemption of	(6,741)	(5,711)
Bank borrowings	(531)	(1,165)
Payables to Group companies and associates	(6,187)	(4,514)
Other payables	(23)	(32)
Dividend payments	(1,331)	(909)
Cash flow from financing activities	(1,738)	(1,747)
Net increase/decrease in cash or cash equivalents	(742)	(1,562)
Cash and cash equivalents at the beginning of the year	1,244	2,806
Cash and cash equivalents at the year end	502	1,244

Notes to the annual accounts of Gas Natural SDG, S.A. for the year ended 31 December 2016

Note 1. General information

Gas Natural SDG, S.A. (hereon, the Company), parent company of Gas Natural Fenosa group (hereon, Gas Natural Fenosa), was incorporated as a public limited company in 1843 and its registered office for corporate purposes is in Plaça del Gas, number 1, Barcelona.

The company's corporate purposes, as per its articles of association, comprise the following activities:

- a) All types of activities related to the gas and electricity business and any other type of existing energy source, the production and selling of electrical, electro-mechanical and electronic equipment and components, management of architectural projects, civil engineering works, public services and gas and hydro-carbon distribution in general; management of communications and telecommunications networks and maintenance of electro- and gas-related appliances; as well as consulting, business and energy planning services and the rationalisation of energy use, research, development and exploitation of new technologies, communications, computer and industrial security systems; training and selection of human resources and real estate management and development.
- b) The activity as a holding company, incorporating companies or holding shares as a stakeholder or shareholder in other companies no matter what their corporate purposes or nature, by subscribing, acquiring or holding shares, stakes or any other securities deriving from the same, subject to compliance with the legal requirements in each and every case.

The Company's most relevant ordinary activity is the holding of shares in subsidiaries through which the Company pursues its corporate objects.

The shares of Gas Natural SDG, S.A. are listed on the four Spanish stock exchanges, the continuous market and form part of the Ibex 35 stock index.

Note 2. Regulatory framework

2.1. Regulation of the natural gas industry in Spain

Main characteristics of the natural gas industry in Spain

The Spanish gas sector is regulated by Law 34/1998, October 7, on the hydrocarbons sector, as amended by Law 12/2007, July 2, Royal Decree-law 13/2012 and Law 18/2015, May 21, as well as Law 18/2014, and by its enabling regulations, the most relevant being Royal Decree 1434/2002, December 27, Royal Decree 949/2001, August 3 and Royal Decree 984/2015, 30 October.

The Ministry of Energy, Tourism and the Digital Agenda (MINETAD) is the competent organisation in the regulation of the gas and electricity industries, while the National Markets and Competition Commission (CNMC) is the regulatory authority in charge of maintaining and ensuring effective competition and transparent functioning of the Spanish energy industries. Prior to the publication of Law 3/2013 of June 4, these functions were performed by the National Energy Commission (CNE), which has been integrated into the CNMC. The relevant Ministries of the Regional Governments have competencies in legislative, enforcement and legislation.

Furthermore, the Technical Manager of the System, Enagás, S.A., is responsible for the appropriate functioning and coordination of the gas system. It should therefore be borne in mind that Law 12/2007 limits the shareholding in Enagás, S.A. to a maximum of 5% of its share capital, and voting rights to 3% in general, and the voting rights of participants in gas activities to 1%, and, in any case, the sum of the interest of the shareholders undertaking activities in the gas sector cannot exceed 40%.

In general, the Spanish gas sector has the following main characteristics:

- It is an industry in which regulated and unregulated activities coexist. The regulated activities consist of transport, regasification, storage and distribution of natural gas. The non-regulated activities comprise generation, supply and retailing of natural gas.
- The natural gas sector is almost entirely dependent on foreign supplies of natural gas, which represent almost 99.9% of the natural gas supply in Spain.
- Under EU legislation (Directives 2003/55/CE of June 26, and 2009/73/EU), the supply of natural gas in Spain is totally non-regulated, and all Spanish consumers can freely choose their natural gas provider as from 1 January 2003. The deregulation procedure for the industry has been reinforced substantially by the disappearance as from 1 July 2008 of the bundled tariff of distribution companies and the subsequent right of consumers to participate in the deregulated market (although as indicated further below a tariff of last resort has been maintained for consumers of lower consumption).

The Company supplies gas that is subsequently sold mainly to other Gas Natural Fenosa companies. This activity is treated as described below:

Natural gas is supplied in Spain mainly by gas operators such as Gas Natural Fenosa under long-term contracts with gas producers. Although such supplies are not regulated, they are subject to two types of limit, basically to assure supply diversification and competition in the market: 1) no country may be source of more than 60% of the natural gas brought to Spain; and 2) no party or business group may bring natural gas to Spain for consumption in a volume exceeding 70% of domestic consumption, excluding self-consumption.

2.2. Regulation of the electricity sector in Spain

Main characteristics of the electricity sector in Spain

The regulation of the electricity industry in Spain has undergone a major reform process during the year 2013 which led to the publication of Law 24/2013, of 26 December, of the Electricity Sector, which adapts the previous law (Law 54/1997, of 27 November) to the circumstances of both the economy and the power and energy sector in Spain.

The Ministry of Industry, Energy and Tourism is the body responsible for regulating the gas and electricity sectors, while the CNMC is the regulatory authority that is entrusted with the task of maintaining and ensuring effective competition and transparent functioning of Spanish energy sectors. The relevant Ministries of the Regional Governments have competencies in legislative, enforcement and legislation. The Nuclear Safety Council exercises specific competencies over the facilities using this technology.

Furthermore, the Technical System Manager, Red Eléctrica de España, S.A. (REE), has the main function of guaranteeing the continuity and safety of the electricity supply and the proper coordination of the production and transport system. Thus, please bear in mind that law provides a strict legal separation between the system operator and the activities of generation or sale of electric power.

Generally, the electricity sector has the following main features:

- > It is a sector in which regulated and non-regulated activities coexist. The regulated activities consist of transport and electricity distribution (as well as system and market operation).

Following the directives of EU legislation (Directives 2009/72/CE), all Spanish consumers can freely choose their electricity provider. A system of regulated tariff applies to consumers with contracted capacity of less than 10 kW. This regulated tariff has been referred to as the Small Consumer Voluntary Price (PVPC), and it also exists the last-resort tariff (TUR) having become the regulated price applicable to consumers classed as vulnerable and to consumers that do not meet requirements to apply the PVPC but are temporarily without a supply company in the free market. The last-resort tariff (TUR) for vulnerable consumers is funded by the social bond which will be assumed by the parent companies of electricity supply groups or by individual electricity supply companies if they do not form part of a group.

- > The electricity consumed in Spain is mostly generated domestically, since the international connections with France and Portugal have a very small capacity.
- > Since July 1, 2007 the Iberian Electricity Market (MIBEL) has begun to operate effectively between Spain and Portugal, which has involved the integration of the electricity systems of both countries (although this integration is still not perfect).
- > During the period 2000-2013, the electricity system was not self-sufficient in terms of price, an annual deficit having been generated and financed by the conventional electricity companies, including Gas Natural Fenosa.

With the aim of eliminating the sector deficit, a number of provisions introduced in recent years have brought in important measures and adjustments to electricity sector activities to correct departures caused by mismatches between costs and revenue, culminating in the regulatory package known as the July 2013 electricity reform and the approval in December 2013 of Electricity Sector Law 24/2014, which established the basic principle of the sector's economic and financial sustainability.

Finally, on 27 December, Law 24/2013 (26 December) on the electricity sector was published, being the main developments as follows:

- > With respect to the principle of the system's economic and financial sustainability:
 - The remuneration calculation parameters will have a six-year term and will be reviewed prior to the start of the regulatory period taking into account the economic cycle, demand for electricity and an adequate return from these activities.
 - A distinction is made between transport and distribution network access tolls and the charges that are necessary to cover other costs of the relevant system activities, which will be determined using methodology to be established by the Government; in general, tolls and charges will be reviewed annually or in the event of circumstances that have a material impact on regulated costs or on the calculation parameters employed.
 - Small consumer voluntary prices (PVPC) are regulated and will be the same throughout Spain. These prices are defined in line with the prices previously referred to as last-resort tariffs, as the maximum prices that the reference supply companies may charge consumers that avail themselves of the prices. The last-resort tariff (TUR) has become the regulated price applicable to consumers classed as vulnerable and to consumers that do not meet requirements to apply the voluntary price for small consumers but are temporarily without a supply company in the free market.

- Mismatches due to a revenue deficit are limited to the extent that they may not exceed 2% of revenues estimated for the reference period and cumulative liabilities due to mismatches may not exceed 5% of those revenues. Should these limits not be observed, the relevant tolls or charges will be reviewed. The portion of the mismatch that is not offset by a rise in tolls and charges shall be financed by the parties subject to the settlement system in proportion to their debt claims arising from the activities performed. The amounts contributed in this way will be reimbursed in the settlements for the following five years, plus applicable interest. Any surplus revenues generated will be used to offset prior-year mismatches; while there are outstanding prior-year liabilities, the access tolls or charges may not be reduced.
- For year 2013, an income deficit for liquidations of the electrical system for a maximum amount of Euros 3,600 million is recognised. This deficit will generate receivables consisting in the right to receive an amount of the monthly billing for fifteen successive years beginning on January 1, 2014 until its complete satisfaction.
- The obligation to keep separate accounting records is extended, applying not only to the separation of electricity activities from non-electricity activities, but also to the separation of production with regulated remuneration activity from non-regulated. This obligation extends to all producers receiving regulated remuneration.

> Electricity generation:

- The temporary closure of generation facilities is contemplated and will be subject to prior administrative authorisation.
- Hydraulic resources that must be used to generate electricity are regulated as well as the daily market system of offers, with the particularity that all production units must offer its energy in the market, including those operating under the former special regime.
- Electricity demand and contracting, rights and obligations of electricity generators, and specific remuneration regime records are all regulated.

> System's economic and technical management:

- System operator and market operator functions are regulated, as are the procedures for the certification of the system operator by the National Markets and Competition Commission, and for authorisation and designation as a transmission grid manager by the Ministry of Industry, Energy and Tourism, which must be notified to the European Commission, and certification relating to non-European Union countries.
- Grid access and connection is regulated, clearly defining the access right and connection right concepts, as well as access and connection permits, the related grant procedure and requirements, and parties responsible for granting permits subject to technical and economic criteria to be stipulated in enabling regulations.

> Electricity transmission:

- A specific requirement is provided whereby remuneration for new facilities must be included in the planning phase.
- The functions that must be performed by the transmission company are provided, having previously been included in different laws or enabling regulations.

> Electricity distribution:

- A definition of distribution facilities is provided.
- The obligations and functions of electricity distribution companies are stipulated, distinguishing between distribution performed as the owners of distribution grids and distribution performed as grid management companies.

> Regime for inspections, infringements and penalties:

- The classification of infringements is revised and new infringements are included, certain conduct having been identified that had not been envisaged in Law 54/1997 (27 November) but has a negative impact on the electricity system's economic sustainability and functioning.
- The amount of penalties is revised, existing incidental penalties are extended and powers to impose penalties are modified.

Note 3. Basis of presentation

Gas Natural SDG, S.A. Annual accounts for 2015 were approved by the Annual General Meeting on 4 May 2016.

The Annual accounts for 2016, which were issued by the Board of Directors of Gas Natural SDG, S.A. on 7 February 2017, will be submitted to the General Meeting for approval; they are expected to be approved without any changes.

The accompanying Annual accounts have been prepared on the basis of the Company's accounting records and are presented in accordance with prevailing commercial legislation and the provisions of the Chart of Accounts introduced under Royal Decree 1514/2007 (16 November), as amended by Royal Decree 1159/2010 (17 September) and Royal Decree 602/2016 (2 December), so as to present fairly the Company's equity and financial position at 31 December 2016, and the results, changes in equity and cash flows of Gas Natural SDG, S.A. for the year then ended.

The figures set out these Annual accounts are expressed in million euros, unless otherwise stated.

At 31 December 2016, the Company records negative working capital, in the amount of Euros 1,923 million, covered by dividends expected in the following year and the amount drawable on long-term credit lines (Note 16).

The consolidated Annual accounts of Gas Natural Fenosa for 2016 have been prepared in accordance with the International Financial Reporting Standards adopted by the European Union (IFRS-EU), in accordance with Regulation (EU) 1606/2002 of the European Parliament and the Council. The main figures disclosed in the consolidated Annual accounts, which have been audited, are as follows:

Total assets	47,114
Equity attributed to the parent Company	15,225
Minority interests	3,780
Net turnover	23,184
Net income after tax attributed to the parent Company	1,347

Note 4. Comparability

Pursuant to paragraph 2 of the Single Transitional Provision and Additional Provision Two of Royal Decree 602/2016, the Company has opted to calculate the effect of the change in the amortisation of goodwill from the acquisition date of the assets concerned against the goodwill reserve, adjusting the comparative information so that for each item in the balance sheet, income statement, statement of changes in equity, cash-flow statement and notes to the accounts, the figures for the previous year have been included as well as the figures for 2016. The figures for 2015 were calculated by applying the alternative option provided for in Royal Decree 602/2016. As a result, the figures for the previous year relating to these items differ from the figures included in the approved annual accounts for 2015, which were drawn up in accordance with the accounting principle and standards in force in said year.

The changes to the comparative figures are summarised below:

	31/12/15	Adjustments	Adapted to RD 602/2016
Non-current assets	30,440	(533)	29,907
Intangible assets	815	(543)	272
Property, plant and equipment	179	–	179
Long-term investments in Group companies and associates	29,308	–	29,308
Long-term investments	15	–	15
Deferred income tax assets	123	10	133
Current assets	2,739	–	2,739
Total assets	33,179	(533)	32,646
Net equity	13,815	(530)	13,285
Shareholders' equity	13,828	(530)	13,298
Capital	1,001	–	1,001
Share premium	3,808	–	3,808
Reserves	8,324	(451)	7,873
Profit for the year	1,103	(79)	1,024
Interim dividend	(408)	–	(408)
Adjustments for changes in value	(13)	–	(13)
Non-current liabilities	15,117	(3)	15,114
Long-term provisions	481	–	481
Long-term borrowings	3,159	–	3,159
Amounts owing to group companies and associates falling due in more than one year	11,239	–	11,239
Deferred income tax liabilities	237	(3)	234
Long-term accruals and deferred income	1	–	1
Current liabilities	4,247	–	4,247
Total net equity and liabilities	33,179	(533)	32,646

	31/12/15	Adjustments	Adapted to RD 602/2016
Net turnover	5,640	–	5,640
Supplies	(3,647)	–	(3,647)
Other operating income	361	–	361
Personnel costs	(191)	–	(191)
Other operating expenses	(365)	–	(365)
Amortisation expenses	(11)	(81)	(92)
Impairment and results on disposals of financial instruments	(109)	–	(109)
Operating profit	1,678	(81)	1,597
Net financial income	(680)	–	(680)
Profit before taxes	998	(81)	917
Income tax	105	2	107
Profit for the year	1,103	(79)	1,024

Note 5. Demerger of Gas Natural SDG, S.A. in favour of Gas Natural Fenosa Generación, S.L.U. in 2015

On 30 January 2015, the Board of Directors of Gas Natural SDG, S.A. and the Sole Administrator of Gas Natural Fenosa Generación, S.L.U. signed the Plan for the Demerger of Gas Natural SDG S.A.'s nuclear generating business in favour of the wholly-owned company Gas Natural Fenosa Generación, S.L.U. The operation was approved by Gas Natural SDG, S.A.'s General Shareholders' Meeting and by Gas Natural Fenosa Generación, S.L.U.'s Single Shareholder on 11 April 2015 and entered in the Barcelona Mercantile Register on 1 July 2015, once the legally stipulated periods had elapsed and the necessary authorisations had been obtained, with retroactive effects to 1 January 2015 for accounting purposes. Pursuant to Article 89 of Corporate Income Tax Law 27/2014, the demerger was specifically completed under the special scheme provided by Title VII, Chapter VII of that law.

As this contribution was made to a Group company, over which there is control, it was recognised, pursuant to Rule 21 of the Chart of Accounts introduced under Royal Decree 1514/2007 (16 November), as amended by Royal Decree 1159/2010 (17 September), by which consolidation rules are approved, at the carrying amount of the assets and liabilities handed over, in the Group's consolidated Annual accounts on the operation date.

Set out below is a breakdown of the assets and liabilities demerged from the Company at 1 January 2015 in favour of Gas Natural Fenosa Generación, S.L.U.:

Intangible assets	247
Property, plant and equipment	876
Long-term investments	2
Deferred income tax assets	9
Non-current assets	1,134
Inventories	64
Other current assets	33
Current assets	97
Total assets	1,231
Grants	3
Long-term provisions	147
Long-term payables to group companies and associates	543
Deferred income tax liabilities	95
Non-current liabilities	785
Short-term borrowings	12
Trade and other payables	69
Current liabilities	81
Total liabilities	869
Total net assets	362

In exchange for the demerged net assets, Gas Natural SDG, S.A. received the shares involved in the capital increase carried out by Gas Natural Fenosa Generación, S.L.U. amounting to Euros 362 million.

Note 6. Accounting policies

The main accounting principles applied by the Company to prepare these annual accounts are described below.

6.1. Intangible assets

Intangible assets are carried at acquisition price or production cost, or at fair value in the case of assets acquired through a business combination, less accumulated amortisation and any recognised impairment losses.

a) Goodwill

Goodwill represents the excess, on the date of acquisition, of the cost of a business combination over the fair value of the net identifiable assets acquired at the date of the operation. Consequently, goodwill is only recognised when it has been acquired for valuable consideration and relates to the future economic profits from assets that have not been identified individually and recognised separately.

Goodwill is amortised in ten years and it is to be recovered on a straight-line basis. Goodwill is tested annually to analyse possible impairment losses. It is recognised in the consolidated balance sheet at cost value less amortisation and any cumulative impairment adjustments.

The impairment of goodwill cannot be reversed.

b) Other intangible assets

Research expenditure is recognised in the income statement when incurred.

Costs associated directly with the production of computer software programs that are likely to generate economic profits greater than the costs related to their production are recognised as intangible assets. The direct costs include the personnel costs that has developed the computer programs.

Computer software development costs recognized as assets are amortised on a straight-line basis in four to five years as from the time the assets are prepared to be brought into use.

The Company does not have intangible asset with an indefinite useful life.

6.2. Property, plant and equipment

a) Cost

Property, plant and equipment are carried at acquisition price or production cost, or at the value attributed to the asset if it is acquired as part of a business combination.

Financial costs relating to financing for plant projects during the plant construction period to the date the asset is ready for use form part of property, plant and equipment.

Renewal, extension or improvement costs are capitalised as an increase in the asset's value only when its capacity, productivity or useful life increases.

Major maintenance expenditures are capitalised and amortised over the estimated useful life of the asset (generally 2 to 6 years) while minor maintenance is expensed as incurred.

Own work capitalised under Property, plant and equipment relates to the direct cost of production.

Expenses arising from actions designed to protect and improve the environment are expensed in the year they are incurred.

When such costs entail additions to property, plant and equipment the purpose of which is to minimise the environmental impact and to protect and improve the environment, they are accounted for as an increase in the value of property, plant and equipment.

Gains and losses on disposals are determined by comparing proceeds with carrying amounts. These are included in the Income statement.

b) Depreciation

The assets are depreciated on a straight-line basis over their useful lives or the concession term, if shorter. Estimated useful lives are as follows:

	Estimated useful life years
Buildings	33-50
Computer hardware	4
Vehicles	6
Other	3-20

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each Balance sheet date.

When the carrying value of an asset is greater than its estimated recoverable amount or when it is no longer useful, its value is written down immediately to its recoverable amount (Note 6.3).

6.3. Impairment of assets

Assets are tested for impairment provided that an event or change in circumstances indicates that their carrying amount might not be recoverable. Additionally, investments in group companies and associates, long-term investments, goodwill and intangible assets that are not in use are tested annually for impairment.

When the recoverable amount is less than the asset's carrying amount, an impairment loss is recognised through profit and loss for the amount of the difference between the two. The recoverable amount is calculated at the higher of an asset's fair value less costs of sale and value in use calculated by applying the discount cash flow method. In general, Gas Natural SDG, S.A. is considering recoverable amount to be value in use, which is calculated using the methodology described below.

For the purposes of assessing impairment losses, assets are grouped together at the lowest level for which there are separately identifiable cash flows. Assets and goodwill are assigned to these cash-generating units (CGUs).

In the case of investments in group companies, barring investments the recoverable amount of which is determined based on the investee's equity (Note 6.4) and goodwill, the cash flows employed are based on the Strategic Plan approved by Gas Natural SDG, S.A., extended to five years on the basis of regulations and expected market evolution, drawing on available industry forecasts and historical experience of price trends and volumes produced.

The cash flows after the projected period are extrapolated using the growth rates estimated for each CGU or group of CGUs, and in no case exceed the average long-term growth rate for the business in which they operate. In all cases, they are lower than the growth rates stated in the strategic plan. Additionally, in order to estimate future cash flows in the calculation of residual values, all maintenance investments have been considered and, if applicable, renewal investments necessary to maintain the CGUs' production capacity.

The nominal growth rates used for the CGU and financial assets in Spain fluctuate between 1.2% and 2.2% (0.8% and 1.8% in 2015). Specifically, a growth rate of 1.8% has been applied to the shareholding in Unión Fenosa Gas, S.A. (1.4% in 2015). For the businesses in which Gas Natural Distribución Latinoamérica, S.A., Global Power Generation, S.A.U. and Gas Natural Fenosa Internacional, S.A. hold interests, the growth rates used vary between 1.0% and 4.6% (1.0% and 4.9% in 2015).

The cash flows have been discounted using the average costs of funds before tax. For the CGU and financial assets in Spain this cost fluctuates between 5.2% and 6.1% (5.6% and 6.8% in 2015). In the particular case of Unión Fenosa Gas, S.A. the discount rate has been 11.9% (11.0% in 2015). For the businesses in which Gas Natural Distribución Latinoamérica, S.A., Global Power Generation, S.A.U. and Gas Natural Fenosa Internacional, S.A. hold interests, rates are between 5.8% and 17.0% (6.3% and 16.0% in 2015).

The parameters used in the breakdown of the above discount rates have been:

- > Risk free bond: 10-year Bond reference market for the CGU.
- > Market risk premium: Estimate of the variable interest of each country at 10 years.
- > Deleveraged Beta: According to average of each sector in each case.
- > Local current interest rate swaps: 10-year swap.
- > Net Equity-debt ratio: Sector average.

Apart from the discount rates, the most sensitive aspects that are included in the projections used and are based on industry forecasts and historical experience are as follows:

In the case of the investment in Gas Natural Fenosa Generación, S.L.U. and Gas Natural Fenosa Renovables, S.L.U.:

- Electricity generated. Market demand evolution has been estimated based on the consensus expressed by several international bodies. The share has been estimated based on Gas Natural Fenosa's market share in each technology and on the expected evolution of each technology's share of the total market. It has been considered the impacts of Royal Decree-Law 2/2013, Royal Decree-Law 9/2013, Law 24/2013 and Royal Decree-Law 413/2014.
- Electricity price. Market electricity prices used have been calculated using models that cross expected demand with supply forecasts, taking into account the foreseeable evolution of generation capacity in Spain, based on sector forecasts.
- Fuel costs. Estimated by reference to long-term supply contracts concluded by Gas Natural Fenosa, the forecast evolution of price curves and market experience.
- Operation and maintenance costs. Estimated from historical costs of managed park.
- The effect of taxes established by Law 15/2012.

For the investment in Unión Fenosa Gas, S.A.:

- Gas supply costs In accordance with the prices of the long-term contracts entered into by Unión Fenosa, S.A. and expected price fluctuations in spot markets.
- Gas volumes to be obtained from each supply source.
- Selling price of natural gas. Valued using predictive modelling based on the forecast performance of price curves and experience in the markets where Union Fenosa Gas, S.A. operates.

As a result of the above process, in 2016 the recoverable values of the CGUs' assets, calculated using the methodology described, have been, except for the interest in Union Fenosa Gas, S.A., which an impairment have been recognised on such interest (Note 9) higher than the carrying amounts recognised in these annual accounts.

In 2015, impairment analyses did not reveal the need to post impairment losses, except for the shares in Unión Fenosa Gas, S.A. (Note 9).

Gas Natural SDG, S.A. has carried out a sensitivity analysis of the unfavourable variations which, drawing on historical experience, may reasonably affect the above-mentioned sensitive variables used as a basis for the recoverable amount of the CGUs. Specifically, the most relevant sensitivity analyses performed are as follows:

	Increase	Decrease
Discount rate	50 basis points	–
Electricity generated (%)	–	5
Electricity price (%)	–	5
Fuel and gas supply costs (%)	5	–
Operating and maintenance costs (%)	5	–

These sensitivity analyses performed separately for each basic assumption would not affect the conclusions drawn to the effect that the recoverable amount exceeds the carrying amount, except for Unión Fenosa Gas, S.A., the recoverable value of which is equivalent to its carrying amount.

6.4. Financial assets and liabilities

Investments in the equity of group and multi-group companies and associates

These are stated at the lower of cost of acquisition or fair value, if the investments are acquired through a business combination, and the recoverable value. The recoverable value is determined as the larger of fair value minus cost of sale and the current value of the cash flows generated by the investment. If there is no better evidence of recoverable value, recoverable value will be the equity of the investee company adjusted by any tacit capital gains subsisting at the valuation date. The value adjustment, and as the case may be, its reversal, is recorded on the income statement in which it takes place.

In non-cash contributions of a business to a group company, the investment is measured at the carrying amount of the assets and liabilities contributed, as per the consolidated Annual accounts on the transaction date. The consolidated Annual accounts of the largest group or subgroup into which the assets and liabilities are integrated, where the parent is a Spanish company, are used.

In mergers and spin-offs between group companies that involve the group's parent, directly or indirectly, the assets and liabilities acquired are measured at the amount that would be reflected in the group's Consolidated Annual accounts following the transaction. The difference between the cost of the shares handed over and the carrying amount of the assets and liabilities acquired, in the group's Consolidated annual accounts, is recognised under "Reserves" in the balance sheet.

Investments

Purchases and sales of investments are recognised on trade-date, which is the date on which Gas Natural SDG, S.A. commits to purchase or sell the asset, and are classified under the following categories:

a) Loans and receivables

These are non-derivative financial assets, with fixed or determinable pay outs, that are not listed on an active market, and for which there is no plan to trade in the short-term. They include current assets, except for those maturing after twelve months as from the balance sheet date that are classified as non-current assets.

They are initially recorded at their fair value and then at their amortised cost using the effective interest rate method.

A provision is set up for impairment of receivables when there is objective proof that all the outstanding amounts will not be paid. The provision is the difference between the book value of the asset and the present value of the estimated future cash flows discounted at the effective interest rate.

b) Held-to-maturity financial assets

These are assets representing debt with fixed or determinable pay outs and fixed maturity which the Company plans to and can hold until maturity. The valuation criteria for these investments are the same as those for loans and financial receivables.

c) Fair value financial assets through profit or loss

These are assets acquired for short-term sale. Derivatives form part of this category unless they are designated as hedges. These financial assets are stated, both initially and in later valuations, at their fair value, and the changes in their value are taken to the income statement for the year

d) Available-for-sale financial assets

Available-for-sale financial assets are non-derivative debt or equity instruments that are not designated in either category.

They are recognised at fair value. The changes are recorded directly in equity until the asset is sold or impaired, at which time the accumulated gains and losses in equity are taken to the Income statement.

The fair values of quoted investments are based on current bid prices. In the case of shareholdings in unlisted companies, fair value is determined using valuation techniques that include the use of recent transactions between willing and knowledgeable parties, references to other instruments that are substantially the same and the analysis of discounted future cash flows. If none of these techniques can be used to determine fair value, investments are carried at cost less any impairment loss.

Financial assets are written off when the contractual rights to the asset's cash flows have expired or they have been transferred; in the latter case, the risks and rewards of ownership must have been substantially transferred. Financial assets are not written off, and a liability is recognised in the same amount as the payment received, in asset assignments where the risks and rewards of ownership are retained.

Cash and cash equivalents

Cash and cash equivalents include cash at hand, time deposits with financial entities and other short-term investments noted for their great liquidity with an original maturity no longer than three months as from the acquisition date.

Borrowings

Borrowings are initially recognised at their fair value, net of the transaction costs that they may have incurred. Any difference between the amount received and the repayment value is recognised in the income statement during the period of repayment using the effective interest rate method.

Borrowings are classified as current liabilities unless they mature in more than twelve months as from the balance sheet date, or include tacit one-year prorogation clauses that can be exercised by Gas Natural SDG, S.A.

Trade and other payables

Trade and other current payables are financial liabilities that fall due in less than twelve months that are stated at their fair value and do not accrue explicit interest. They are accounted for at their nominal value. Those maturing in more than twelve months are considered non-current payables.

6.5. Financial derivatives and other financial instruments

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the asset being hedged.

For each hedging transaction, Gas Natural SDG, S.A. documents at the inception of the transaction and periodically, the relationship between hedging instruments and hedged items, as well as its risk management objective. Additionally, the aims of risk management and hedging strategies are periodically reviewed.

A hedge is considered to be highly effective when the changes in the fair value or the cash flows of the assets hedged are offset by the change in the fair value or cash flows of the hedging instrument, with an effectiveness ranging from 80% to 125%.

The market value of the different financial instruments is calculated using the following procedures:

- > Derivatives listed on an official market are calculated on the basis of their year-end quotation.
- > Derivatives that are not traded on official markets are calculated on the basis of the discounting of cash flows based on year end market conditions, based on market conditions as at Consolidated balance sheet date or, for some non-financial items, on best estimation on forward curves of said non-financial item.

Fair values obtained in absence of risk are adjusted by the expected impact of the risk of counterparty credit observable in positive valuation scenarios and the impact of own credit risk in observable negative valuation scenarios.

The embedded derivatives in other non-financial instruments are booked separately as derivatives only when their economic characteristics and tacit risks are not closely related to the instruments in which they are embedded and when the whole is not being booked at fair value through profit and loss.

For accounting purposes, the operations are classified as follows:

1. Derivatives eligible for hedge accountings

a) Fair value hedge

Changes in the fair value of derivatives that are designated and qualified as fair value hedges are recognised in the Income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

b) Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recognised in equity. The gain or loss relating to the ineffective portion is recognised immediately in the Income statement.

Amounts accumulated in equity are reclassified to the Income statement in the periods when the hedged item will affect profit or loss.

c) Hedges of net foreign investments

Fair value hedge accounting is applied to the differences arising from the exchange rates on loans in foreign currency for financing foreign investments in group and multi-group companies and associates made in the same functional currency.

2. Derivatives that do not qualify for hedge accounting

Certain derivative instruments do not qualify for hedge accounting. Such derivatives are classified as at fair value through profit or loss, and changes in the fair value of any derivative instruments that do not qualify for hedge accounting are recognised immediately in the Income statement.

3. Energy purchase and sale agreements

During the normal course of its business Gas Natural SDG, S.A. enters into energy purchase and sale agreements which in most cases include “take or pay” clauses, by virtue of which the buyer takes on the obligation to pay the value of the energy contracted independently of whether he receives it or not. These agreements are executed and maintained in order to meet the needs of receipt of physical delivery of energy projected by Gas Natural SDG, S.A. in accordance with the energy purchase and sale estimates made periodically, which are monitored systematically and adjusted as the case may be by physical delivery. Consequently, these are negotiated contracts for “own use”, and, accordingly, lie beyond the standards on valuation of financial instruments.

6.6. Non-current assets held for sale and discontinued activities

Gas Natural SDG, S.A. classifies as held-for-sale assets those assets for which, at the year end, active initiatives have been initiated for their sale, which is estimated to take place within the next twelve months.

These assets are stated at the lower of their carrying value and fair value minus the costs necessary for their sale and are not subject to depreciation, since the date they are classified as non-current assets held for sale.

Additionally, Gas Natural SDG, S.A. treats components (cash-generating units or groups of CGUs) representing a business line or geographic area of operations that is significant and may be analysed separately from the rest, and has been sold or otherwise disposed of, or meets the conditions to be classed as held for sale, as discontinued operations. Entities acquired solely for resale are also classed as discontinued operations.

6.7. Share capital

Share capital is represented by ordinary shares.

Incremental costs directly attributable to the issue of new shares or options, net of taxes, are deducted from equity as a deduction from Reserves or share premium in the case of issues of capital with premiums.

Dividends on ordinary shares are recognised as a deduction from equity in the period they are approved.

Acquisitions of treasury shares are recorded at acquisition cost, deducted from equity until disposal. The gains and losses on disposal of treasury shares are recognised under “Reserves” in the Balance sheet.

6.8. Earnings per share

Basic earnings per share are calculated as a quotient between profit or loss for and the average weighted number of ordinary shares in circulation during this period excluding the average number of treasury stock held by Gas Natural SDG, S.A.

Diluted earnings per share are calculated as a quotient between profit or loss for attributable to the ordinary shareholders adjusted by the effect attributable to the potential ordinary shares having a dilutive effect and the average weighted number of ordinary shares in circulation during this period, adjusted by the average weighted number of ordinary shares that would be issued if all the potential ordinary shares were converted into ordinary shares of the Company. Accordingly, the conversion is considered to take place at the beginning of the period or at the time of issue of the potential ordinary shares, if these have been placed in circulation during the period itself.

6.9. Provisions for employee obligations

a) Post-employment pension obligations and the like

Defined contribution plans

Gas Natural SDG, S.A., together with other group companies, is the promoter of a joint occupational pension plan, which is defined contribution plan for retirement and a defined benefit plan for the so-called risk contingencies, which are assured.

Additionally, there is a defined contribution plan for a group of executives, for which Gas Natural SDG, S.A. undertakes to make certain contributions to an insurance policy. Gas Natural SDG, S.A. guarantees this group a yield of 125% of the CPI of the contributions made to the insurance policy. All the risks have been transferred to the insurance company, since it insures the guarantee indicated above.

The contributions made have been recognised in "Staff costs" in the Income statement.

Defined benefit plans

For certain groups of employees there are commitments for defined benefit schemes in relation to the payment of supplements on retirement, death and disability pensions, in accordance with the benefits agreed by the entity, which have been transferred out of the company in the form of single premium insurance policies under Royal Decree 1588/1999, 15 October, which adopted the Regulations on the instrumentation of pension commitments.

The liability recognised on the Balance sheet in respect of defined benefit pension plans is the present value of the defined benefit obligation at the Balance sheet date less the fair value of plan assets, together with adjustments for unrecognised actuarial gains or losses and past service costs. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension liability.

Actuarial losses and gains arising from changes in actuarial assumptions or from differences between assumptions and reality are recognised entirely in the period in which they arise, directly in equity reserves.

Past service costs are recognised immediately in the Income statement, in "Staff costs".

b) Other post-employment benefit obligations

Gas Natural SDG, S.A. provides for post-employment benefits to their retirees. The entitlement to these benefits is usually conditional on the employee remaining in service up to retirement age and the completion of a minimum service period. The expected costs of these benefits are accrued over the period of employment using an accounting methodology similar to that used for defined benefit pension plans. Actuarial gains and losses arising from changes in actuarial assumptions, are charged or credited to income in "Reserves".

c) Termination benefits

Termination benefits are payable when employment is terminated before the normal retirement date, or when an employee accepts voluntary redundancy in exchange for these benefits. Gas Natural SDG, S.A. recognises a liability when current employees are laid off based on a detailed formal plan that cannot be withdrawn; or providing termination benefits. In the event that mutual agreement is required, the provision is only recorded in those situations in which Gas Natural SDG, S.A. has decided to give its consent to voluntary redundancies once they have been requested by the employees.

6.10 Provisions

Provisions are recognised when Gas Natural SDG, S.A. has a present legal or implicit obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

Provisions are measured at the present value of the Company's best estimate of expenditure required to settle the present obligation at the Balance sheet date.

When it is expected that part of the disbursement needed to settle the provision is paid by a third party, the payment is recognised as a separate asset, provided that its receipt is practically assured.

In the contracts in which the obligations borne include inevitable costs greater than the economic profit expected to be received from them, the expenses and respective provisions are recognised in the amount of the current value of the existing difference.

6.11. Leases

a) Finance leases

Leases of property, plant and equipment where the lessee substantially bears all the risks and rewards of ownership are classified as finance leases.

These leases are capitalised at the lease's inception at the lower of the fair value of the leased property and the present value of the lease payments, including the purchase option. Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The corresponding rental obligations, net of finance charges, are included in other long-term liabilities except for those falling due more than twelve months. The interest element of the finance cost is charged to the income statement over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The property, plant and equipment acquired under finance leases are depreciated over the asset's useful life.

b) Operating leases

Leases in which substantially all the risks and rewards of ownership are retained by the lessor are classified as operating leases.

Operating lease payments are charged to the income statement on a straight-line basis over the lease term.

6.12 Income tax

Corporate income tax expense includes the deferred tax expense and the current tax expense, which is the amount payable (or refundable) on the tax profit for the year.

Deferred taxes are recorded by comparing the temporary differences that arise between the taxable income on assets and liabilities and their respective accounting figures in the Annual accounts used the tax rates that are expected to be in force when the assets and liabilities are realized.

Deferred tax arising from direct charges or credits to equity accounts are also charged or credited to equity.

Deferred tax assets and tax credits are recognised only to the extent that it is probable that future taxable income will be available against which to offset temporary differences and apply tax credits.

When tax rates change, deferred tax assets and liabilities are reestimated. These amounts are charged or credited to losses or profits, or to reserves, depending on the account to which the original amount was charged or credited.

6.13. Revenue recognition and payments for regulated activities

a) General

Sales are recognised when products are delivered to the customer and have been accepted by the customer, even if they have not been invoiced, or if applicable, services are rendered, and it is probable that the economic benefits associated with the transaction will flow to the entity. Net turnover for the year includes the estimate of the energy supplied that has not yet been invoiced

The expenses are recognised on an accruals basis, immediately in the case of disbursements that are not going to generate future economic profits or when the requirements for recording them as assets are not met.

Sales are stated net of tax and discounts.

b) Income from the gas business

Note 2.1. describes the basic aspects of the applicable gas sector regulations.

c) Income from electricity activities

Note 2.2. describes the basic aspects of the applicable electricity sector regulations.

From 2006 to 2013, given that the income collected by the companies in the Spanish electricity industry has not been sufficient to remunerate the different activities and costs of the system, The companies themselves, including the Company, were forced to finance this income deficit until its definite funding. Following successive auctions and assignments of the outstanding debt claims, on 15 December 2014 the electricity system deficit securitisation process was completed.

Following the publication of Electricity Sector Law 24/2013, December 26 (Note 2.2), temporary mismatches between electricity system revenues and costs are funded by the companies subject to the settlement system, including Gas Natural Fenosa, generating the right to recover the relevant amount over the following five years, including interest at a market rate. Consequently, the financing for the electricity system revenue deficit is recognised as a financial asset since, on the basis of this regulation, Gas Natural Fenosa is entitled to a reimbursement and there are no future contingent factors. From 2014 to 2016, following the reforms undertaken, there has been no revenue shortfall in the sector, according to the provisional settlements of these years.

d) Other income and expenses

In accounting for revenues from the service provision agreements is used the percentage realisation method in which, when the income can be reliably estimated, it is recorded on the basis of the degree of progress in the completion of the contract at the year end, calculated as a proportion of the costs incurred at that date of the estimated costs required to fulfil the contract.

If the income from the contract cannot be estimated reliably, the costs (and respective income) are recorded in the period in which they are incurred, provided that the former can be recovered. The contract margin is not recorded until there is certainty of its materialisation, based on cost and income planning.

In the event that the total costs exceed the contract revenues, this loss is recognised immediately in the Income statement for the year.

Interest incomes and expenses are recognised using the effective interest method.

Dividend income is recognised when the right to collect the dividend is established.

The holding of shares in Group companies and associates is deemed to be the Company's most relevant ordinary activity from which periodic revenue is obtained. In accordance with the stance adopted by the Spanish Institute of Accounting and Auditing ("ICAC") in connection with the calculation of net revenue in holding companies (Reply number 2 in ICAC Official Gazette number 79), dividends from Group companies and associates, and interest received on loans granted to Group companies and associates, are recognised as "Revenue". Additionally, the item "Impairment and results on disposal of equity instruments of Group companies and associates" is included in "Operating profit/(loss)".

6.14. Foreign currency transactions

Foreign currency transactions are translated to euro using the exchange rates in force at the transaction dates. Gains and losses resulting from the settlement of these transactions and translation at the year-end exchange rates of monetary assets and liabilities denominated in foreign currency are recognised in the income statement.

6.15. Transactions between related parties

In general, transactions between related parties are recorded initially at their fair value. If the agreed price differs from its fair value, the difference is recorded taking into account the economic reality of the operation. The later valuation is made in accordance with the provisions of the respective legislation.

Notwithstanding the above, in merger, de-merger or non-cash contribution operations of a business, the assets that make up the acquired business are stated at the amount corresponding to the same once the operation takes place in the Consolidated Annual accounts of Gas Natural Fenosa.

In these cases, the difference that could arise between the net value of the assets and liabilities of the acquired company, adjusted by the balance of the groupings of grants, donations and bequests received, or any value adjustments or capital or share premiums, as the case may be, issued by the merging company, is recorded under "Reserves" in the balance sheet.

6.16. Business combinations

Business combinations are recorded using the acquisition method. The cost of an acquisition is calculated using the fair value of the assets given, the equity instruments issued and the liabilities incurred or borne on the transaction date plus the costs directly attributable to the acquisition. The valuation process required in order to use the acquisition method is completed within the period of one year as from the acquisition date.

The identifiable assets acquired and the liabilities or contingent liabilities incurred or borne as a result of the transaction, are initially stated at their fair value at the date of acquisition, provided that this can be reliably measured.

The surplus cost of the acquisition in relation to the fair value of the shareholding of Gas Natural SDG, S.A. in the net identifiable assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets acquired, the difference is recognised directly in the Income statement.

6.17. Cash flow statement

The cash flow statements has been prepared using the indirect method and contain the use of the following expressions and their respective meanings:

- a) Operating activities: activities that constitute ordinary Gas Natural SDG, S.A. revenues, as well as other activities that cannot be qualified as investment or financing.
- b) Investing activities: acquisition, sale or disposal band other means of assets in the long-term and other investments not included in cash and cash equivalents.
- c) Financing activities: activities that generate changes in the size and composition of equity and liabilities that do not form part of operating activities.

6.18. Significant accounting estimates and judgments

The preparation of Annual accounts requires the formulation of estimates and judgments. The valuation standards that require a large number of estimates are set out below:

a) Intangible assets and Property, plant and equipment (Notes 6.1 and 6.2)

The determination of useful life of intangible assets and property, plant and equipment requires estimates of their degree of use, as well as expected technological evolution. The assumptions regarding the degree of use, technological framework and future development involve a significant degree of judgement, insofar as the timing and nature of future events are difficult to foresee.

b) Impairment of assets (Note 6.3)

The estimated recoverable value of the CGU applied to the impairment tests has been determined using the discounted cash flows based on the projections approved by Gas Natural SDG, S.A., which have historically been substantially met.

c) Derivatives or other financial instruments (Note 6.5)

The fair value of financial instruments traded in active markets is based on quoted market prices at the Balance sheet date. The quoted market price used for financial assets is the current bid price.

The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques. Gas Natural SDG, S.A. uses a variety of methods and makes assumptions that are based on market conditions existing at each balance sheet date. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments. The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows. The fair value of forward foreign exchange contracts is determined using quoted forward exchange rates at the Balance sheet date. The fair value of commodity derivatives is calculated by using forward prices curves. The recoverable value of the investments in the equity of group and multi-group companies and associates is determined as the greater of their fair value less costs of sale and the current value of the cash flows from the investment.

The carrying value less impairment provision of trade receivables and payables are assumed to approximate their fair values. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to Gas Natural SDG, S.A. for similar financial instruments.

d) Provisions for employee benefits (Note 6.9)

A number of assumptions must be used to calculate pension costs, other costs of post-retirement benefits and other post-retirement liabilities. Gas Natural SDG, S.A. estimates at the year end the provision required to cover pension commitments and similar obligations, based on advice from independent actuaries. The changes affecting such assumptions may result in the recording of different amounts and liabilities. The most significant assumptions for the measurement of pension or post-retirement benefit liabilities are energy consumption by beneficiaries during retirement, retirement age, inflation and the discount rate employed. Social security coverage assumptions are also essential to determine other post-retirement benefits. Future changes to these assumptions will have an impact on future pension costs and liabilities.

e) Provisions (Note 6.10)

Gas Natural SDG, S.A. makes an estimate of the amounts to be settled in the future, including amounts relating to contractual obligations, outstanding litigation, restoration of land or other liabilities. These estimates are subject to the interpretation of current events and circumstances, projections of future events and estimates of their financial effects.

f) Income tax (Note 6.12)

The calculation of the income tax expense requires interpretations of tax legislation in the jurisdictions in which Gas Natural SDG, S.A. operates. The determination of expected outcomes of outstanding disputes and litigation requires the preparation of significant estimates and judgment. Gas Natural SDG, S.A. evaluates the recoverability of the deferred income tax assets based on estimates of future taxable income. The recoverability of the deferred tax assets depends ultimately on the capacity of Gas Natural SDG, S.A. to generate sufficient tax profits during the periods in which these deferred taxes are deductible. Deferred tax liabilities are recognised based on estimates of the net assets that will not be tax deductible in the future.

Note 7. Intangible assets

Set out below there is an analysis of movements in intangible assets:

	Computer software	Other intangible assets	Subtotal	Goodwill	Total
Cost	2	–	2	1,062	1,064
Accumulated amortisation	(2)	–	(2)	(462)	(464)
Net carrying value at a 01/01/2015	–	–	–	600	600
Amortisation charge	–	–	–	(81)	(81)
Demerger scope (Note 5)	–	–	–	(247)	(247)
Net carrying value at 31/12/2015	–	–	–	272	272
Cost	2	–	2	815	817
Accumulated amortisation	(2)	–	(2)	(543)	(545)
Net carrying value at a 01/01/2016	–	–	–	272	272
Investment	4	1	5	–	5
Amortisation charge	–	–	–	(82)	(82)
Net carrying value at 31/12/2016	4	1	5	190	195
Cost	6	1	7	815	822
Accumulated amortisation	(2)	–	(2)	(625)	(627)
Net carrying value at 31/12/2016	4	1	5	190	195

Goodwill derives from the vertical merger of Unión Fenosa, S.A. completed in 2009 and is attributable to the benefits and synergies arising from the integration with the Gas Natural Fenosa Group. In 2016, following changes in accounting legislation, this goodwill has started to be amortised, adjusting the comparative information (Note 4).

Intangible assets include, at 31 December 2016, fully amortised assets still in use totalling Euros 2 million (Euros 2 million at 31 December 2015).

Note 8. Property, plant and equipment

Set out below is an analysis showing movements in Property, plant and equipment during 2016 and 2015:

	Land and buildings	Plant and other property, plant and equipment	Property, plant and equipment Under construction	Total
Cost	237	2.316	5	2,558
Accumulated depreciation	(76)	(1,433)	–	(1,509)
Net carrying value at a 01/01/2015	161	883	5	1.049
Investment	15	2	–	17
Depreciation charge	(9)	(2)	–	(11)
<i>Demerger scope (Note 5)</i>	–	(871)	(5)	(876)
Net carrying value at 31/12/2015	167	12	–	179
Cost	248	34	–	282
Accumulated depreciation	(81)	(22)	–	(103)
Net carrying value at a 01/01/2016	167	12	–	179
Investment	12	3	–	15
Divestments	(23)	–	–	(23)
Depreciation charge	(10)	(2)	–	(12)
Reclassifications and transfers	(6)	–	–	(6)
Net carrying value at 31/12/2016	140	13	–	153
Cost	201	33	–	234
Accumulated depreciation	(61)	(20)	–	(81)
Net carrying value at 31/12/2016	140	13	–	153

At 1 January 2015, as indicated in Note 5, “Plant and other PPE” basically included nuclear power plants, which were transferred to Gas Natural Fenosa Generación, S.L.U. in the demerger operation.

In December 2016, Gas Natural SDG, S.A., General de Edificios y Solares, S.L. and Unión Fenosa Distribución S.A., 100% companies of Gas Natural Fenosa completed the sale of four properties in Madrid (Avenida San Luis 77, Antonio Lopez 193, A Canto 11-13 and Avenida América 38). For Gas Natural SDG, S.A., it has sold the Avenida América 38 building, for Euros 64 million and recognised a gain before income tax of Euros 36 million. Additionally, the company has signed 10-year operating lease contracts, without a purchase option, with the buyers of each of those properties, which are renewable, except for Avenida América 38, for five years more (Note 29). At the transaction date, the remaining useful life of all the sold properties was far higher than the maximum lease term.

In 2016 there have been disposals of fully-depreciated assets totalling Euros 7 million (Euros 14 million at 31 December 2015).

Property, plant and equipment include fully-depreciated assets still in use totalling Euros 16 million at 31 December 2016 (Euros 20 million in 2015).

It is Gas Natural SDG, S.A.'s policy to take out insurance where deemed necessary to cover risks that could affect its property, plant and equipment.

At 31 December 2016 and 31 December 2015, Gas Natural SDG, S.A. has no investment commitments.

Note 9. Investments in group companies and associates

A breakdown of the investments in group companies and associates is as follows:

	At 31/12/16	At 31/12/15
Equity instruments	13,688	14,613
Loans	15,755	14,695
Non-current	29,443	29,308
Loans	816	727
Other financial assets	67	3
Current	883	730
Total	30,326	30,038

Movements during the year in non-current investments in group companies and associates are as follows:

	Shareholdings in group companies	Loans to group companies	Shareholdings in associates	Total
Balance at 01/01/2015	13,833	13,935	11	27,779
Additions	912	789	–	1,701
Divestments	(399)	(713)	–	(1,112)
Demerger scope (<i>Note 5</i>)	362	–	–	362
Reclassification	–	627	–	627
Charge/reversal provisions	(106)	–	–	(106)
Net exchange gains / losses	–	57	–	57
Balance at 31/12/2015	14,602	14,695	11	29,308
Additions	40	1,584	–	1,624
Divestments	(759)	(259)	–	(1,018)
Reclassification	–	(266)	–	(266)
Charge/reversal provisions	(206)	–	–	(206)
Net exchange gains / losses	–	1	–	1
Balance at 31/12/2016	13,677	15,755	11	29,443

Year 2016

The most significant movements in the item “Shareholdings in Group companies and associates” in 2016 relate to:

- Capital contribution to offset losses posted by the company Gas Natural Exploración, S.L. in the amount of Euros 30 million.
- Capital contribution to offset losses in Gas Natural S.U.R. SDG, S.A. in the amount of Euros 10 million.
- Capital reduction through the reimbursement of contributions from Clover Financial and Treasury Services, Ltd in the amount of USD 825 million. The reduction in the shareholding has generated a Euros 33 million profit due to the effect of the exchange rate.
- Sale of the 50% shareholding in Nueva Generadora del Sur, S.A. to Gas Natural Generación, S.L.U. at its carrying amount of Euros 1 million.
- Capital reduction in Natural Re, S.A. in the amount of Euros 4 million.
- The distributions of reserves by Global Power Generation, S.A.U. and Gasifica, S.A. amounting to Euros 64 million and Euros 1 million, respectively, has been recorded as a decrease in the carrying value of shareholdings.
- During the year Gasifica, S.A. was dissolved, leading to a reduction in the investment of Euros 3 million and a loss of Euros 2 million.

Year 2015

The most significant movements in the item “Shareholdings in Group companies and associates” in 2015 related to:

- Demerger of the nuclear power generation business, which was transferred in bloc to the company Gas Natural Fenosa Generación, S.L.U. in exchange for shares in the beneficiary company totalling Euros 362 million (Note 5).
- Spin-off of Nueva Generadora del Sur, S.A. (owned 50% by Gas Natural SDG, S.A. and 50% by Compañía Española de Petróleos, S.A. (CEPSA)) to Genroque, S.L. and Puente Mayorga Generación, S.L. in order to separate the two 400 MW units that formed the combined cycle plant operated by Nueva Generadora del Sur, S.A.

Following the spin-off, the 50% stake in Puente Mayorga Generación, S.L. was sold to CEPSA and a 50% stake in Genroque, S.L. was purchased from CEPSA, so that each of Nueva Generadora del Sur, S.A.’s shareholders operated and managed each unit separately.

- Sale of the shareholding in the company Genroque, S.L.U. to Gas Natural Generación, S.L.U. for its carrying amount of Euros 200 million. On 30 December 2015, Gas Natural Fenosa Generación, S.L.U.'s Extraordinary General Meeting approved the vertical merger of Genroque, S.L.U. in order to fully integrate the unit into Gas Natural Fenosa's generation facilities.
- Capital reduction and reimbursement of contributions in Clover Financial and Treasury Services, Ltd. in the amount of Euros 175 million.
- Subscription for a capital increase in Nueva Generadora del Sur, S.A. in the amount of Euros 61 million.
- Gas Natural Fenosa and Kuwait Investment Authority (KIA) entered into an agreement for increase capital by USD 550 million, fully subscribed by KIA. Following this capital increase, KIA holds a 25% stake in the international generation subsidiary Global Power Generation, S.A.

Additionally, Gas Natural SDG, S.A. fully subscribed a capital increase of USD 713 million (Euros 640 million) in Global Power Generation, S.A.

- Subscription for a capital increase in Natural Re, S.A. in the amount of Euros 4 million.
- Capital contribution to offset losses in Gas Natural S.U.R. SDG, S.A. in the amount of Euros 12 million.

The cumulative provision for the impairment of shareholdings in Group companies and associates totals Euros 1,487 million at 31 December 2016 (Euros 1,281 million at 2015), relating basically to the following companies:

- Gas Natural Exploración, S.L.: the recoverable amount has been calculated on the basis of its equity. In 2016 an impairment loss of Euros 21 million was posted. The provision at 31 December 2016 totals Euros 213 million (Euros 192 million at 31 December 2015).
- Unión Fenosa Gas, S.A.: At 31 December 2015 the fair value of Unión Fenosa Gas, S.A. was similar to its carrying value. Euros 86 million was provided for basically in relation to the change in the contribution to the consolidated figure of the shareholding in said company.

In the previous years an impairment of the interest in Unión Fenosa Gas, S.A. amounting to Euros 1,002 million had been recognised basically due to the substantial failure of the Egyptian supplier to comply with the agreements to re-establish supplies of gas to the Damietta (Egypt) liquefaction plant and the variation of the contribution of this invested company to the consolidated group.

In 2016 an impairment of Euros 174 million was recognised with respect to the interest in Unión Fenosa Gas, S.A. due to the need to update the assumptions concerning the supply cost in view of the forecast evolution of the energy scenario for Unión Fenosa Gas and the change in the contribution to the consolidated figures. In Note 6.3, the assumptions corresponding to the discount and growth rate are detailed. The other assumptions have not been altered. The provision at 31 December 2016 totals Euros 1,262 million (Euros 1,088 million at 31 December 2015).

Financial income for dividends received from investments in equity instruments of group companies and associates during the years 2016 and 2015, correspond to the following companies:

	2016	2015
Holding Negocios Regulados Gas Natural, S.A.	354	336
Gas Natural Comercializadora, S.A.	326	133
Gas Natural Aprovisionamientos SDG, S.A.	242	58
Unión Fenosa Distribución, S.A.	241	458
Sagane, S.A.	177	209
Gas Natural Servicios SDG, S.A.	62	80
Global Power Generation, S.A.U.	58	–
Clover Financial And Treasury Services, Ltd.	45	66
Unión Fenosa Preferentes, S.A.	29	42
Gas Natural Almacenamientos Andalucía, S.A.	8	–
Gas Natural Informática, S.A.	5	4
Gas Natural Fenosa Finance, B.V.	3	1
Gas Natural Fenosa Engineering, S.L.U.	3	–
General de Edificios y Solares, S.L.	2	5
Gasifica, S.A.	2	–
Gas Natural Capital Markets, S.A.	2	15
Unión Fenosa Minería, S.A.	1	1
Gas Natural Distribución Latinoamérica, S.A.	–	121
Unión Fenosa Gas, S.A.	–	13
Total	1,560	1,542

Dividends pending collection at 31 December 2016 amounted to Euros 64 million, recorded under “Other current financial assets”.

The breakdown of shareholdings in group companies is set out below:

Company	Registered Office	Activity	Net carrying value 2016	Net carrying value 2015	Data at 31 december 2016							
					% shareholding			Net equity				
					Direct	Indirect	Total	Capital	Reserves ¹	Profit/(loss)	Interim dividend	Others ²
Gas Natural Aprovisionamientos SDG, S.A.	Spain	Gas commercialisation	18	18	100.0	-	100.0	1	19	32	-	14
Gas Natural Fenosa LNG, S.L.	Spain	Gas commercialisation	2	2	100.0	-	100.0	2	-	-	-	-
Sagane, S.A.	Spain	Gas commercialisation	42	42	100.0	-	100.0	95	22	145	-	5
Unión Fenosa Gas, S.A.	Spain	Gas commercialisation	1,179	1,353	50.0	-	50.0	33	655	15	-	52
Gas Natural Comercializadora, S.A.	Spain	Gas and electricity commercialisation	121	121	100.0	-	100.0	3	102	259	(125)	19
Gas Natural S.U.R. SDG, S.A.	Spain	Gas and electricity commercialisation	44	34	100.0	-	100.0	2	15	(14)	-	1
Gas Natural Servicios SDG, S.A.	Spain	Gas and electricity commercialisation	106	106	100.0	-	100.0	3	51	169	-	5
Unión Fenosa Distribución, S.A.	Spain	Electricity distribution	1,630	1,630	100.0	-	100.0	833	437	167	(159)	322
Gas Natural Fenosa Generación Nuclear, S.L.	Spain	Electricity generation	-	-	100.0	-	100.0	-	-	-	-	-
Gas Natural Fenosa Generación, S.L.U.	Spain	Electricity generation	3,897	3,897	100.0	-	100.0	552	1,652	(375)	-	4
Gas Natural Fenosa Renovables, S.L.U.	Spain	Electricity generation	397	397	100.0	-	100.0	90	105	9	-	-
Global Power Generation, S.A.U.	Spain	Electricity generation	1,556	1,608	75.0	-	75.0	20	1,877	(2)	-	143
Nueva Generadora del Sur, S.A.	Spain	Electricity generation	-	1	50.0	-	50.0	-	-	-	-	-
P.H. La Perla, S.A.	Costa Rica	Electricity generation	-	-	100.0	-	100.0	-	-	-	-	-
Toledo PV A.I.E.	Spain	Electricity generation	-	-	33.3	-	33.3	-	1	1	-	-
Gas Natural Almacenamientos Andalucía, S.A.	Spain	Gas infrastructures	8	8	100.0	-	100.0	-	9	1	-	-
Gas Natural Exploración, S.L.	Spain	Gas infrastructures	9	-	100.0	-	100.0	8	13	(1)	-	(11)
Petroleum Oil & Gas España, S.A.	Spain	Gas infrastructures	41	41	32.3	67.7	100.0	4	29	(8)	-	2
Natural Re, S.A.	Luxembourg	Insurance	9	9	100.0	-	100.0	4	57	8	-	-

Company	Registered Office	Activity	Net carrying value 2016	Net carrying value 2015	Data at 31 december 2016							
					% shareholding			Net equity				
					Direct	Indirect	Total	Capital	Reserves ¹	Profit/(loss)	Interim dividend	Others ²
Arte Contemporáneo y Energía, A.I.E.	Spain	Services	-	-	75.0	25.0	100.0	-	-	-	-	-
Compañía Española de Industrias Electroquímicas, S.A.	Spain	Services	4	4	98.5	-	98.5	3	12	1	-	-
General de Edificios y Solares, S.L.	Spain	Services	63	63	100.0	-	100.0	34	35	19	-	-
Clover Financial and Treasury Services, Ltd.	Ireland	Financial services	680	1,382	100.0	-	100.0	-	422	41	-	289
Gas Natural Capital Markets, S.A.	Spain	Financial services	-	-	100.0	-	100.0	-	-	8	-	-
Gas Natural Fenosa Finance, B.V.	Netherlands	Financial services	7	7	100.0	-	100.0	-	2	1	-	(1)
Unión Fenosa Financiación, S.A.	Spain	Financial services	11	11	100.0	-	100.0	1	-	-	-	-
Unión Fenosa Preferentes, S.A.	Spain	Financial services	-	-	100.0	-	100.0	-	1	2	(2)	110
Gas Natural Informática, S.A.	Spain	IT services	20	20	100.0	-	100.0	20	9	(1)	-	-
Gas Natural Fenosa Engineering, S.L.	Spain	Engineering services	24	24	100.0	-	100.0	-	19	1	-	-
Holding Negocios Regulados Gas Natural, S.A.	Spain	Holding company	1,981	1,981	100.0	-	100.0	300	1,682	341	(325)	-
Gas Natural Distribución Latinoamérica, S.A.	Spain	Holding company	558	558	100.0	-	100.0	402	221	91	-	-
Gasifica, S.A.	Spain	Holding company	-	3	10.0	45.0	55.0	-	-	-	-	-
La Energía, S.A.	Spain	Holding company	11	11	100.0	-	100.0	11	5	-	-	-
La Propagadora del Gas, S.A.	Spain	Holding company	10	10	100.0	-	100.0	10	1	-	-	-
Gas Natural Fenosa Internacional, S.A.	Spain	Holding company	944	945	100.0	-	100.0	250	464	(116)	-	140
Unión Fenosa Minería, S.A.	Spain	Holding company	305	316	100.0	-	100.0	11	169	-	-	-
Total			13,677	14,602								

Appendix I to Gas Natural Fenosa's consolidated annual accounts provides a breakdown of other indirect shareholdings. The Capital, Reserves, Profit/(loss) and the rest of the Net equity information is shown at a societal level.

¹ Includes the share premium, reserves, prior-year losses and retained earnings.

² Includes measurement adjustments, other equity instruments and grants, donations and bequests.

The non-current loans to group companies which at 31 December 2016 total Euros 15,755 million mature in 2018 (at 31 December 2015, Euros 14,695 million maturing in 2017).

Set out below are movements during 2016 and 2015 in loans and other current financial assets:

	Loans to group companies	Other financial assets	Total
Balance at 01/01/2015	1,079	3	1,082
Additions	1,282	–	1,282
Divestments	(448)	–	(448)
Reclassifications	(1,186)	–	(1,186)
Balance at 31/12/2015	727	3	730
Additions	424	64	488
Divestments	(673)	–	(673)
Reclassifications	338	–	338
Balance at 31/12/2016	816	67	883

There are no significant differences between carrying values and fair values in the balances under Loans to group companies and other receivables.

The item “Loans to Group companies” relates to the cash pooling balances with investees, as manager of the Group centralised cash. It also includes accrued unmatured interest of Euros 32 million (Euros 31 million in 2015).

At 31 December 2016, loans to Group companies and associates have borne interest at a rate of 2.54% (2.89% in 2015) in the case of non-current amounts, and 1% (1.03% in 2015) in the case of current amounts.

Note 10. Investments

The breakdown of investments by category is as follows:

A 31 December 2016	Available for sale financial assets	Loans and receivables	Assets at fair value through P&L	Hedging derivatives	Total
Equity instruments	5	–	–	–	5
Derivatives (<i>Note 16</i>)	–	–	31	28	59
Other financial assets	–	10	–	–	10
Non-current investments	5	10	31	28	74
Other financial assets	–	27	–	–	27
Current investments	–	27	–	–	27
Total	5	37	31	28	101

At 31 December 2015	Available for sale financial assets	Loans and receivables	Assets at fair value through P&L	Hedging derivatives	Total
Equity instruments	5	–	–	–	5
Derivatives (<i>Note 17</i>)	–	–	1	–	1
Other financial assets	–	9	–	–	9
Non-current investments	5	9	1	–	15
Other financial assets	–	63	–	–	63
Current investments	–	63	–	–	63
Total	5	72	1	–	78

Available-for-sale financial assets

The main variations in available-for-sale financial assets are as follows:

	2016	2015
At 1 January	5	7
Demerger scope (<i>Note 5</i>)	–	(2)
At 31 December	5	5

All available-for-sale financial assets relate to unlisted shareholdings at 31 December 2016 and 31 December 2015.

Loans and receivables

The breakdown of Loans and other receivables is as follows:

	A 31/12/16	A 31/12/15
Loans to companies	2	2
Deposits and guarantee deposits	8	7
Non-current	10	9
Deposits and guarantee deposits	27	63
Current	27	63
Total	37	72

Note 11. Trade and other receivables

The breakdown of this account is as follows:

	At 31/12/16	At 31/12/15
Trade receivables	169	116
Trade receivables, group companies and associates	368	400
Sundry receivables	77	11
Provision	(24)	(21)
Derivatives (<i>Note 16</i>)	76	181
Current income tax asset	–	10
Public Administration	4	4
Total	670	701

In general, amounts billed pending collection do not bear interest, being the average maturity period less than 19 days.

Movements in the bad debt provision are as follows:

	2016	2015
At 1 January	(21)	(13)
<i>Net charge for the year (Note 23)</i>	(5)	(8)
Other	2	–
At 31 December	(24)	(21)

Note 12. Cash and cash equivalents

Cash and cash equivalents include:

	At 31/12/16	At 31/12/15
<i>Cash at banks and in hand</i>	502	1,089
Other cash equivalents	–	155
Total	502	1,244

Investments in "Other Cash equivalents" in 2015 matured in less than three months at a weighted effective interest rate of 0.41%.

Note 13. Net equity

The main items of Net equity are as follows:

Share capital and share premium

The variations during the years 2016 and 2015 in the number of shares and share capital and share premium accounts have been as follows:

	Number of shares	Share capital	Share premium	Total
At 1 January 2015	1,000,689,341	1,001	3,808	4,809
Changes	–	–	–	–
A 31 December 2015	1,000,689,341	1,001	3,808	4,809
Changes	–	–	–	–
At 31 December 2016	1,000,689,341	1,001	3,808	4,809

All issued shares are fully paid up and carry equal voting and dividend rights.

The Spanish Companies Act specifically allows the use of the “Share premium balance” to increase capital and imposes no specific restrictions on its use.

The most representative holdings in the share capital of Gas Natural SDG, S.A. at 31 December 2016 and 31 December 2015, in accordance with the public information available or the communication issued by the Company itself, are as follows:

	Interest in share capital %	
	2016	2015
Fundación Bancaria Caixa d’Estalvis i Pensions de Barcelona, “la Caixa” ¹	24.4	34.4
Repsol, S.A.	20.1	30.0
Global Infrastructure Partners III ²	20.1	–
Sonatrach	4.0	4.0

¹Through Criteria Caixa, S.A.U. and Caixabank, S.A. In 2015 additionally through Vida Caixa, S.A. de Seguros y Reaseguros.

²Global Infrastructure Partners III, whose investment manager is Global Infrastructure Management LLC, owns its stake indirectly through GIP III Canary 1, S.à.r.l.

On 21 September 2016 the shareholders of Gas Natural Fenosa, Criteria Caixa, S.A.U. (la Caixa) and Repsol, S.A. (Repsol) reported the sale to GIP III Canary 1, S.à.r.l. (GIP) of shares representing 20% (10% Criteria and 10% Repsol) of the capital of Gas Natural SDG, S.A. in accordance with the sale and purchase agreement concluded on 12 September 2016. As a result of this sale, the agreement between “la Caixa” and Repsol concerning Gas Natural of 11 January 2000, amended on 16 May 2002, 16 December 2002 and 20 June 2003, has been terminated and the composition of the Board of Directors and Board committees of Gas Natural Fenosa has changed; in addition, the Regulations of its Board of Directors envisages a majority of two thirds of Board members for the approval of certain reserved matters.

All the shares of Gas Natural SDG, S.A. are traded on the four official Spanish Stock Exchanges and the “Mercado continuo” and form part of Spain’s Ibex 35 stock index.

The share price at 31 December 2016 of Gas Natural SDG, S.A. was Euros 17.91 (Euros 18.82 at 31 December 2015).

Reserves

Reserves include the following:

	2016	2015
Legal reserve	200	200
Statutory reserve	100	100
RD 7/96 revaluation reserve	225	225
Goodwill reserve	496	496
Voluntary reserves	6,603	6,580
Other reserves	274	272
	7,898	7,873

Legal reserve

Appropriations to the legal reserve are made in compliance with the Spanish Capital Companies Act, which stipulates that 10% of the profits must be transferred to this reserve until it represents at least 20% of share capital. The legal reserve can be used to increase capital in the part that exceeds 10% of the capital increased.

Except for the use mentioned above, and as long as it does not exceed 20% of share capital, the legal reserve can only be used to offset losses in the event of no other reserves being available.

Statutory reserve

Under the articles of association of Gas Natural SDG, S.A., 2% of net profit for the year must be allocated to the statutory reserves until it reaches at least 10% of share capital.

Revaluation reserve

The revaluation reserve can be used to offset accounting losses, increase share capital, or can be allocated to freely distributable reserves, provided that the monetary gain has been realised. The part of the gain that will be considered realised is the part relating to the amortisation recorded or when the revaluated assets have been transferred or written off the books of account.

Goodwill reserve

Law 22/2015 on Auditing has eliminated the requirement to record annually the restricted reserve for at least 5% of the goodwill figuring under assets on the balance sheet, stipulating that in periods starting as from 1 January 2016, the goodwill reserve is to be reclassified to voluntary reserves and will be available in the amount that exceeds the goodwill recognised under assets on the balance sheet.

The amortisation reserve at 1 January 2015 has been used in the calculation of accumulated goodwill amortisation at that date (Note 4).

Voluntary and other reserves

It relates basically to voluntary reserves for undistributed profits, also including the effects of the measurement of shareholdings in group companies as a result of transactions between group companies recognised in the same amounts stated in Gas Natural Fenosa's Consolidated annual accounts.

Treasury shares

Movements during 2016 and 2015 involving the treasury shares of Gas Natural SDG, S.A. are as follows:

	Number of shares	In million euro	% Capital
At 1 January 2015	–	–	–
Acquisitions	2,899,180	58	0.3
Disposals	(2,899,180)	(58)	(0.3)
At 31 December 2015	–	–	–
Acquisitions	3,049,189	53	0.3
Disposals	(2,298,644)	(40)	(0.2)
At 31 December 2016	750,545	13	0.1

On 14 May 2015, the shareholders in General Meeting authorised the Board of Directors to purchase, within five years, in one or more operations, a maximum of 10% of share capital or the maximum figure applicable under legislation prevailing at the time of acquisition. The relevant Company shares must be fully paid in and the nominal value of the shares directly or indirectly acquired, added to those already held by the Company and its subsidiaries, may not exceed 10% of share capital or any other limit established by law.

The minimum and maximum acquisition price will be the share price on the continuous market of the Spanish stock exchanges, within an upper or lower fluctuation of 5%.

In 2016, gains made on transactions involving treasury shares by Gas Natural Fenosa has been Euros 0.4 million, which was recorded in "Other reserves" (Euros 2 million, in 2015).

Earnings per share

Basic earnings per share are calculated by dividing profit by the weighted average number of ordinary shares in issue during the year.

	At 31/12/16	At 31/12/15
Profit for the year	1,067	1,024
Weighted average number of ordinary shares in issue	1,001,468,342	1,001,689,341
Earnings per share (in Euros):		
Basic	1.07	1.02
Diluted	1.07	1.02

The weighted average number of ordinary shares in issue used to calculate the Earnings per share of 2016 is as follows:

	2016
Weighted average number of ordinary shares	1,001,689,341
Weighted average number of treasury shares	(220,999)
Weighted average number of ordinary shares in issue	1,001,468,342

The Company has no financial instruments that could dilute the earnings per share.

Dividends

Set out below is a breakdown of the payments of dividends made in 2016 and 2015:

	2016			2015		
	% of Nominal	Euros per share	Amount	% of Nominal	Euros per share	Amount
Ordinary shares	133	1,33	1.331	91	0,91	909
Other shares (without voting rights, redeemable, etc.)	-	-	-	-	-	-
Total dividends paid	133	1,33	1.331	91	0,91	909
a) Dividends charged to income statement	133	1,33	1.331	91	0,91	909
b) Dividends charged to reserves or share premium account	-	-	-	-	-	-
c) Dividends-in-kind	-	-	-	-	-	-

Year 2016

Includes the payment of an interim dividend of Euros 0.4078 per share out of 2015 profits, for a total amount of Euros 408 million, agreed on 30 October 2015 and paid on 8 January 2016.

The proposal for the distribution of 2015 profits approved by the Annual General Meeting held on 4 May 2016 included the payment of a supplementary dividend of Euros 0.5922 per share, for a total amount of Euros 593 million, paid on 30 June 2016.

On 30 October 2016, the Board of Directors of Gas Natural SDG, S.A. resolved to pay an interim dividend of Euros 0.330 per share out of 2016 results, for a total of Euros 330 million, which was paid on 27 September 2016.

The Company had sufficient liquidity to pay out the dividend at the approval date, with the necessary liquidity to proceed to payment pursuant to the Spanish Companies Act. The provisional liquidity statement drawn up by the Directors on 22 July 2016 as follows:

Profit/(loss) after tax	721
Reserves to be recognised	-
Maximum amount distributable	721
Forecast interim dividend payment	330
Cash resources	1,434
Undrawn credit facilities	6,906
Total liquidity	8,340

On 7 February 2017, the Board of Directors approved the following proposal for the distribution of Gas Natural SDG, S.A.'s net profit for 2016, for submission to the Annual General Meeting:

Available for distribution	
Profit/(loss)	1,067
Distribution	
To Voluntary reserve	66
To Dividend	1,001

This proposal for the distribution of profits prepared by the Board for approval by the Annual General Meeting includes the payment of a supplementary dividend of Euros 0.67 per qualifying share outstanding on the proposed payment date, 27 June 2017.

The economic rights inherent to treasury shares, with the exception of the right to free allocation of new shares, will be allocated proportionally to the rest of the shares.

Year 2015

Includes the payment of an interim dividend of Euros 0.397 per share out of 2014 profits, for a total amount of Euros 397 million, agreed on 28 November 2014 and paid out on 8 January 2015.

The proposal for the distribution of 2014 profits approved by the Annual General Meeting held on 14 May 2015 included the payment of a supplementary dividend of Euros 0.511 per share, for a total amount of Euros 512 million, paid on 1 July 2015.

Grants

Movements in capital grants during 2015 were as follows:

	Capital grants
At 01/01/2015	3
Demerger scope (<i>Note 5</i>)	(3)
At 31/12/2015	-

Movements in the above table are shown net of taxes.

Note 14. Provisions

The breakdown of provisions at 31 December 2016 and 2015 is as follows:

	At 31/12/16	At 31/12/15
Provisions for employee obligations	285	283
Other provisions	182	198
Non-current provisions	467	481

Provisions for employee obligations

A breakdown of the provisions related to employee obligations is as follows:

	2016			2015		
	Pensions and other similar obligations	Other obligations with personnel	Total	Pensions and other similar obligations	Other obligations with personnel	Total
At 1 January	274	9	283	280	9	289
Contributions charged to profits	8	7	15	8	9	17
Payments during the year	(10)	–	(10)	(15)	–	(15)
Changes recognised directly in equity	(4)	–	(4)	(4)	–	(4)
Demerger scope (<i>Note 5</i>)	–	–	–	(1)	–	(1)
Transfers and other applications	7	(6)	1	6	(9)	(3)
At 31 December	275	10	285	274	9	283

Pensions and other similar liabilities

Most of the post-employment obligations of Gas Natural SDG, S.A. consist of the contribution of defined amounts to occupational pension plan systems. Nevertheless, at 31 December 2016 and 31 December 2015, Gas Natural SDG, S.A. held the following defined benefit obligations for certain groups of workers:

- Pensions to retired workers, the disabled, widows, orphans and other related groups.
- Defined benefit supplement obligations with retired personnel of the legacy Unión Fenosa group who retired before November 2002 and a residual part of current personnel.
- Coverage of retirement and death for certain employees.
- Gas subsidy for current and retired personnel.
- Electricity for current and retired personnel.
- Obligations with employees that took early retirement until they reach official retirement age and early retirement plans.
- Salary supplements and contributions to social security for a group of employees taking early retirement until they can access ordinary retirement.
- Health care and other benefits.

The amounts recognised in the Balance sheet for pensions and similar obligations, as well as the movement in the current value of the obligations and the fair value of the plan assets are determined as follows:

Present value of obligations	2016	2015
At 1 January	1,057	1,112
Service cost for the year	2	2
Interest cost	20	21
Changes recognised directly in equity	65	(13)
Benefits paid	(71)	(73)
Transfers and other	7	8
At 31 December	1,080	1,057
Fair value of plan assets		
At 1 January	783	832
Expected yield	14	15
Contributions	(2)	1
Changes recognised directly in equity	69	(9)
Benefits paid	(59)	(59)
Transfers and other	–	3
At 31 December	805	783
Provisions for pensions and similar obligations	275	274

The amounts recognised in the income statement for all the above-mentioned defined benefit plans are as follows:

	2016	2015
Service cost for the year	2	2
Interest cost	20	21
Expected return on plan assets	(14)	(15)
Total charge to the income statement	8	8

Benefits to be paid in the coming years for the above-mentioned commitments are as follows:

	2016	2015
1 to 5 years	2	4
5 to 10 years	37	30
More than 10 years	236	240
Provisions for pensions and similar obligations	275	274

The plan assets expressed as a percentage of the total fair value of the assets are as follows:

% of total	2016	2015
Bonds	100	100

Cumulative actuarial gains and losses, net of the tax effect, recognised directly in equity are negative in the amount of Euros 3 million in 2016 (negative in the amount of Euros 6 million in 2015).

The change recognised in equity relates to actuarial losses and gains derived basically from adjustments to:

	2016	2015
Financial assumptions	22	7
Experience	(26)	(11)
Limits on assets	–	–
At 31 December	(4)	(4)

Actuarial assumptions applied are as follows:

	At 31/12/16	At 31/12/15
Discount rate (% annual)	0.0 to 1.8	0.2 to 2.6
Expected return on plan assets (% annual)	0.0 to 1.8	0.2 to 2.6
Future salary increases (% annual)	2.0	2.0
Future pension increases (% annual)	2.0	2.0
Inflation rate (annual)	2.0	2.0
Mortality table	PERMF 2000	PERMF 2000
Life expectancy:		
Men		
Retired during the year	22.5	22.5
Retiring within 20 years	42.5	42.5
Women		
Retired during the year	27	27
Retiring within 20 years	48.4	48.4

These assumptions are applicable to all the obligations homogeneously irrespective of the origin of their collective bargaining agreements.

The interest rates used to discount post-employment commitments are applied based on the period of each commitment and the reference curve is calculated applying observable rates for high-credit-quality corporate bonds (AA) issued in the Eurozone.

The costs of health care have been measured on the basis of the expected costs of the premiums of the different medical care policies taken out. A 1% variation in the increase in the cost of these premiums would not have a significant impact on the liability booked at 31 December 2016 and 31 December 2015, nor would it cause a relevant variation in the normal and financial costs for future years in relation to those booked in 2016 and 2015.

Other obligations with personnel

The Company operates a variable multi-annual remuneration system aimed at strengthening the commitment of the management to achieving the economic objectives of the group directly related to those established in the current Strategic Plans, approved by the Board of Directors and communicated to the financial markets and the achievement of which, along with their permanence in the group, grants the right to receive a variable remuneration in cash in the first quarter of the year after their termination.

At 31 December 2016, there is a provision for the 2014-2016, 2015-2017 and 2016-2018 remuneration programmes totalling Euros 19 million (Euros 18 million at 31 December 2015), Euros 9 million of which are classed as non-current in 2016 (Euros 9 million 2015).

Other non-current provisions

The movement in other non-current provisions is as follows:

	2016	2015
	Non-current provisions	Non-current provisions
At 1 January	198	328
Appropriations ¹	1	15
Reversals	(10)	2
Payments	(7)	(17)
Transfers and others	–	20
Demerger scope (<i>Note 5</i>)	–	(146)
At 31 December	182	198

¹ Includes Euros 1 million and Euros 2 million in 2016 and 2015, respectively, relating to the financial update of provisions.

Non-current provisions" mainly includes provisions posted to cover obligations deriving mainly from tax claims (Note 19), litigation and arbitration, and other liabilities.

No provision for onerous contracts was deemed necessary at 31 December 2016 or 2015.

At 31 December 2016, the estimated payment dates for these obligations are between one and five years (Euros 7 million), between five and 10 years (Euros 0 million) and more than 10 years (Euros 175 million) (2015: Euros 9 million at between one and five years, Euros 0 million at between five and 10 years and Euros 189 million at more than 10 years).

Note 15. Borrowings

The breakdown of borrowings at 31 December 2016 and 2015 is as follows:

	At 31/12/16	At 31/12/15
Borrowings from financial institutions	3,190	2,983
Derivatives (<i>Note 16</i>)	93	161
Other financial liabilities	17	15
Non-current borrowings	3,300	3,159
Borrowings from financial institutions	270	187
Derivatives (<i>Note 16</i>)	15	14
Other financial liabilities	12	420
Current borrowings	297	621
Total	3,597	3,780

The carrying amounts and fair value of the non-current borrowings are as follows:

	Carrying amount		Fair value	
	At 31/12/16	At 31/12/15	At 31/12/16	At 31/12/15
Borrowings from financial institutions and other financial liabilities	3,300	3,159	3,301	3,164

The fair value of loans with fixed interest rates is estimated on the basis of the discounted cash flows over the remaining terms of such debt. The discount rates were determined based on market rates available at 31 December 2016 and 31 December 2015 on borrowings with similar credit and maturity characteristics.

The movement in borrowings is as follows:

	2016	2015
At 1 January	3,780	4,521
Demerger scope (Note 5)	–	(12)
Increase	859	845
Decrease	(1,042)	(1,574)
At 31 December	3,597	3,780

The following tables describe borrowings and maturities at 31 December 2016 and 2015, taking into account the impact of derivative hedges.

	2017	2018	2019	2020	2021	2022 and beyond	Total
At 31 December 2016							
Fixed	156	232	630	127	84	92	1,321
Floating	141	192	500	348	471	624	2,276
Total	297	424	1,130	475	555	716	3,597

	2016	2017	2018	2019	2020	2021 and beyond	Total
At 31 December 2015							
Fixed	579	365	191	588	177	255	2,155
Floating	42	79	196	720	400	188	1,625
Total	621	444	387	1,308	577	443	3,780

Setting aside the impact of derivatives on borrowings, fixed-rate debt would amount to Euros 104 million of total borrowings at 31 December 2016 (Euros 630 million at 31 December 2015); variable-rate debt would amount to Euros 3,385 million at 31 December 2016 (Euros 2,975 million at 31 December 2015).

The following tables describe the gross borrowings denominated in foreign currencies at 31 December 2016 and at 31 December 2015 and their maturities, taking into account the impact of the derivative hedges:

	2017	2018	2019	2020	2021	2022 and beyond	Total
At 31 December 2016:							
Euro debt	264	409	705	475	555	716	3,124
USD debt	33	15	425	–	–	–	473
Total	297	424	1,130	475	555	716	3,597

	2016	2017	2018	2019	2020	2021 and beyond	Total
At 31 December 2015							
Euro debt	589	413	373	896	577	443	3,291
USD debt	32	31	14	412	–	–	489
Total	621	444	387	1,308	577	443	3,780

Borrowings bore an average effective interest rate in 2016 of 1.53% (2.02% in 2015) including the derivatives assigned to each transaction.

At 31 December 2016, Euros 6 million in interest pending payment are included (Euros 7 million at 31 December 2015).

Set out below are the most relevant financial instruments:

Bank borrowings

Bank borrowings include other bilateral bank loans of Euros 1,537 million at 31 December 2016 (Euros 1,670 million at 31 December 2015), no amounts having been drawn down on credit lines.

These payables include bank borrowings totalling Euros 1,169 million (Euros 625 million at 31 December 2015) that are subject to the fulfilment of certain covenants.

At the preparation date of these Annual accounts, Gas Natural SDG, S.A. is not in breach of its financial obligations or of any type of obligation that could give rise to the early maturity of its financial commitments.

Institutional financing

The Company records balances payable to the Official Credit Institute (ICO) relating to instruments maturing in 2018 at maximum, for a total amount of Euros 112 million (Euros 185 million in 2015).

Additionally, financing granted by the European Investment Bank (EIB) to Gas Natural SDG, S.A. has been drawn down in the amount of Euros 1,811 million, the sum of Euros 300 million being drawable on a financing line granted but not utilised (Euros 1,315 million and Euros 133 million drawable in 2015).

Note 16. Risk management and derivative financial instruments

Risk management

Gas Natural Fenosa has a series of standards, procedures and systems for identifying, measuring and managing different types of risk which are made up of the following basic action principles:

- > Guaranteeing that the most relevant risks are correctly identified, evaluated and managed.
- > Segregation at the operating level of the risk management functions.
- > Assuring that the level of risk exposure of Gas Natural Fenosa in its business is in line with the objective risk profile and achievement of its annual, strategic objectives.
- > Ensuring the appropriate determination and review of the risk profile by the Risk Committee, proposing global limits by risk category, and assigning them to the Business Units.

On 23 June 2016, the United Kingdom voted to withdraw from the European Union ("Brexit"). Although the UK's withdrawal will be accompanied by a process of negotiation over a period of time that cannot be determined as yet, the decision has already had consequences in the capital and foreign exchange markets. Gas Natural Fenosa's exposure to Brexit risk is practically non-existent.

Interest rate risk

The fluctuations in interest rates modify the fair value of the assets and liabilities that accrue a fixed interest rate and the cash flows from assets and liabilities pegged to a floating interest rate, and, accordingly, affect equity and profit, respectively.

The purpose of interest rate risk management is to balance floating and fixed borrowings in order to reduce borrowing costs within the established risk parameters.

Gas Natural SDG, S.A. employs financial swaps to manage exposure to interest rate fluctuations, swapping floating rates to fixed rates.

The financial debt structure at 31 December 2016 and 2015 (Note 15), after taking into account the hedges arranged through derivatives, is as follows:

	At 31/12/16	At 31/12/15
Fixed interest rate	1,321	2,155
Floating interest rate	2,276	1,625
Total	3,597	3,780

The floating interest rate is mainly subject to the fluctuations of the Euribor and the Libor.

The sensitivity of results and equity (measurement adjustments) to interest rate fluctuations is as follows:

	Increase/decrease in interest rates (basis points)	Effect on profit before tax	Effect on equity before tax
2016	+50	(11)	80
	-50	11	(80)
2015	+50	(8)	10
	-50	8	(10)

Exchange rate risk

The variations in the exchange rates can affect the fair value of:

- > Counter value of cash flows related to the purchase-sale of raw materials denominated in currencies other than local or functional currencies.
- > Debt denominated in currencies other than local or functional currencies.
- > Operations and investments in non-Euro currencies, and, accordingly, the counter value of equity contributed and results.

In order to mitigate these risks Gas Natural SDG, S.A. finances, to the extent possible, its investments in local currency. Furthermore, it tries to match, whenever possible, costs and revenues indexed in the same currency, as well as amounts and maturities of assets and liabilities arising from operations denominated in non-Euro currencies.

For open positions, the risks in investments in non-functional currencies are managed through financial swaps and foreign exchange fluctuation insurance when its marginal contribution to the risk is relevant and can exceed the risk limits established.

The non-Euro currency with which Gas Natural SDG, S.A. operates the most is the US Dollar. The sensitivity of results and equity ("Adjustments for changes in value") of the Society to a 5% variation (increase or decrease) in the US Dollar / Euro exchange rate is as follows:

	%	2016	2015
Effect on profit before tax	+5	-	(1)
	-5	-	1
Effect on equity before tax	+5	-	-
	-5	-	-

Commodity price risk

A portion of operating expenses of Gas Natural SDG, S.A. are linked to the purchase of gas for supplies for other group companies. Therefore, Gas Natural SDG, S.A. is exposed to the variation in commodity prices whose determination is basically subject to crude oil prices and those of its by-products.

The exposure to these risks is managed and mitigated through the monitoring of its position regarding these commodities, trying to balance purchase and supply obligations and diversification and management of supply contracts. When it is not possible to achieve a natural hedge the position is managed, within reasonable risk parameters, through derivatives to reduce exposure to price risk, generally through hedging instruments.

In electricity and CO₂ emission allowances trading by the Company, risk is insignificant due to the low volume of transactions and the established limits placed, both on the amount and maturity date.

The sensitivity of results and equity (measurement adjustments) to changes in the fair value of derivatives contracted to hedge commodity prices and for trading purposes is analysed below:

	Increase / decrease in the electricity sale price (%)	Effect on profit before tax	Effect on equity before tax
2016	+10	–	–
	–10	–	–
2015	+10	1	–
	–10	(1)	–

As regards exposure to low commodity prices, Gas Natural Fenosa has no relevant investments in upstream businesses or commodities production, so that fluctuations in commodity prices have no significant impact on asset values.

Sensitivity to the prices of oil, gas, coal and electricity is explained below:

- > Gas and electricity distribution. It is a regulated activity with revenue and profit margins linked to distribution infrastructure management services rendered, irrespective of the prices of the commodities distributed. In any event, a fall in the price of gas could increase consumption, having a favourable impact on revenue and thus contributing to the stability of Gas Natural Fenosa's results.
- > Gas and electricity. Profit margins on gas and electricity supply activities are directly affected by commodity prices. In this regard, Gas Natural Fenosa has a risk policy that stipulates the tolerance range, based on applicable risk limits, among other aspects. Measures employed to keep risk within the stipulated limits include active supply management, balanced acquisitions and sales formulas, and specific hedging so as to maximise the risk-profit relationship.

Credit risk

The credit risk arising from the default of a counterparty is controlled through policies that assure that wholesale sales of products are made to customers with an appropriate credit history, for which the respective solvency studies are established and based on which respective credit limits are assigned.

Various credit quality measurement models have been designed. Based on these models, the probability of customer default on payment can be measured, and the expected commercial loss can be kept under control.

The main guarantees negotiated are bank guarantees, guarantees and deposits.

Furthermore, the outstanding trade receivables are stated on the balance sheet net of provisions for bad debts (Note 11), estimated by Gas Natural SDG, S.A. based on the age of the debt and the experience of previous years in line with the prior segregation of customer portfolios and the current economic environment.

At 31 December 2016 and 2015 Gas Natural SDG, S.A. does not have significant concentrations of credit risk.

In order to mitigate credit risk in financial positions, derivatives have been contracted and cash surpluses are placed in banks and financial institutions that are highly solvent according to credit ratings by Moody's and S&P.

Likewise, most of the accounts receivable not due nor provided for, have a high credit rating according to the valuations of Gas Natural SDG, S.A. based on an analysis of the solvency and payment habits of each customer.

The ageing analysis of financial assets concluded that there were no unimpaired, past due financial assets at 31 December 2016 and 2015.

The impaired financial assets are broken down in Note 11.

Liquidity risk

Gas Natural SDG, S.A. has liquidity policies that ensure compliance with its payment commitments, diversifying the coverage of financing needs and debt maturities. A prudent management of the liquidity risk includes maintaining sufficient cash and realisable assets and the availability of sufficient funds to cover credit obligations.

At 31 December 2016, available cash totalled Euros 7,883 million (Euros 8,187 million in 2015), including cash and cash equivalents of Euros 502 million (Euros 1,244 million in 2015), undrawn bank financing and credit lines to the amount of Euros 7,381 million (Euros 6,943 million in 2015). There is also unused capacity to issue debt on the capital markets (Note 17).

Capital management

The main purpose of capital management of Gas Natural SDG, S.A. is to ensure a financial structure to optimise capital cost and maintain a solid financial position, in order to combine the creation of added value with the access to the financial markets at a competitive cost to cover financing needs.

Gas Natural Fenosa considers the following to be objective indicators of capital management: maintaining a long-term leverage ratio of approximately 50%.

The long-term credit rating of Gas Natural SDG, S.A. is as follows:

	2016	2015
Moody's	Baa2	Baa2
Standard & Poor's	BBB	BBB
Fitch	BBB+	BBB+

Derivative financial instruments

The breakdown of derivative financial instruments by category and maturity is as follows:

	At 31/12/16		At 31/12/15	
	Assets	Liabilities	Assets	Liabilities
Hedging derivative financial instruments	28	61	-	160
Fair value hedge				
Interest rate and foreign exchange rate	-	40	-	122
Cash flow hedge				
Interest rate	28	21	-	38
Other financial instruments	31	32	1	1
Interest rate and foreign exchange rate	31	32	1	1
Derivative financial instruments – non current	59	93	1	161
Hedging derivative financial instruments	-	15	-	14
Fair value hedge				
Exchange rate	-	10	-	13
Cash flow hedge				
Interest rate	-	5	-	1
Other financial instruments	76	82	181	189
Price of commodities	76	82	181	189
Derivative financial instruments current	76	97	181	203
Total	135	190	182	364

"Other financial instruments" include the derivatives not qualifying for hedge accounting.

The impact on the Income statement of derivative financial instruments is as follows:

	2016		2015	
	Operating results	Financial results	Operating results	Financial results
Cash flow hedge	–	(10)	–	(11)
Other financial instruments	(28)	(2)	(2)	15
Total	(28)	(12)	(2)	4

The breakdown of derivatives at 31 December 2016 and 2015, their fair value and maturities of their notional values is as follows:

	Fair value	31/12/16 Notional value						Subsequent years	Total
		2017	2018	2019	2020	2021			
Interest rate hedges:									
Cash flow hedges:									
Financial swaps (EUR)	23	684	–	–	–	–	1.500	2,184	
Financial swaps (USD)	–	166	259	–	–	–	–	425	
Financial swaps (NOK)	(21)	–	–	–	–	–	101	101	
Exchange rate hedges:									
Fair value hedges:									
Financial swaps (USD)	(40)	–	–	60	–	160	–	220	
Foreign exchange insurance (USD)	(10)	219	–	–	–	–	–	219	
Others:									
Commodities price derivatives (EUR)	(6)	13	–	–	–	–	–	13	
Financial swaps (MXN)	(1)	–	–	–	–	–	–	–	
	(55)	1,082	259	60	–	160	1,601	3,162	

	Fair value	31/12/15						Subsequent years	Total
		Notional value							
		2016	2017	2018	2019	2020			
Interest rate hedges:									
Cash flow hedges:									
Financial swaps (EUR)	(13)	255	684	–	–	–	–	939	
Financial swaps (USD)	(1)	–	161	251	–	–	–	412	
Financial swaps (NOK)	(25)	–	–	–	–	–	101	101	
Exchange rate hedges:									
Fair value hedges:									
Financial swaps (USD)	(122)	–	–	–	722	–	160	882	
Foreign exchange insurance (USD)	(13)	675	–	–	–	–	–	675	
Others:									
Commodities price derivatives (EUR)	(8)	103	27	–	–	–	–	130	
	(182)	1,033	872	251	722	–	261	3,139	

Note 17. Amounts owing to group companies and associates

The breakdown by maturity of borrowings from group companies is as follows:

Maturity	At 31/12/16	At 31/12/15
2016	–	2,891
2017	3,000	1,602
2018	1,556	1,470
2019	1,199	1,196
2020	1,639	1,636
2021	1,531	1,238
2022	1,742	–
Subsequent years	2,960	4,097
Total	13,627	14,130

Payables to Group companies mainly relate to issuances by Gas Natural Capital Markets, S.A. and Gas Natural Fenosa Finance, B.V. under the European Medium-Term Notes (EMTN) programme. This programme was created in 1999; following a number of extensions, the latest in December 2016, the programme limit is Euros 14 billion (Euros 14 billion in 2015). At 31 December 2016, a total of Euros 10,205 million principal had been utilised (Euros 10,605 million in 2015), being the amount yet to be utilised at Euros 3,795 million.

Additionally, it includes the amount payable to Gas Natural Finance, B.V. for Euro Commercial Paper (ECP) issues, Euros 100 million having been utilised (Euros 300 million in 2015), the amount available is Euros 900 million (Euros 700 million in 2015). The balances payable to Gas Natural Fenosa Finance, B.V. in respect of perpetual subordinated debentures amounting to Euros 1,500 million (Euros 1,500 million 2015) and the debt with Unión Fenosa Preferentes, S.A. relating to preferred shares totalling Euros 110 million (Euros 110 million in 2015), are also included.

Borrowings from group companies include interest accrued pending maturity of Euros 350 million (Euros 354 million in 2015).

“Cash-pooling” balances with Group companies amounting to Euros 1,163 million are also included.

Borrowings from group companies and associates accrued an average interest rate of 4.2% in 2016 (4.1% in 2015).

There are no significant differences between the carrying amounts and fair values of Payables to Group companies and associates.

Note 18. Trade and other payables

The breakdown in 2016 and 2015 is as follows:

	At 31/12/16	At 31/12/15
Trade payables	242	247
Payables with group companies and associates	311	254
Derivatives (<i>Note 16</i>)	82	189
Other payables	11	7
Personnel (outstanding remuneration)	23	22
Public Administrations	17	16
Current tax liabilities	24	–
Total	710	735

Most payables do not accrue interest and have contractual maturity dates of less than 30 days, in the case of gas purchases and within the legal limits, for other suppliers.

Information on average supplier payment period. Additional Provision 3 “Duty of disclosure” of Law 15/2010/5 July

The average payment period is in accordance with Law 15/2010 on measures to combat late payment in business operations.

Information disclosed under the Resolution of 29 January 2016 of the Institute of Accountants and Auditors concerning the details to be included in the notes to the annual accounts concerning the average supplier payment period is as follows:

	2016	2015
	Amount	Amount
Total payments (euros)	3,993,685,684	5,411,897,950
Total payments outstanding (euros)	88,041,054	99,655,311
Average supplier payment period (days) ¹	22	24
Transactions paid ratio (days) ²	22	24
Transactions pending payment ratio (days) ³	24	26

¹ Calculated on the basis of amounts paid and pending payment

² Average payment period in transactions paid during the year.

³ Average age, suppliers pending payment balance.

In the following ratios are not included all those situations that could affect the calculation, such as payables with group companies and associates.

Note 19. Tax situation

Gas Natural SDG, S.A. is the parent of the tax consolidated group 59/93, in which are all the companies resident in Spain subsidiaries, directly or indirectly integrated in at least 75 % of the parent company and meet certain requirements, which involves joint determination of taxable income of the group and the deductions and allowances to the quota. The tax consolidated group for 2016 is analysed in Appendix I.

Corporate income tax is calculated on the basis of economic or accounting profit obtained by application of generally accepted accounting principles, which do not necessarily coincide with taxable profit, understood as taxable income for corporate income tax purposes.

The reconciliation of accounting profit for the years 2016 and 2015 to taxable income is as follows:

	At 31/12/16	At 31/12/15
Accounting profit before tax	983	998
Permanent differences	(1,278)	(1,438)
Temporary differences		
Arising during current year	28	18
Arising in prior years	(28)	(129)
Tax base	(295)	(551)

Permanent differences in 2016 mainly relate to the application of the tax consolidation system and to the exemption for the avoidance of double taxation on dividends and income derived from the transfer of shareholdings provided for in Article 21 of Law 27/2014 on corporate income tax, which entails permanent negative differences of Euros 1,560 million resulting mainly from the negative adjustments of dividends accrued in the year and the impairment of Group company and associate shareholdings amounting to Euros 206 million.

In 2015, permanent differences relate basically to the application of the tax consolidation system and to the exemption for the avoidance of double taxation on dividends and income derived from the transfer of shareholdings provided for in Article 21 of Law 27/2014 on corporate income tax, entailing negative permanent differences of Euros 1,542 million, due mainly to downward adjustments for dividends accrued during the year and the impairment of Group company and associate shareholdings amounting to Euros 106 million.

In 2016 the Company posted a tax loss of Euros 295 million, which is recovered from the Tax Group companies due to the taxable income generated by them during the year.

Law 27/2014 keeps the non deductibility in corporate income tax of the impairment losses on shareholdings, as a result of Law 16/2013 with effect as from 1 January 2013. In 2016 and 2015 the impairment losses recognised for shareholdings were not treated as tax deductible. Items yet to be included in the tax base after having filed the final corporate income tax return for 2015 are the following:

Company	Amounts pending inclusion in tax base in 2015	Amounts included in 2016	Amounts pending inclusion in tax base in 2016
Gas Natural Sao Paulo Sul, S.A.	7	(7)	–
Others	1	–	1
	8	(7)	1

Income tax expense is as follows:

	2016	2015
Current tax	(84)	(136)
Deferred tax	–	29
Total	(84)	(107)

Current corporate income tax is the result of applying a 25% tax rate (28% in 2015) to taxable income. In the tax consolidated group, tax credits applied in 2016 amounted to Euros 7 million (Euros 8 million in 2015) and no tax losses were offset. Adjustments are also included for prior-year taxable differences, entailing an increase in expense of Euros 10 million (increase of Euros 8 million in 2015).

On 27 November 2014, Corporate Income Tax Law 27/2014 was approved, stipulating a general tax rate cut from 30% to 28% for 2015 and to 25% as from 2016. However, in order to neutralise the tax rate cut, a deduction for the reversal of temporary measures has been provided to offset the economic cost of the rate cut for taxpayers that were affected by the 30% limit on the deduction of depreciation charges, or that restated fixed assets, in both cases under Law 16/2012 (27 December) on tax measures to consolidated public finances and encourage economic activities. Finally, Law 27/2014 provides an exemption regime for the transfer of significant shareholdings in resident entities that eliminates related temporary taxable differences.

Royal Decree-Act 3/2016, adopting tax-related measures to strengthen public finances, was enacted on 3 December 2016; it made significant amendments to the law on corporate income tax. Those amendments include: the obligation, from 1 January 2016, to reverse, within at most five years, any impairment recognised on holdings that were deductible prior to 2013; limitation of tax loss carryforwards for large companies (revenues over Euros 60 million) to 25% of the preceding taxable base; and limitation of the application of the earned or unused internal or international double-taxation tax credit to 50% of the pre-existing gross tax payable. Additionally, with effects from 1 January 2017, the transmissions losses of participations will not be deducted. In 2016 these measures had a non-material impact in the financial statements of Gas Natural Fenosa.

Incomes that qualify for the tax credit for reinvestment of extraordinary profits provided by Article 42 of the revised Corporate Income Tax Act introduced under Legislative Royal Decree-Law 4/2004 (TRLIS) and the resulting investments made in previous periods are explained in the annual accounts for the relevant years. The breakdown is as follows:

Year of sale	Amount obtained from sale	Amount reinvested	Income qualifying for deduction	Year reinvested
2011	2	2	1	2011
2014	412	412	209	2014
Total	414	414	210	

The reinvestment made in fixed assets used in business activities both by the Company and by the other companies in the tax group, pursuant to Article 75 of the Corporate Income Tax Act.

Income qualifying for the tax scheme for transfers of assets made in compliance with competition law (Additional Provision 4 of the revised CIT Act) is explained below:

Year of sale	Amount obtained from sale	Amount reinvested	Initial capital gain	Capital gain included in tax base at year end	Capital gain yet to be included in tax base at year end
2002	917	917	462	18	444
2003	39	39	20	–	20
2004	292	292	177	9	168
2005	432	432	300	1	299
2006	309	309	226	–	226
2009	161	161	87	–	87
2010	752	752	551	–	551
2011	450	450	394	–	394
2012	38	38	32	–	32
Total	3,390	3,390	2,249	28	2,221

The reinvestment has been made in fixed assets used in business activities both by the Company and by the other companies in the tax group, pursuant to Article 75 of the Corporate Income Tax Act.

A breakdown of the tax effect of each item on the Statement of Recognised Income and Expenses is as follows:

	At 31/12/16			At 31/12/15		
	Gross	Tax effect	Net	Gross	Tax effect	Net
Cash flow hedges	34	(8)	26	2	(1)	1
Actuarial gains and losses and other adjustments	3	(1)	2	4	(1)	3
	37	(9)	28	6	(2)	4

A breakdown of deferred taxes is as follows:

	At 31/12/16	At 31/12/15
Deferred tax assets:	128	123
Non-current	118	114
Current	10	9
Deferred tax liabilities:	(231)	(234)
Non-current	(231)	(234)
Net deferred tax	(103)	(111)

Movements and breakdown of deferred asset accounts are as follows:

Deferred tax assets	Provisions	Tax credits	Valuation of assets and financial instruments	Goodwill	Other	Total
At 01/01/2015	144	5	5	8	12	174
Creation (reversal)	(31)	(1)	–	2	–	(30)
Movements linked to equity adjustments	(1)	–	(1)	–	–	(2)
Demerger scope (<i>Note 5</i>)	–	–	–	–	(9)	(9)
At 31/12/2015	112	4	4	10	3	133
Creation (reversal)	(4)	–	–	1	–	(3)
Movements linked to equity adjustments	(1)	–	(1)	–	–	(2)
Others	(2)	2	–	–	–	–
At 31/12/2016	105	6	3	11	3	128

Deferred tax liabilities	Depreciation differences	Deferred gains	Merger ¹	Other	Total
At 01/01/2015	62	210	37	25	334
Creation (reversal)	–	–	–	(1)	(1)
Demerger scope (<i>Note 5</i>)	(58)	–	(36)	(1)	(95)
Other	–	–	(1)	(3)	(4)
At 31/12/2015	4	210	–	20	234
Creation (reversal)	(1)	–	–	(2)	(3)
Movements linked to equity adjustments	–	–	–	7	7
Other	–	–	–	(7)	(7)
At 31/12/2016	3	210	–	18	231

¹ “Merger” relates basically to the tax effect of the part of the merger difference resulting from the merger of Unión Fenosa, S.A. into Gas Natural SDG, S.A. in 2009, allocated to net assets acquired, which is not expected to have tax effects.

In 2015, the demerger of Gas Natural SDG, S.A. was completed in favour of Gas Natural Fenosa Generación, S.L.U. (Note 5), relating to the nuclear power generation business. Pursuant to Article 76.3 of Law 27/2014, this operation was defined as a non-cash contribution of a line of business and was thus subject to the special scheme provided by Title VII, Chapter VIII of that law. Note 5 provides a breakdown of the carrying amount of the assets handed over, which matches the value recognised for the shareholding in the company Gas Natural Fenosa Generación, S.L.U.

In 2014, the demerger of the thermal and hydroelectric power generation business from Gas Natural SDG, S.A. to Gas Natural Fenosa Generación, S.L.U. was completed. Pursuant to Article 83.3 of Royal Decree-Law 4/2004 whereby the Corporate Income Tax Act (CIT Act) was approved, this operation is defined as a non-cash contribution of a line of business and is thus subject to the special scheme provided for in Title VII, Chapter VIII of said Act.

In 2009, the companies Unión Fenosa, S.A. and Unión Fenosa Generación S.A. were merged into Gas Natural SDG, S.A. under the special tax scheme for mergers, spin-offs, asset contributions, share exchanges and changes of registered address of European companies or European cooperatives from one European Union Member State to another, provided by Title VII, Chapter VIII TRLIS. The information requirements stipulated in the special tax scheme are fulfilled in the notes to Gas Natural SDG, S.A.'s 2009 annual accounts.

In October 2015, the tax inspection of Gas Natural SDG, S.A. and Gas Natural Distribución Latinoamérica, S.A. (formerly Gas Natural Internacional SDG, S.A.) for corporate income tax (2009 and 2010) and value added tax (2010) came to an end without any material issues having been identified and without any significant impacts on the income statement.

Gas Natural SDG, S.A.'s tax group is open to inspection for 2011 and subsequent periods and the taxes to which it is subject.

As a result, among other things, of the different interpretations to which current tax legislation lends itself, additional liabilities could arise as a result of an inspection. The Company considers, however, that any liabilities that might arise would not significantly affect these Annual accounts.

Gas Natural Fenosa has recorded provisions for obligations deriving from a number of tax claims. At 31 December 2016 the main tax litigation affecting the Group relates to the tax credit for export activities. As a result of the inspection proceedings on tax periods 2003 to 2008, the Inspectorate has questioned the admissibility of the tax credit for export activities applied by Gas Natural Fenosa; the tax assessments have been contested and appeals have been lodged at the Tax and Treasury Court and the Supreme Court. At 31 December 2016, the assessments amount to Euros 93 million, including interest, and are fully provisioned (Note 14).

Note 20. Net turnover

Sales break down as follows:

	2016	2015
Electricity sales	1,460	1,696
Natural gas sales	1,620	1,938
Other sales	8	6
Income from equity instruments of Group companies and associates (<i>Note 9</i>)	1,560	1,542
Income from marketable securities and other financial instruments of Group companies and associates	414	458
Total	5,062	5,640

Electricity and gas sales are made basically in the domestic market.

Note 21. Supplies

This caption includes natural gas purchases under supply contracts in force and electricity purchases relating to the energy supply business.

Note 22. Personnel costs

The breakdown of this account in the income statement for 2016 and 2015 is as follows:

	2016	2015
Wages and salaries	152	143
Social security costs	22	22
Defined contribution plans	13	13
Defined benefit plans (Note 14)	2	2
Others	12	11
Total	201	191

The average number of employees of Gas Natural SDG, S.A. during 2016 and 2015 is as follows:

	2016	2015
Executives	478	467
Middle managers	192	189
Specialists	709	681
Workers	356	380
Total	1,736	1,716

The average number of employees of Gas Natural SDG, S.A. during 2016 and 2015 with a disability equal to or greater than 33% is as follows:

	2016		2015	
	Men	Women	Men	Women
Executives	3	–	2	–
Middle managers	–	1	–	1
Specialists	11	12	10	10
Workers	8	9	10	9
Total	22	22	22	20

The number of Company employees by gender and categories at year-end 2016 and 2015 is as follows:

	2016		2015	
	Men	Women	Men	Women
Executives	323	159	316	156
Middle managers	110	88	101	82
Specialists	340	375	342	353
Workers	94	257	88	276
Total	867	879	847	867

Note 23. Other operating expenses

A breakdown of this heading on the income statement account for 2016 and 2015 is as follows:

	2016	2015
Taxes	2	2
Leases, royalties, operation and maintenance	79	88
Professional services and insurance	60	51
Advertising and other commercial services	25	25
Contribution to Gas Natural Fenosa Foundation	2	2
Impairment losses and changes in trade provisions (<i>Note 11</i>)	5	8
Others	164	189
Total	337	365

The Company makes contributions to the Gas Natural Fenosa Foundation to enable it to carry out its energy and environmental projects in the community area, as well as to fund international initiatives and the activities of the Gas Museum and Historical Archive.

Note 24. Other operating income

This account includes Euros 370 million in transactions with group companies and associates in 2016 (Euros 354 million in 2015).

Note 25. Net financial income/(expense)

The breakdown of this account in the Income statement for 2016 and 2015 is as follows:

	2016	2015
Income from marketable securities and other financial instruments	30	29
Total financial income	30	29
Cost of borrowings	(633)	(663)
Interest expense on pensions (<i>Note 14</i>)	(6)	(6)
Other financial expense	(25)	(29)
Total financial expense	(664)	(698)
Variation in fair value of financial instruments	(1)	2
Trading portfolio and other available-for-sale assets	(1)	2
Net exchange differences	1	(13)
Net financial income/(expense)	(634)	(680)

Note 26. Foreign currency transactions

Transactions effected in foreign currencies are analysed below, the main currency being the US dollar:

	2016	2015
Sales	624	894
Income from equity instruments of Group companies and associates	46	66
Income from marketable securities and other financial instruments of Group companies and associates	4	23
Purchases	(886)	(874)
Services received	(23)	(14)
Total	(235)	95

Note 27. Information on transactions with related parties

The following are related parties for the purposes of this Note:

- Significant shareholders of Gas Natural SDG, S.A., shareholders that directly or indirectly hold an interest equal to or greater than 5%, as well as the shareholders who, without being significant, have exercised the power to put forward appointments of a member of the Board of Directors.

Based on this definition, the significant shareholders of Gas Natural SDG, S.A. are Fundació Bancaria Caixa d'Estalvis i Pensions de Barcelona ("la Caixa"), Repsol, S.A. (Repsol) and Global Infrastructure Partners III (GIP) and subsidiaries.

- Directors and executives of the Company and their immediate families. The term "director" means a member of the Board of Directors; "executive" means a member of the Management Committee of Gas Natural Fenosa and the Internal Audit Director. The operations with directors and executives are disclosed in Note 28.
- Group companies or entities. Transactions effected between group companies form part of the ordinary course of business and they have been done at market conditions.

The aggregated amounts of operations with significant shareholders are as follows (in thousand Euros):

Income and expense (in thousand Euros)	2016			2015	
	"la Caixa"	Repsol	GIP*	"la Caixa"	Repsol
Financial expenses	1,515	–	–	2,565	–
Services received	9,378	1	–	8,518	1
Purchases of goods	–	2,331	–	–	2,798
Other expenses ¹	10,125	–	–	14,389	–
Total expenses	21,018	2,332	–	25,472	2,799
Financial income	148	–	–	1,818	–
Services provided	–	39	–	–	5
Total income	148	39	–	1,818	5

Other transactions (in thousand Euros)	2016			2015	
	"la Caixa"	Repsol	GIP*	"la Caixa"	Repsol
Financing agreements, loans and capital contributions(lender) ²	341,770	–	–	599,298	–
Financing agreements, loans and capital contributions(borrower) ³	100,000	–	–	200,000	–
Warranties and guarantees received	100,000	–	–	201,667	–
Dividends and other profit distributions	424,923	367,291	66,045	311,716	273,873
Other operations ⁴	173,884	–	–	489,199	–

* Since 21 September 2016.

¹ Includes contributions to pension plans, group insurance policies, life insurance and other expenditure.

² Includes cash and cash equivalents.

³ At 31 December 2016, credit lines contracted with "la Caixa" amounted to Euros 569,000 thousand (Euros 569,000 thousand at 31 December 2015), of which no amounts having been utilised. "la Caixa" also has shares of other loans totalling Euros 100,000 thousand. At 31 December 2014, its shares in other loans amounted to Euros 200,000 thousand.

⁴ At 31 December 2016, the item "Other transactions" with "la Caixa" includes the amount of Euros 72,976 thousand in respect of foreign exchange hedges (Euros 207,996 thousand at 31 December 2015) and Euros 100,908 thousand in respect of interest rate hedges (Euros 201,203 thousand at 31 December 2015).

The aggregated amounts of operations with group companies and associates are as follows (in million Euros):

Expenses, income and other transactions	2016		2015	
	Group companies	Jointly-controlled entities and associates	Group companies	Jointly-controlled entities and associates
Financial expenses	(575)	–	(580)	–
Lease expenses	(53)	(6)	(60)	(6)
Services received	(24)	–	(25)	–
Purchases of goods	(2,215)	–	(2,560)	–
Total expenses	(2,867)	(6)	(3,225)	(6)
Financial income	431	1	458	–
Dividends received	1,623	2	1,528	14
Sale of goods	3,154	–	4,108	–
Other income	369	1	352	2
Total income	5,577	4	6,446	16
Sale of Property, plant and equipment, intangible and other assets	6	–	–	–
Other transactions	6	–	–	–

The item “Purchases” relates basically to electricity purchased from the other Group companies, since Gas Natural SDG, S.A. is their market representative.

Under the heading “Dividends received” are included the dividend payments from voluntary reserves, registered as a lower value on investments in group companies (Note 9).

Sales of natural gas and electricity are included under “Sale of goods”.

The item “Other income” includes income from services rendered in accordance with the nature and extent thereof.

Costs shared between the Company and other group companies are allocated on the basis of business or cost generation parameters.

Detailed definitions are prepared of services to be provided and of related activities or tasks in order to determine the measurement indicators used to calculate costs allocated. Transactions between companies are objective, transparent, non-discriminatory and always effected at arm’s length.

Note 28. Information regarding members of the Board of Directors and Management Committee

Remuneration of the members of the Board of Directors

In accordance with the By-laws and the General Meeting resolution of 14 May 2015, the Company may earmark a maximum of Euros 5 million for Board directors' remuneration each year.

The amount accrued by the members the Board of Directors of Gas Natural SDG, S.A., for belonging to the Board of Directors, Executive Committee (EC), Audit Committee (CA) and Appointments and Remuneration Committee (ARM), totalled Euros 4,573 thousand (Euros 4,205 thousand in 2015), broken down in euros as follows:

	Office	Board	EC	AC	ARC	Total
Mr. Isidro Fainé Casas ¹	Chairman	280,500	200,000	–	–	480,500
Mr. Salvador Gabarró Serra ²	Chairman	400,000	400,000	–	–	800,000
Mr. Josu Jon Imaz San Miguel ³	First Deputy Chairman	46,000	46,000	–	–	92,000
Mr. Antonio Brufau Niubó ⁴	Deputy Chairman	92,000	–	–	18,182	110,182
Mr. William Alan Woodburn ³	Second Deputy Chairman	46,000	46,000	–	9,091	101,091
Mr. Rafael Villaseca Marco	Chief Executive Officer	126,500	126,500	–	–	253,000
Mr. Ramón Adell Ramón	Director	126,500	126,500	40,000	–	293,000
Mr. Enrique Alcántara–García Irazoqui	Director	126,500	92,000	14,545	–	233,045
Mr. Xabier Añoveros Trías de Bes	Director	126,500	–	14,545	–	141,045
Mr. Marcelino Armenter Vidal ³	Director	46,000	46,000	–	–	92,000
Mr. Mario Armero Montes ³	Director	46,000	–	–	–	46,000
Mr. Francisco Belil Creixell	Director	126,500	46,000	29,091	9,091	210,682
Mr. Demetrio Carceller Arce ⁴	Director	92,000	92,000	–	–	184,000
Mrs. Benita María Ferrero–Waldner	Director	126,500	80,500	–	–	207,000
Mr. Alejandro García–Bragado Dalmau ³	Director	46,000	–	–	9,091	55,091
Mrs. Cristina Garmendia Mendizábal	Director	126,500	–	14,545	25,000	166,045
Mrs. Elena Herrero Starkie ⁵	Director	80,500	–	14,545	–	95,045
Mr. Emiliano López Achurra ⁶	Director	46,000	46,000	–	–	92,000
Mr. Miguel Martínez San Martín	Director	126,500	126,500	–	9,091	262,091
Mr. Heribert Padrol Munté ⁴	Director	92,000	–	–	–	92,000
Mr. Rajaram Rao ³	Director	46,000	46,000	14,545	–	106,545
Mr. Juan Rosell Lastortras ⁴	Director	92,000	92,000	–	–	184,000
Mr. Luis Suárez de Lezo Mantilla	Director	126,500	–	40,000	–	166,500
Mr. Miguel Valls Maseda ⁴	Director	92,000	–	–	18,182	110,182
		2,681,500	1,612,000	181,816	97,728	4,573,044

¹ Since 21 September 2016, previously a Member of the Board of Directors.

² Until 21 September 2016. Appointed Honorary President, unremunerated, on 30 September 2016.

³ Since 21 September 2016.

⁴ Until 21 September 2016.

⁵ Since 4 May 2016.

⁶ Until 4 May 2016.

In 2016, as in 2015, no amounts were received for other items.

In 2016, the Chief Executive Officer received Euros 57 thousand (Euros 85 thousand in 2015) as a Board member of the investee company CGE. These amounts are deducted from the CEO's variable remuneration.

The amounts accrued to the Chief Executive Officer for executive functions in respect of fixed remuneration, annual variable remuneration, multi-year variable remuneration and other items totalled Euros 1,212 thousand, Euros 1,002 thousand, Euros 860 thousand and Euros 8 thousand, respectively, in 2016 (Euros 1,142 thousand, Euros 1,054 thousand, Euros 883 thousand and Euros 8 thousand in 2015).

Contributions to pension plans and group insurance policies, together with life insurance premiums paid, totalled Euros 328 thousand in 2016 (Euros 315 thousand in 2015). Funds accumulated due to these contributions amount to Euros 3,241 thousand at 31 December 2016 (Euros 2,930 thousand at 31 December 2015).

The members of the Board of Directors of the Company have not received remuneration from profit sharing, bonuses or indemnities, and have not been given loans or advances. Neither have they received shares or share options during the year, nor have they exercised options or have options to be exercised.

The members of the Board of Directors are covered with the same liability policy that insures all managers and directors of Gas Natural Fenosa. In 2016, the premium paid by Gas Natural SDG, S.A. for the entire policy amounted to 101 thousand euros.

The Chief Executive Officer's contract was amended in October 2016 to remove the clause under which the contract would be terminated in the event of a material change in the Company's shareholders and its duration was extended to cover the entire term of his current appointment as a Company director.

It contains an agreement whereby six months' prior notice must be provided by the Chief Executive Officer, except in the event of force majeure, an exclusivity pact for the period during which he is to fulfil his functions and a confidentiality agreement for both the duration of the contract and post-termination.

The Chief Executive Officer's contract provides for an indemnity of three yearly payments of his full emoluments at the date of contractual amendment for certain termination events: at the company's decision, except in the event of a serious and culpable breach of his professional obligations causing serious harm to the interests of Gas Natural SDG, S.A., at the Chief Executive Officer's decision, or due to the finalisation of the contract. In addition, as consideration for a post-contractual no-competition agreement with a duration of one year, an indemnity equivalent to one year's full remuneration is provided for.

The contract requires the Company to arrange third-party liability insurance.

Transactions with Directors

The Directors have the obligation to avoid conflicts of interest as established by Regulation of the Board of Gas Natural SDG, S.A. and Articles 228 and 229 of the Capital Companies Law. Additionally, these articles require that conflicts of interest incurred by the board shall be reported in the annual accounts.

The Directors of Gas Natural SDG, S.A. have not reported any conflict of interest that has to be informed.

In the operations with related parties (significant shareholders) that have been submitted for approval by the Board, subject to a favourable report of the Appointments and Remuneration Committee or Audit Committee, the Directors representing the related party involved have abstained.

During the years 2016 and 2015, the members of the Board have not carried out related transactions outside the ordinary course or transactions that are not conducted under normal market conditions with the company or Group companies.

Remuneration of Executive personnel

For the sole purposes of the information contained in this section, “executives” refers to the members of the Management Committee, excluding the CEO, whose remuneration has been included in the previous section, and the Internal Audit Director.

During 2016 a total of 11 persons formed part of the Management Committee. One person left the committee in April.

Amounts accrued to executives in respect of fixed remuneration, annual variable remuneration, multi-year variable remuneration and other items totalled Euros 4,827 thousand, Euros 2,553 thousand, Euros 1,945 thousand and Euros 120 thousand, respectively, in 2016 (Euros 4,962 thousand, Euros 2,528 thousand, Euros 1,982 thousand and Euros 112 thousand, respectively, in 2015).

Contributions to pension plans and group insurance policies, together with life insurance premiums paid, totalled Euros 2,389 thousand in 2016 (Euros 2,428 thousand in 2015). Funds accumulated due to these contributions amount to Euros 22,121 thousand at 31 December 2016 (Euros 24,955 thousand at 31 December 2015).

The executives have received no remuneration in respect of profit sharing or bonuses and no loans have been granted to them. Advances to management personnel at 31 December 2016 amounted to Euros 175 thousand. At 31 December 2015 no advances to management personnel were granted. No indemnities were received during 2016 or 2015.

The contracts of the executives contain a clause that stipulates a minimum indemnity of two years pay in certain cases of termination of contract and an indemnity equivalent to one year’s fixed remuneration for the post-employment no-competition clause for a period of two years.

Note 29. Contingent liabilities and commitments

Guarantees

At 31 December 2016 Gas Natural SDG, S.A. has given guarantees to third parties for activities totalling Euros 251 million (Euros 260 million at 31 December 2015).

Financial guarantees have also been given totalling Euros 133 million (Euros 150 million at 31 December 2015), of which Euros 113 million relate to the guarantee for compliance with the obligations on loans received (Euros 132 million at 31 December 2015).

Gas Natural SDG, S.A. estimates that the unforeseeable liabilities at 31 December 2016, if any, that could arise from the guarantees given would not be significant.

Contractual commitments

At 31 December 2016, the Company is party to several gas supply contracts with “take or pay” clauses negotiated for “own use” (Note 6.5), by virtue of which it has gas purchase rights for the period 2017-2040 in the amount of Euros 8,358 million, calculated on the basis of natural gas prices at 31 December 2016.

Operating lease obligations breakdown as follows:

Period	2016	2015
	Operating leases	Operating leases
Up to one year	18	6
Between 1 and 5 years	70	14
Between 5 and 10 years	48	–
	136	20

Lease commitments include the rent of the “Torre del Gas” building owned by Torre Marenostrum, S.L., for which Gas Natural SDG has an operating lease without a purchase option for a period of ten years as from March 2006, extended at market value during the year in course for three years, as extensions are provided for at market value for successive periods of three years, on a discretionary basis for Gas Natural and an obligatory basis for Torre Marenostrum S.L.

It also includes operating leases without a purchase option that were written down in December 2016 of four buildings in Madrid (Avenida San Luís 77, Antonio López 193, Acanto 11-13 and Avenida América 38), for a term of ten years, except for Avenida América 38, extendable for five years more (Note 6).

Contingent liabilities

Gas Natural SDG, S.A. reports no relevant contingent liabilities relating to litigation or arbitration at the date of these Annual accounts.

Note 30. Auditors' fees

The fees accrued in thousand Euros by the different companies trading under the PwC brand are as follows:

(Thousand euros)	2016	2015
Auditing services	674	658
Assurance services and services related to the audit	289	402
Total fees	963	1,060

Note 31. Environment

Environmental actions

Gas Natural Fenosa's main activities related to the company's environmental strategy so as to assure compliance with environmental legislation, reduce environmental impacts, mitigate climate change, preserve biodiversity, optimise consumption of natural resources such as water, prevent pollution and promote continuous improvement, going beyond the stipulations of applicable laws.

Measures continued to make energy development compatible with environmental protection. General activities included the promotion of continuous improvement by updating and extending environmental management, involving our suppliers and encouraging our customers to use energy responsibly.

This is achieved through environmental management of Gas Natural Fenosa based on the ISO 14001 model, the correct functioning of which is verified periodically, providing the tools required to assure environmental management. In 2016, certification was obtained for the environmental management system applied to electricity distribution in Chile. Along similar lines, progress was made in the process to adapt environmental management of rest of the Chilean activities to ensure consistency with the rest of the company.

Gas Natural Fenosa's positioning in relation to climate change is based on its contribution to climate change mitigation by using low-carbon and renewable energies, promoting energy saving and efficiency, applying new technologies and capturing carbon in the Group's projects. During 2016 there have been significant reductions in direct CO₂ emissions with respect to 2015, as a result of lower production in coal generation in Spain which has been replaced by cleaner generation options. As a result, specific emission per unit of energy generated was significantly reduced compared with 2015. There was also a reduction in emissions of other substances due to lower thermal generation in Spain.

In 2016, Gas Natural Fenosa undertook numerous actions to promote the conservation of biodiversity, some in response to requirements implemented by environmental authorities and others voluntarily. During this period, the initial steps have been taken to implement biodiversity action plans and highly significant progress has been made in the creation of tools to support the company's biodiversity strategy.

Gas Natural Fenosa is aware of the essential role played by water in the production process; as part of its ongoing commitment to the environment and to the efficient management of natural resources, in 2016 progress was made in its water strategy by determining management indicators and lines of action to optimise water use in the most significant production processes. Within the commitment towards the environment and the efficient management of natural resources, during 2016 Gas Natural Fenosa started work on bringing together, in 2017, the lines of action in the circular economy area on which it has been working for some time.

The environmental activities undertaken in 2016 amounted to Euros 7 million, relating to the costs of environmental management at facilities (Euros 12 million related to environmental management at facilities in 2015).

Possible contingencies, indemnities and other environmental-related risks in which Gas Natural Fenosa could be incur are adequately covered by subscribed liability insurance policies.

Note 32. Subsequent events

On 11 January 2017 Gas Natural Fenosa Finance, B.V., through its Euro Medium Term Notes (EMTN) programme, for which the Company acts as guarantor, carried out a bond issue amounting to Euros 1,000 million, maturing in January 2027 with an annual coupon of 1.375%.

Appendix I. Gas Natural tax group companies.
The companies in the Gas Natural tax group are as follows:

Gas Natural SDG, S.A.	Gas Natural Redes Distribución Gas SDG, S.A.
Ampliación de Nerea, S.L.U.	Gas Natural Redes GLP, S.A.
Banteay Srei, S.L.U.	Gas Natural Rioja, S.A.
Boreas Eólica 2, S.A.	Gas Natural S.U.R. SDG, S.A.
Compañía Española de Industrias Electroquímicas, S.A.	Gas Natural Servicios SDG, S.A.
Energías Ambientales de Somozas, S.A.	Gas Natural Transporte SDG, S.L.
Energías Especiales Alcohólicas, S.A.	Gas Natural Wind 4, S.L.U.
Energías Especiales De Extremadura, S.L.	Gas Navarra, S.A.
Eólica La Vega I, S.L.U.	Gecal Renovables, S.A.
Eólica La Vega II, S.L.U.	General de Edificios y Solares, S.L.
Estela Eólica, S.L.U.	Genroque, S.L.U.
Europe Maghreb Pipeline Limited	Global Power Generation, S.A.
Explotaciones Eólicas Sierra de Utrera, S.L.	Holding Negocios Regulados Gas Natural, S.A.
Fenosa Wind, S.L.	JGC Cogeneración Daimiel, S.L.
Fenosa, S.L.U.	La Energía, S.A.
Gas Directo, S.A.U.	La Propagadora del Gas Latam, S.L.U.
Gas Natural Almacenamiento Andalucía, S.A.	La Propagadora del Gas, S.A.
Gas Natural Andalucía, S.A.	Lanzagorta Comunicaciones, S.L.
Gas Natural Aprovisionamientos SDG, S.A.	Lignitos de Meirama, S.A.
Gas Natural Aragón SDG, S.A.	Operación y Mantenimiento Energy, S.A.
Gas Natural Balears, S.A.	Parque Eólico Cova Da Serpe, S.L.U.
Gas Natural Capital Markets, S.A.	Parque Eólico La Rabia, S.L.U.
Gas Natural Castilla La Mancha, S.A.	Parque Eólico Las Claras, S.L.U.
Gas Natural Castilla y León, S.A.	Parque Eólico El Hierro, S.L.
Gas Natural Catalunya SDG, S.A.	Parque Eólico Los Pedreros, S.L.
Gas Natural Cegas, S.A.	Parque Eólico Montamarta, S.L.
Gas Natural Comercializadora, S.A.	Parque Eólico Nerea, S.L.
Gas Natural Distribución Latinoamérica, S.A.	Parque Eólico Peñaroldana, S.L.
Gas Natural Exploración, S.L.	Petroleum Oil & Gas España, S.A.
Gas Natural Fenosa Electricidad Colombia, S.L.	Sagane, S.A.
Gas Natural Fenosa Engineering, S.L.	Sociedad de Tratamiento Hornillos, S.L.
Gas Natural Fenosa Generación Nuclear, S.L.	Societat Eòlica de L'Enderrocada, S.A.
Gas Natural Fenosa Generación, S.L.U.	Tratamiento Almazán, S.L.
Gas Natural Fenosa Ingeniería y Desarrollo de Generación, S.L.U.	Tratamiento Cinca Medio, S.L.
Gas Natural Fenosa Internacional, S.A.	Unión Fenosa Distribución, S.A.
Gas Natural Fenosa LNG, S.L.	Unión Fenosa Financiación, S.A.
Gas Natural Fenosa Renovables, S.L.U.	Unión Fenosa Minería, S.A.
Gas Natural Informática, S.A.	Unión Fenosa Preferentes, S.A.U.
Gas Natural Madrid SDG, S.A.	



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Director's Report



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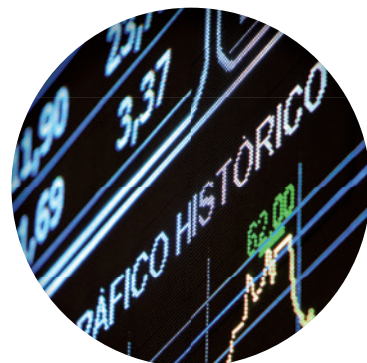
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1. Company situation

Gas Natural Fenosa's business model is characterised by responsible and sustainable management of all resources. Our commitment to sustainability and value creation over time is reflected specifically in our corporate responsibility policy, approved by the Board of Directors and implemented across all the Company's business processes; it comprises seven corporate responsibility commitments to stakeholders, which guide our activities: commitment to results, customer orientation, environmental protection, concern for people, health and safety, commitment to society and integrity.

Gas Natural Fenosa is an integrated energy company that supplies gas and electricity to almost 22 million customers. Its main purpose is to supply energy to society so as to maximise development and welfare, using innovation, energy efficiency and sustainability as the fundamental pillars of the business model. It is a leading energy company and a pioneer in the integration of gas and electricity. The business focuses on the full gas life cycle and on electricity generation, distribution and supply. There are other business lines, such as energy services, that favour diversification of activities and revenues, anticipating new market trends, meeting specific customer needs and providing an integrated service not focused only on selling energy.

Gas Natural Fenosa's business model is implemented through a large number of companies, basically in Spain, the rest of Europe, Latin America and Africa; there are four major business areas:

> **Gas distribution (Spain, rest of Europe and Latin America)**

Gas Natural Fenosa has a leading position in the markets in which it operates, allowing organic growth opportunities to be leveraged both by winning new customers in municipalities to which gas is supplied and by expanding networks into zones without a gas supply. It is the leader in Spain and has a solid presence in Italy. It is also the leader in Latin America, with a presence in Mexico, Chile, Colombia, Brazil, Argentina and Peru.

> **Electricity distribution (Spain, rest of Europe and Latin America)**

Gas Natural Fenosa is one of the most efficient operators in terms of operating and maintenance costs in electricity distribution. It is the third-ranked operator in the Spanish market and the leader in Moldova. In Latin America, it operates in Chile, Argentina, Panama and Colombia.

> **Gas (Infrastructures, Supply and Unión Fenosa Gas)**

Gas Natural Fenosa has a unique, integrated gas infrastructure that provides considerable business stability, operational flexibility and the capacity to transport gas towards the best business opportunities.

For Gas Natural Fenosa, our suppliers play a critical role in the optimal functioning of the value chain; accordingly, long-term contracts are concluded, a commitment to society is assumed and environmental impacts are minimised so as to guarantee supply.

Gas Natural Fenosa responds with value-added services to customers' demands for speed, guarantees, quality and energy efficiency.

> **Electricity (Spain and International)**

Gas Natural Fenosa has broad knowledge of all power generation technologies and an infrastructure that can be tailored to the needs of any energy model and each country's circumstances. A competitive, flexible gas supply allows the Company to achieve better margins than its competitors when managing combined cycle plants.

Our leading position in the combined retailing of natural gas and electricity brings major advantages, such as a lower service cost, integrated customer service and lower acquisition costs, as well as greater proximity to customers.

In the international market, Gas Natural Fenosa, through Global Power Generation, is established in Mexico, Puerto Rico, the Dominican Republic, Costa Rica, Panama, Kenya, Australia and, most recently, Chile and Brazil.

Our operations throughout the gas value chain provide Gas Natural Fenosa with a competitive advantage and a leading position in the sector. Our electricity management capacity and experience, combined with a unique integrated position in the gas and electricity markets, make the company a benchmark in this sector. International presence guarantees a privileged position to achieve growth in new regions that are in the process of economic development, making the Company one of the world's leading operators.

Appendix I to the Consolidated Annual Accounts contains a list of Gas Natural Fenosa's investees.

1.1. Corporate governance

Gas Natural Fenosa develops and continuously updates its corporate governance rules, which are formed by:

- > Company By-laws.
- > General Shareholders' Meeting Regulations.
- > Board of Directors and Board Committee Regulations.
- > Internal Code of Conduct with regard to the Securities Markets.
- > Code of Ethics.
- > Corporate Responsibility Policy.

Gas Natural Fenosa has continued to enhance its commitment to transparency and good practices, with the participation of the General Shareholders' Meeting, the Board of Directors and the Board committees: Executive Committee, Appointments and Remuneration Committee, and Audit Committee. The Management Committee also plays a significant role. In 2015, Gas Natural Fenosa adapted its corporate governance rules to the requirements of Act 31/2014, 3 December, which amended the Spanish Companies Act 2010 to improve corporate governance, and to the new the recommendations of the corporate governance code for listed companies of February 2015.

The accompanying 2016 Annual Corporate Governance Report contains a more detailed description.

The Board of Directors represents the Company and is Gas Natural Fenosa's ultimate decision-taking body, except for decisions reserved for the General Meeting. In particular, the Board is responsible for the following matters:

- > Determining strategy and economic objectives.
- > Supervising and verifying that the top executives fulfill the strategies and objectives.
- > Assuring the company's future viability and competitiveness.
- > Approving codes of conduct.

The Executive Committee is the Board committee responsible for continuous monitoring of Company management.

The Appointments and Remuneration Committee proposes Board remuneration criteria and general management remuneration policies. It also reviews the Board's structure and composition, supervising the appointment of new members and establishing guidelines for the appointment of directors.

The Audit Committee supervises internal control and risk management systems and evaluates their effectiveness, and also oversees the preparation of financial information and internal audit services.

The Management Committee coordinates business and corporate areas. Its main functions include studying and proposing Objectives, the Strategic Plan and the Annual Budget, as well as assessing, for the main Governing Bodies, action proposals that could affect the fulfilment of the Company's Strategic Plan. All the Management Committee members participate in the preparation of the Corporate Risk Map through work meetings in which they express opinions on the main uncertainties and potential impacts on the businesses.

2. Business evolution and results

The main financial aggregates of Gas Natural SDG and their performance are as follows:

	2016	2015	%
Net turnover	5,062	5,640	(10.2)
Operating profit	1,617	1,597	1.3
Profit for the year	1,067	1,024	4.2
Shareholders' equity	13,431	13,298	1.0
Net equity	13,444	13,285	1.2
Current liabilities	3,597	3,780	(4.8)
Average period for payment to suppliers	22 days	24 days	-

Gas Natural SDG, S.A., is a company that develops its activity basically through the tendency of other group and associated companies shares, so information below refers to de Consolidated group of Gas Natural Fenosa.

2.1. Main milestones in 2016

Net profit amounted to Euros 1,347 million in 2016, 10.3% less than in 2015.

EBITDA amounted to Euros 4,970 million in 2016, 5.6% less than in 2015, after discontinuation of the liquefied petroleum gas business in Chile; these results were affected by a very demanding macroeconomic and energy situation. This situation had a particular impact on the contribution by the gas supply business, while the depreciation of Latin American currencies on translation to euro impacted EBITDA in the amount of Euros 112 million, mainly attributable to the Colombian peso and the Mexican peso.

As of 31 December 2016, the indebtedness ratio was 44.8%, i.e. lower than at 2015 year-end (45.8%), and the net financial debt/EBITDA ratio was 3.1, compared with 3.0 at the end of 2015, despite bringing forward the 2016 interim dividend.

The sale of a 20.0% stake in GNL Quintero, S.A. (Chile) to Enagas for Euros 182 million by Aproveionadora Global de Energía, S.A. (AGESA), a subsidiary of Gas Natural Chile, S.A., was completed in November 2016, providing Euros 128 million in capital gains before taxes and non-controlling interests (Euros 50 million net capital gains).

On 14 November 2016, the Superintendence for Residential Public Services of the Republic of Colombia ("the Superintendence") ordered, as a necessary measure to ensure the provision of electrical energy services, the seizure of the goods, assets and businesses of Electricaribe. The Superintendence also ordered the removal of the members of the governing body and the general manager, and their replacement by a special agent appointed by the Superintendence. In the fulfilment of his functions, this agent has replaced the executive personnel appointed by Gas Natural Fenosa and has centralised decision-making on the information to be supplied to Gas Natural Fenosa. Therefore, at 31 December 2016, Gas Natural Fenosa had lost control and any significant influence over Electricaribe as it does not take part in, and has no direct information about, material business activities or decisions. Subsequently, on 11 January 2017, the Superintendence extended this government take-over until 14 March 2017. In the light of the above facts and in accordance with IFRS 10, on 31 December 2016, Electricaribe ceased to be consolidated on the consolidated balance sheet of Gas Natural Fenosa, and its assets, liabilities and non-controlling interests have been derecognised for a net amount of Euros 475 million. In addition, the investment in Electricaribe has been recorded at fair value as defined by IAS 39 (Euros 475 million) under Available-for-sale financial assets.

Gas Natural Fenosa confirms its guidance for net profit for 2017 to be between Euros 1,300 million and Euros 1,400 million, as well as the continuity of its dividend policy in accordance with the Strategic Vision 2016 - 2020.

The Board of Directors will propose to the Ordinary Shareholders' Meeting that it allocate Euros 1,001 million out of 2016 income to dividends, i.e. the same as in the previous year, in line with the new dividend policy for 2016-18, which was approved in March 2016. The interim dividend of Euros 0.330 per share was paid in full in cash on 27 September 2016, and the supplementary dividend amounting to Euros 0.670 per share will also be paid in cash in June 2017, representing a payout of 74.3%.

2.2. Main aggregates

Gas Natural Fenosa's financial information contains magnitudes and measurements prepared in accordance with the International Financial Reporting Standards (IFRS), as well as others prepared in accordance with the Group's own reporting model, referred to as Alternative Performance Metrics (APM), which are considered to be adjusted magnitudes with respect to those presented in accordance with IFRS. In the last chapter of the Consolidated Directors' Report there is a glossary of terms and the definitions of the APMs.

Financial main aggregates

	2016	2015	%
Net sales	23,184	26,015	(10.9)
Ebitda	4,970	5,264	(5.6)
Operating income	3,006	3,261	(7.8)
Net income attributable to equity holders of the Company	1,347	1,502	(10.3)
Cash flows from operating activities	3,375	3,500	(3.6)
Investments	2,225	1,422	56.5
Net equity (at 31/12)	19,005	18,518	2.6
Attributed net equity (at 31/12)	15,225	14,367	6.0
Net borrowings (at 31/12)	15,423	15,648	(1.4)

Main financial ratios

	2016	2015
Leverage (%)	44.8	45.8
EBITDA / Net financial expenses	6.7x	6.4x
Net borrowings / EBITDA	3.1x	3.0x
Liquidity ratio	1.1x	1.2x
Solvency ratio	1.0x	1.0x
Return on equity (ROE) (%)	8.8	10.5
Return on assets (ROA) (%)	2.9	3.1

Main stock market ratios and shareholder remuneration

	2016	2015
Average number of shares (thousand)	1,000,468	1,000,689
Share price at 31/12 (euro)	17.91	18.82
Stock market capitalisation at 31/12 (million euro)	17,922	18,828
Earnings per share (euro) ¹	1.35	1.57
Attributable equity per share (euro)	15.21	14.36
Price-earnings ratio (P/E)	13.3	12.5
EV/ Ebitda	6.7	6.5

¹ Profit at 31 December 2015 adjusted in accordance with IAS 33 due to the carrying amount of the preference shares exceeding the amount paid to redeem them, net of the tax effect.

Main physical aggregates

	2016	2015	%
Gas distribution:			
Sales-TPA ¹ :	458,265	473,831	(3.3)
Europe	188,197	181,212	3.9
Latin America	270,068	292,619	(7.7)
Gas distribution connections points (thousand) (at 31/12):	13,546	13,172	2.8
Europe	5,773	5,724	0.9
Latin America	7,773	7,448	4.4
Electricity distribution:			
Sales-TPA ¹ :	68,258	68,731	(0.7)
Europe	34,697	34,676	0.1
Latin America*	33,561	34,055	(1.5)
Electricity distribution connections (thousand) (at 31/12):	8,202	10,622	(22.8)
Europe	4,580	4,550	0.7
Latin America	3,622	6,072	(40.3)
ICEIT ² (minutes)	43	44	(2.3)

* Figures for Colombia are as of 30/11/2016 since the December data are not available.

¹ Third-Party Access (energy distributed).

² Installed capacity equivalent interruption time in Spain.

Main physical aggregates (continuation)

	2016	2015	%
Gas:			
Gas supply (MW):	325,384	316,268	2.9
Spain	178,916	185,851	(3.7)
Rest of Europe	77,136	54,787	40.8
LNG International	69,332	75,630	(8.3)
Gas transportation – EMPL (MW)	111,720	112,861	(1.0)
Electricity:			
Electricity generated (GWh):	46,552	49,548	(6.0)
Spain:	28,504	31,568	(9.7)
Hydroelectric	3,933	2,457	60.1
Nuclear	4,463	4,544	(1.8)
Coal	5,687	7,973	(28.7)
CCGTs	11,963	14,494	(17.5)
Renewables and Cogeneration	2,458	2,100	17.0
Global Power Generation:	18,048	17,980	0.4
Hydroelectric	496	481	3.1
CCGTs	15,648	15,519	0.8
Oil-gas	1,111	1,130	(1.7)
Wind	793	850	(6.7)
Installed capacity (MW):	15,418	15,471	(0.3)
Spain:	12,716	12,769	(0.4)
Hydroelectric	1,954	1,954	–
Nuclear	604	604	–
Coal	2,010	2,065	(2.7)
CCGTs	7,001	7,001	–
Renewables and Cogeneration	1,147	1,145	0.2
Global Power Generation:	2,702	2,702	–
Hydroelectric	123	123	–
CCGTs	2,035	2,035	–
Oil-gas	310	310	–
Wind	234	234	–
Electricity supply (GWh)	36,384	35,241	3.2

3. Sustainability

3.1. Environment

Main aggregates

	2016	2015	% Var.
Zero emissions installed capacity (%)	22.1	22.0	0.4
Zero emissions net production (%)	16.4	11.8	39.1
Direct GHG emissions ¹ (Mt CO ₂ eq.)	19.5	22.4	(12.9)
CO ₂ emissions/electricity production (t CO ₂ /GWh)	411	445	(7.6)
Methane emissions in gas distribution (t CO ₂ eq./km network)	9.3	9.3	–
Environmentally certified activities (% of environmentally certified EBITDA/total Group EBITDA potentially certifiable) ²	90.1	88.3	(2.0)

¹ Scope 1 direct greenhouse gas emissions in accordance with "The Greenhouse Gas Protocol. A Corporate accounting and reporting standard".

² Approximately 86.8% of Group EBITDA is potentially certifiable.

Gas Natural Fenosa works to ensure compliance with environmental legislation, reduce environmental impact, mitigate climate change, optimise the consumption of natural resources such as water, preserve biodiversity in the environment, prevent pollution and foster continuous improvement, going beyond the legal requirements.

In 2016, new environmental management systems were certified in accordance with ISO 14001 and internal requirements, and there was a slight increase in the percentage of EBITDA certified as a result of the addition of part of the Chilean electricity distribution business. The work to adapt environmental management systems and certify them to international standards and internal requirements will conclude in 2017.

Regarding climate change, there was a significant reduction in direct CO₂ emissions with respect to 2015 as a result of lower coal-fired output in Spain, replaced by less polluting output. As a result, specific emissions per unit of power generated were reduced considerably with respect to 2015.

In 2016, Gas Natural Fenosa carried out numerous and varied activities in favour of conserving biodiversity, many of which have gone beyond the requirements set by the environmental authorities and others are voluntary in nature.

As part of its commitment to the environment and to efficient management of natural resources, in 2016 Gas Natural Fenosa made progress with its water strategy and commenced work to define lines of action in connection with the circular economy in 2017.

Note 36 to the annual accounts contains other relevant information on the main environmental and sustainability activities, emissions and environmental investments.

3.2. People

Main aggregates

Employment indicators	2016	2015	% Var.
Number of employees at 31/12	17,229	19,939	(13.6)
Voluntary turnover rate (%)	2.5	3.5	(28.6)
Integration rate (persons with disabilities) ¹	2.4	2.4	–
Employee training hours	50.9	61.4	(17.1)
Absenteeism	2.2	2.0	10.0
Days lost	2,424	3,674	(34.0)
Number of accidents resulting in days lost	65	125	(48.0)

¹ Spain.

Human and social development

Gas Natural Fenosa provides stable and quality employment (96% of positions are indefinite) and a solid, structured and appealing professional career.

During 2016, the implementation of the Human and Social Development project continued, the main objective of which is to promote a quality work environment based on respect, diversity and personal and professional development. Through this project, a number of programmes have been promoted and coordinated on the basis of two essential pillars: equality of opportunities, and training as a lever to raise internal awareness about disability.

Gas Natural Fenosa has a common global model for personnel selection for all the geographies in which it operates. This ensures that it applies uniform approach as an employer, using standard criteria and best practices in identifying, attracting and retaining the professional talent necessary to carry on its business.

Gas Natural Fenosa continues to offer all employees the opportunity to participate in the internal mobility programme. Through this programme, employees can apply for any vacant position in any location, irrespective of where the employee's work place is located. This is one of the main components for enhancing career development within the company. To ascertain employees' preferences and concerns in connection with mobility, work continues on the "Conocerte" project. This initiative, which commenced in 2015, has helped to provide individual and centralised information for the entire Company. Aimed at technical professionals not include in executive programmes or the Savia programme, the initiative gathered information about 10,000 employees in 15 countries.

Ethical behaviour, promoting and respecting equality, and occupational health and safety are essential parts of the commitment made by Gas Natural Fenosa to its employees.

These principles are reflected in the company's day-to-day performance through the Code of Ethics, the II Collective Agreement, the Equality Plan and the Protocol for the Prevention of Workplace, Sexual and Gender-based Harassment.

In 2016, progress was made on the implementation of equality and diversity actions for employees, with the design of a Comprehensive Diversity Plan focused on gender, age and disability.

Concerning disability, the Capacitas and Aflora programmes aimed at normalising the professional integration of professionals with disability. Since implementation of these two projects commenced, a total of 156 persons with special needs have received aid relating to employment in Spain, i.e. over 87% of employees with disabilities have availed themselves of these programmes. Gas Natural Fenosa renewed the Bequal Plus Seal in recognition of our inclusion policy as a pioneer in disability commitment within the energy industry.

Gas Natural Fenosa promotes work-life balance through a major set of labour flexibility measures, services and benefits adapted to employees' needs. Our professionals can thus design their own life options in line with their development plans and the company's interests.

Training and talent management

Talent management at Gas Natural Fenosa's is centred on employees' individual development and professional careers, helping to define professional learning in a controlled and consistent manner to ensure that their development is aligned with the company's objectives.

The leadership and talent management model seeks to foster responsibility as well as individual and career development by using innovative tools and methodologies in training and development.

The model was simplified in 2016 to make it more accessible to all employees, the goal being to have a single, homogeneous, standardised model for professional evaluation and development.

The Talent Management and Corporate University unit is responsible for the development of Gas Natural Fenosa's professionals on all organisational levels and for knowledge management in all areas of the company. Training is a success factor for the company since our employees are the ones who achieve business objectives and drive our corporate strategies.

The Corporate University has a network of alliances with academic institutions in Spain and other countries. The Advisory Board, comprising the Polytechnic Universities of Barcelona and Madrid, the Monterrey Institute of Technology, IESE, ESADE and Boston Consulting Group, with the internal units of Gas Natural Fenosa, ensure a permanent link between the company's strategy and the programmes that are implemented.

Gas Natural Fenosa has established itself as a leader in health and safety following the implementation in 2012 of an ambitious "Health and Safety Commitment Plan" aimed at achieving a profound cultural change. The Corporate University has contributed to this process through a related training scheme, under which 100% of the company's employees have been trained.

Remuneration

Gas Natural Fenosa's remuneration policy is guided by the principles of internal equality and competitiveness in the market. Employees' remuneration depends on whether or not they are covered by the Collective Agreement.

The salary levels of employees covered by the Collective Agreement are based on the professional group and sub-group to which they belong.

For those not covered, salaries are defined individually, in line with the Company's remuneration policy.

Variable remuneration under Gas Natural Fenosa's remuneration policy is designed to promote employee commitment and motivate performance, in line with the long-term interests of the Company and its shareholders.

Annual variable remuneration rewards the achievement of individual targets depending on the position, applying financial, efficiency and growth variables, as well as on quality and security issues, directly related to the fulfilment of the objectives proposed in the Management by Objectives Plan.

Management by Objectives and Commercial Variable Remuneration are methodologies deployed in Gas Natural Fenosa to encourage employee involvement in achieving the objectives of the company and their direct participation in results. Both are arranged through two types of Annual Variable Remuneration, depending on the group addressed:

- > Management: based on management by objectives and performance appraisal. Applies to management personnel not covered by the Collective Agreement.
- > Commercial: based on the fulfilment of commercial objectives. Aimed at employees with commercial functions.

The compensation package for employees of Gas Natural Fenosa is complemented by a benefits system which includes the pension plan, the main vehicle for funding post-employment commitments.

Furthermore, Gas Natural Fenosa offers a range of social benefits that complement the employees' remuneration package. The "Mis Beneficios" (My Benefits) platform for the workforce in Spain went live in 2016; it provides a single, comprehensive solution for managing and communicating compensation and benefits programmes. The platform continues to be developed to adapt to the various compensation and benefits strategies.

It includes such modules as: "Sistema de previsión social" to help employees understand their retirement and be aware of the Company's retirement plans, and "Bienestar y Salud", which enables employees to manage their well-being and health related plans.

All personnel in Spain also have a flexible remuneration system, which was implemented in 2012. The system enables beneficiaries to design the composition of their compensation package by combining a range of products on offer.

Personnel structure

Note 25 to the Consolidated Annual Accounts provides a breakdown of personnel by category, gender and geographic area at 31 December.

3.3. Taxation

Tax policies and tax risk management

Gas Natural Fenosa's tax policies are aligned with the Gas Natural Fenosa Corporate Responsibility Policy, which establishes as one of the commitments and principles of action to "act responsibly in managing business and comply with tax obligations in all the jurisdictions in which the company operates, assuming the commitment to transparency and collaborate with the relevant tax authorities."

To this end, since 2010 Gas Natural Fenosa has adhered to the "Code of Best Tax Practices" drawn up by the Large Companies Forum in conjunction with the Spanish tax authorities. This initiative, supported by the Spanish government, aims to promote transparency, good faith and cooperation with the tax authorities in business tax practices, and legal certainty in the application and interpretation of tax regulations

In this respect, the company has expressly undertaken to: (a) avoid opaque structures for tax purposes, (b) collaborate with the tax authorities, (c) regularly report on tax policies to the Board of Directors, and (d) apply tax criteria in line with administrative pronouncements and case law.

To ensure that the tax practices of Gas Natural Fenosa are based on these principles, the group has a General Procedure governing Best Practices in the area of Tax.

In addition, Gas Natural Fenosa has a risk map specifically identifying tax risks and disputes concerning the interpretation and application of tax law. Information on the main tax-related actions is disclosed in Note 21 (Tax Situation) to the consolidated annual accounts.

The tax repercussions of any material or unique transactions are reported to the Board of Directors when they are deemed to be material. The creation or acquisition of holdings in entities domiciled in designated tax havens must be reported to the Board of Directors through the Audit Committee.

On the basis of Spanish legislation concerning countries classified as tax havens (Royal Decree 1080/1991, of 5 July, and Royal Decree 116/2003, of 31 January), Gas Natural Fenosa has interests in only two companies incorporated in such territories:

- 95.0% of Buenergía Gas & Power, Ltd., domiciled in the Cayman Islands. This company indirectly owns only one industrial holding, in a company that engages in power generation by means of a combined cycle gas turbine plant in Puerto Rico (Ecoeléctrica, L.P), whose income is taxed in that country and which does not provide Gas Natural Fenosa with any tax benefits.
- 52.2% of Gasoducto del Pacífico (Cayman), Ltd., domiciled in the Cayman Islands. This company, which is dormant, was acquired by the Group as a consequence of the acquisition of the CGE group and does not provide any tax advantage for Gas Natural Fenosa.

In 2016, the domicile of the 47.5% holding in Ecoeléctrica Holding, Ltd. and the 47.5% holding in Ecoeléctrica Limited was changed from the Cayman Islands to Puerto Rico; accordingly, they have ceased to be classified as holdings in tax havens.

Intragroup transactions with these entities relate to dividends received, as follows:

Receiving subsidiary	Distributing subsidiary	Amount (thousand Euros)
Global Power Generation, S.A.	Buenergía Gas & Power, Ltd.	6,036

Tax contribution

Gas Natural Fenosa is aware of its responsibility for the economic development of the communities in which it conducts its business. The taxes it pays represent a significant part of the economic contribution made to the countries in which it operates. Therefore, Gas Natural Fenosa pays priority attention to fulfilling its obligation to pay taxes under the laws of each territory.

The taxes paid by Gas Natural Fenosa have considerable economic importance and involve a major compliance effort under formal obligations and cooperation with the tax authorities.

The total tax contribution of Gas Natural Fenosa amounted to Euros 3,423 million in 2016 (Euros 3,636 million in 2015). The following table details the taxes actually paid by Gas Natural Fenosa, by country, segmenting those that represent actual expenditure by the group (called group taxes) and those that are withheld or charged to the end taxpayer (called third-party taxes):

Country	Group taxes						Third-party taxes									
	Corporate income tax ¹		Others ²		Total		VAT		Tax on hydrocarbons		Others ³		Total		Total	
	2016	2015	2016	2015	2016	2015	2016	2015	2016	2015	2016	2015	2016	2015	2016	2015
Spain	199	347	512	549	711	896	1,007	1,169	352	362	229	200	1,588	1,731	2,299	2,627
Argentina	10	4	42	40	52	44	13	13	–	–	22	16	35	29	87	73
Brazil	38	51	49	44	87	95	58	56	–	–	9	18	67	74	154	169
Colombia	75	69	78	78	153	147	7	9	–	–	14	22	21	31	174	178
Chile	42	48	11	16	53	64	117	99	–	–	18	22	135	121	188	185
Mexico	31	33	3	4	34	37	39	32	–	–	11	12	50	44	84	81
Panama	89	8	7	11	96	19	–	–	–	–	3	4	3	4	99	23
Rest LatAm	12	11	1	1	13	12	2	3	–	–	3	2	5	5	18	17
Total LatAm	297	224	191	194	488	418	236	212	–	–	80	96	316	308	804	726
Italy	19	14	7	5	26	19	27	30	42	34	5	5	74	69	100	88
Rest	10	10	23	35	33	45	128	112	49	32	6	6	183	150	216	195
Total	525	595	733	783	1,258	1,378	1,398	1,523	443	428	320	307	2,161	2,258	3,419	3,636

¹ Corporate income tax actually paid during the year. Does not include accrued amounts. Information on the reconciliation between the recognised corporate income tax amount and the amount that would result from applying the nominal income tax rate currently prevailing in the country of the parent company (Spain) to pre-tax profits is detailed in Note 21 (Tax Situation) to the consolidated annual accounts.

² Includes energy taxes which in Spain amounted to Euros 244 million in 2016 (Euros 262 million in 2015), local taxes, employer social security contributions and other taxes specific to each country.

³ Basically includes employee income tax withholdings and employee social security contributions.

4. Main risks and uncertainties

4.1. Operating risks

4.1.1. Regulatory risk

Gas Natural Fenosa and its subsidiaries are required to comply with legislation governing the natural gas and electricity sectors. In particular, gas and electricity distribution are regulated activities in most of the countries in which Gas Natural Fenosa performs them.

Legislation applicable to the natural gas and electricity sectors in the countries in which Gas Natural Fenosa operates is generally revised on a regular basis by the competent authorities. Any amendments may affect the current remuneration system for regulated activities, adversely impacting Gas Natural Fenosa's business, profits, grants and financial position.

In the event that competent public or private bodies interpret or apply such regulations based on criteria that differ from those of Gas Natural Fenosa, its compliance might be questioned or appealed and, in the event that an infringement were proven, there might be a material adverse impact on Gas Natural Fenosa's business, prospects, profits, grants and financial position.

Regulatory risk management is founded on smooth communication between Gas Natural Fenosa and regulators. Additionally, in the course of its regulated activities, Gas Natural Fenosa ensures that its costs and investments are aligned with the rates of return recognised for each business.

4.1.2. Gas and electricity volume risk

Most purchases of natural gas and liquefied natural gas (LNG) are made under long-term contracts containing clauses whereby Gas Natural Fenosa is obligated to purchase certain annual volumes of gas ("take-or-pay" clauses). Under such contracts, even if Gas Natural Fenosa does not need to acquire the committed volume of gas at a given time, it is contractually obligated to pay for the minimum volume committed in the take-or-pay clauses.

The contracts stipulate gas volumes in line with Gas Natural Fenosa's estimated needs. However, actual needs may be below the volumes estimated when the contracts were arranged. In the event of significant departures from the estimates, Gas Natural Fenosa will be obligated to purchase a large volume of gas than is actually needed or, failing this, to pay for the minimum volume of gas committed, irrespective of whether or not it acquires the volume that exceeds its needs; this could have a significant adverse effect on Gas Natural Fenosa's operating costs.

In the electricity business, Gas Natural Fenosa's results are exposed to a reduction in the amount of electricity generated, which is shaped by trends in demand for electricity. Additionally, in view of the major role played by CCGT technology in Gas Natural Fenosa's generating fleet, the amount of power generated might be reduced because of the growing importance of power generation from renewable sources.

A decrease in volumes generated would increase uncertainty as regards the achievement of generation/supply objectives.

Gas Natural Fenosa manages contracts and assets on a globally integrated basis to optimise energy balances, enabling it to correct any deviation in the most profitable manner possible.

4.1.3. Operational risk

a) Insurable risks

Gas Natural Fenosa's activities are exposed to a variety of operational risks such as faults in the distribution network, in electricity generation facilities and in gas carriers, explosions, polluting emissions, toxic spillage, fire, adverse weather conditions, contractual breaches, sabotage or accidents affecting the gas distribution network or electricity generation assets, and other damage and force majeure circumstances that might cause bodily harm and/or material damage, affecting or destroying Gas Natural Fenosa's facilities or property. Events such as these, or similar events, are unforeseeable and may interrupt the supply of gas and generation of electricity. In such situations, although coverage is provided by risk insurance policies, such as policies covering loss of profit and material damage, Gas Natural Fenosa's financial situation and results could be affected to the extent that any losses are not insured, coverage is insufficient, or economic losses are generated due to coverage limits or an increase in the excess, as well as potential increases in premiums paid to insurers.

Gas Natural Fenosa might also have to respond to third-party claims for bodily harm and/or other damage caused in the ordinary course of business. Such claims could result in the payment of indemnities under legislation applicable in the countries in which Gas Natural Fenosa operates, which could have a material adverse impact on the business, prospects, financial position and results if the its third-party liability insurance policies not cover the amount of the indemnities.

Gas Natural Fenosa prepares continuous improvement plans to reduce the frequency and severity of potential incidents. Specific asset supervision units have been created to intensify preventive and predictive maintenance, among other measures. Additionally, our approach to insurance coverage is based on optimising the total cost of risk.

b) Image and reputation

Gas Natural Fenosa is exposed to opinions and perceptions of a variety of stakeholders. Such perceptions may be adversely impacted by events caused by the Company or by third parties over which the Company has little or no control, impacting its own reputation or that of the industry. Such impacts might cause medium-term financial damage by increasing regulatory demands or funding costs or by requiring additional expenditure to win customers.

Gas Natural Fenosa is engaged actively in identifying and monitoring potential reputational events and the stakeholders affected. Transparency also forms part of our communication policy.

c) Environment

Gas Natural Fenosa's activities are subject to extensive legislation on environmental protection.

Gas Natural Fenosa and its subsidiaries must comply strictly with extensive environmental protection regulations requiring, among other aspects, the preparation of environmental impact analyses, obtainment of authorisations, licences and permits, and fulfilment of certain requirements. Considerations include:

- > Environmental authorisations and licences might not be granted or might be revoked due to failure to comply with the attached conditions;
- > The regulatory framework or its interpretation by the authorities might be amended, resulting in higher costs or deadlines for compliance with the new requirements.

In order to mitigate this risk, Gas Natural Fenosa has adopted an integrated environmental management system and has emergency plans for facilities where there is a risk of accidents with an environmental impact. Specific insurance policies have also been arranged to cover this type of risks.

d) Climate change

Demand for electricity and natural gas is related to the weather. A significant part of gas consumption during the winter months is driven by electricity generation and space heating, while summer consumption depends basically on electricity generation for air conditioning. Gas Natural Fenosa's revenue and results from natural gas distribution and supply activities might be adversely affected in the event that the autumn months become warmer or winters become milder. Demand for electricity might also fall if summers become milder, due to a decline in demand for air conditioning. Additionally, hydroelectric generation plant utilisation depends on rainfall in the plant locations and might be affected by drought.

European policies and measures to combat climate change could affect Gas Natural Fenosa's results in the event that the competitiveness of the Company's generation mix is altered.

Gas Natural Fenosa forms part of a number of work groups at European level, enabling strategy to be adapted to new regulations in advance. Gas Natural Fenosa also forms part of clean development projects designed to reduce CO₂ emissions.

e) Geopolitical exposure

Gas Natural Fenosa has interests in countries with different political, economic and social environments; in this regard, two main areas are particularly relevant:

> Latin America

A large part of Gas Natural Fenosa's operating profits are generated by its Latin American subsidiaries. Latin American operations are exposed to a number of risks inherent in investment in this region. Risk factors linked to investment and business in Latin America include:

- Considerable influence of local governments on the economy;
- Significant fluctuation in the economic growth rate;
- High inflation;
- Devaluation, depreciation or overvaluation of local currencies;
- Controls or restrictions on the repatriation of earnings;
- Fluctuating interest rates;
- Changes in financial, economic and fiscal policies;
- Unexpected changes to regulatory frameworks;
- Social tensions and
- Political and macroeconomic instability.

> Middle East and Maghreb

Gas Natural Fenosa has both its own assets and major contracts for the supply of gas from various Maghreb countries and the Middle East, particularly Egypt. Political instability in the zone may result in physical damage to the assets of Gas Natural Fenosa's investee companies or the obstruction of the operations of those or other companies, interrupting the Group's gas supply.

Gas Natural Fenosa has a diversified portfolio both in the countries in which it carries on energy distribution activities (Latin America, Europe) and the countries that supply gas (Latin America, Africa, Middle East, Europe). Diversification minimises the risk of expropriation and of supply interruption due to the knock-on effect of political instability in neighbouring countries. Specific insurance policies have also been arranged for these risks.

4.2. Financial risks

Financial risks (interest rate, exchange rate, commodity price, credit and liquidity risk) are detailed in Note 17 to the Consolidated Annual Accounts.

On 23 June 2016, the United Kingdom voted to withdraw from the European Union ("Brexit"). Although the UK's withdrawal will be accompanied by a process of negotiation over a period of time that cannot be determined as yet, the decision has already had consequences in the capital and foreign exchange markets. Gas Natural Fenosa's exposure to Brexit risk is practically non-existent.

4.3. Main opportunities

Gas Natural Fenosa's main opportunities are as follows:

- > **Generation mix:** Gas Natural Fenosa's generating fleet, consisting mainly of CCGT facilities, has the necessary flexibility to adapt to different market circumstances; it is thus a valuable asset to leverage opportunities related to price and demand volume volatility in the gas and electricity markets.
- > **CO₂ market evolution:** The mechanisms proposed by the European Commission to increase the cost of emission rights are intended to discourage the use of the more polluting technologies so as to counteract climate change. In this context, Gas Natural Fenosa's plants would be more competitive than coal plants and opportunities could also arise in the emissions market.
- > **Natural gas and LNG procurement portfolio:** Management of gas pipelines, investment in plants and the fleet of gas carriers enable the Group to meet its business needs in a flexible, diversified manner, optimising its approach to different energy scenarios. Specifically, the fleet of gas carriers makes Gas Natural Fenosa one of the world's leading LNG operators and a principal in the Atlantic and Mediterranean.
- > **A balanced structural position in terms of businesses and geographies,** many with stable flows, irrespective of commodities prices, making it possible to take the maximum advantage of growth in energy demand and of new business opportunities in new markets.

5. Group outlook

5.1. Strategic priorities

In order to achieve its objectives, Gas Natural Fenosa defines medium-term strategies that are updated periodically to adapt to current and future circumstances, taking into consideration the specific features of each of the Company's business lines.

In May 2016, Gas Natural Fenosa presented its updated Strategic Vision 2016-2020, establishing the Group's strategic priorities for the period.

5.2. Financial priorities

The strategic priorities for the period 2016-2020 are based on a financial policy consistent with growth and dividend targets:

- > Strict financial discipline.
- > Sustained dividend growth based on sustainable cash flow (70% payout commitment).
- > Execute the efficiency plan.
- > Manage the business portfolio.
- > Maintain a solid business model with regulated or contracted activities accounting for approximately 70% of EBITDA and more than 80% of future capital expenditure.

The strategic objectives for 2018 are detailed below (Euros billion):

	2018 targets
Ebitda	~ 5,4
Net profit	~ 1,6
Dividend (Pay-out)	~ 70%
Net debt/ebitda	~ 3,0x

5.3. Group outlook

The updated Strategic Vision 2016-2020 is based on three lines of growth (networks, power generation, and supply) that will enable Gas Natural Fenosa to continue expanding in the future:

- > **Networks:** in gas networks, the investment in gas networks in Chile, Mexico and Colombia, the entry into the distribution business in the region of Arequipa in Peru, new licences, and additional growth derived from the conversion of the newly-acquired LPG distribution points in Spain; in electricity networks, investment in smart grids in Spain, investments to meet the additional demand in Chile and Panama, and electricity subtransmission in Chile driven by new renewable energy facilities.
- > **Electricity generation:** improve the efficiency and performance of the generating fleet by adding 3,500 MW overall, of which 2,500 MW renewable (Spain and International) and 500-1,000 MW CCGTs that will contribute to the downstream development of the LNG business. Growth and development of the international power generation business through GPG.

- Gas supply: new gas supply contracts totalling approximately 11 bcm relating to the two Cheniere projects (Sabine Pass and Corpus Christi), the Yamal LNG project in Russia, and the Shah Deniz II project in Azerbaijan; additionally, existing gas supply contracts will be adapted and renegotiated to reflect benchmark market conditions. The gas carrier fleet will be expanded by adding four new carriers (two of which were added in 2016) and a mobile regasification unit. That expansion will increase capacity by almost one million cubic metres EBITDA is expected to increase by about 10%.

As a result, Gas Natural Fenosa is expected to maintain its organic growth trend in 2017 and beyond.

6. R&D and innovation

Innovation is one of the drivers of Gas Natural Fenosa's development; consequently, senior management is implementing an innovation model as part of the Group's updated Strategic Vision 2016-2020.

This model consists of a vision and a focus on innovation, project management methodology and a strong innovation culture within the company to ensure the most appropriate response to a changing situation.

Investment in technological innovation is analysed below:

	2016	2015
Total investment (Euro million)	59.2	15.7

The innovation plan is structured through priority lines of action to help achieve the goals set out in the Strategic Plan. This plan structures innovation around five multidisciplinary networks and eight areas of technology: Power Generation, Networks, Customers, Liquefied Natural Gas (LNG) and Automation and information management.

➤ Power generation:

- Renewable energy: The company has a balanced generation mix that is able to respond appropriately to the demand for energy in the societies where it operates, and it always seeks the most environmentally-friendly generation technologies. Its priorities in this area include notably: developing new technologies to increase the percentage of renewable energy in its portfolio and integrate it into the power grid, and optimising the use of renewable facilities already in service, for example, by extending their useful lives or harnessing wind more efficiently.
- Hydroelectric power: Gas Natural Fenosa's main innovation activities in the area of hydroelectric power are conducted through the Centro Internacional de Excelencia Hidráulica (CIEH). That institution's mission is to promote and channel R&D and innovation initiatives to harness conventional and marine hydroelectric energy that can be scaled up for application at the company's facilities around the world.
- Storage: Innovation in the area of energy storage focuses primarily on storing electricity in batteries, both large installations that enhance power grid operations and small-scale facilities for distributed use.
- Thermoelectric generation: Gas Natural Fenosa is working on two main lines of innovation in this area: improving power plant performance and reducing emissions from power generation.

- **Networks:** The main challenge in gas grids is to optimise safety and durability, as well as to increase the degree of optimisation and improve interactions with customers. In electrical networks, it continues to devote considerable efforts to optimising the electricity distribution network, focusing particularly on workplace safety, environmental aspects and supply quality. The goal is for electricity networks to be increasingly more intelligent.
- **Customers:** In the recently-established Smart Client area of innovation, the company is focused on offering value-added products and services to different categories of end customer.
- **Liquefied Natural Gas (LNG):** The overall objective is to strengthen LNG transportation, storage and distribution infrastructure, at all levels, so as to promote its use as an alternative to petroleum derivatives and as a more environmentally-friendly propulsion solution for shipping.
- **Automation and information management** is a horizontal area that seeks to agglutinate existing projects so as to reap synergies and enhance outcomes.

7. Annual Corporate Governance Report

Attached as an Appendix to this Director's Report, and forming an integral part of it, is the Annual Corporate Governance Report for 2016, as required under article 526 of the Spanish Capital Companies Act.

8. Treasury shares

On 14 May 2015, the General Meeting of Shareholders authorised the Board of Directors, for a period of not more than five years, to purchase, for good and valuable consideration, fully paid-up Company shares on one or more occasions, up to a total maximum amount of 10% of the share capital or the maximum figure applicable under the legislation in force at the time of acquisition, provided that the shares acquired directly or indirectly plus those already held by the Company and its subsidiaries never exceed 10% of subscribed capital or such other limit as may be established by law.

The minimum and maximum purchase price is the share price listed on Spain's electronic market, plus or minus 5%.

The variations in the treasury shares of Gas Natural SDG, S.A. in 2016 and 2015 are as follows:

	Number of shares	Amounts in million euro	% Share Capital
At 1 January 2015	–	–	–
Acquisitions	2,899,180	58	0.3
Disposals	(2,899,180)	(58)	(0.3)
At 31 December 2015	–	–	–
Acquisitions	3,049,189	53	0.3
Disposals	(2,298,644)	(40)	(0.2)
At 31 December 2016	750,545	13	0,1

Transactions with own shares of Gas Natural Fenosa in 2016 resulted in a gain of Euros 0.4 million, recognised under "Other reserves" (a gain of Euros 2 million in 2015).

For complete information about treasury shares see Note 13 to the Consolidated Annual Accounts.

9. Events after the reporting date

Events after the reporting date are described in Note 38 to the Consolidated Annual Accounts.

A. Ownership structure

A.1 Complete the following table on the Company's share capital:

Date of last change	Share capital (€)	Number of shares	Number of voting rights
22/06/2012	1,000,689,341	1,000,689,341	1,000,689,341

Report if there are different classes of shares with different rights associated:

No

Class	Number of shares	Nominal value per share	Number of voting rights per unit	Different rights
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A.2 Detail the direct or indirect holders of significant shareholdings of the company at the close of the financial year, excluding the Board Members:

Name or corporate name of the shareholder	Number of direct voting rights	Indirect voting rights		% of total voting rights
		Direct holder of the interest	Number of voting rights	
Société Nationale pour la Recherche, la Production, le Transport, la Transformation et la Commercialisation	40,092,780		0	4.01
Repsol, S.A.	200,964,920		0	20.08
Fundacion Bancaria Caixa d'Estalvis i Pensions de Barcelona ("la Caixa")	0	Criteria Caixa, S.A.U.	244,557,521	24.44
		Caixabank, S.A.	208	0
Global Infrastructure Partners III	0	Gip III Canary 1, S.À R.L.	200,137,868	20.00

State the most significant changes in the shareholding structure that have occurred during the financial year:

Name or corporate name of the shareholder	Date of transaction	Descripción de la operación
Repsol, S.A.	21-09-2016	10% of capital stock has fallen
Criteria Caixa, S.A.U.	21-09-2016	10% of capital stock has fallen
Gip III Canary 1, S.À R.L.	21-09-2016	15% of capital stock has exceeded

A.3 Complete the following tables about members of the board of directors of the company who have voting rights attaching to shares of the company:

Name or corporate name of the director	Number of direct voting rights	Indirect voting rights		% of total voting rights
		Direct holder of the interest	Number of voting rights	
Mr. Isidro Fainé Casas	17,426			0.00
Mr. Josu Jon Imaz San Miguel	2,100			0.00
Mr. William Alan Woodburn	0			0.00
Mr. Rafael Villaseca Marco	13,055	Ravifa 2013, S.L. B66079922	8,917	0.00
Mr. Ramón Adell Ramón	5,000			0.00
Mr. Enrique Alcántara-García Irazoqui	8,339			0.00
Mr. Xabier Añoveros Trías de Bes	350			0.00
Mr. Marcelino Armenter Vidal	12,600			0.00
Mr. Mario Armero Montes	0			0.00
Mr. Francisco Belil Creixell	7,128			0.00
Mrs. Benita María Ferrero-Waldner	0			0.00
Mr. Alejandro García-Bragado Dalmau	0			0.00
Mrs. Cristina Garmendia Mendizábal	0			0.00
Mrs. Helena Herrero Starkie	0			0.00
Mr. Miguel Martínez San Martín	0			0.00
Mr. Rajaram Rao	0			0.00
Mr. Luís Suárez de Lezo Mantilla	18,156			0.00
% total voting rights held by the board of directors				0.00

Complete the following tables about members of the company's board of directors who hold rights to shares of the company:

A.4 State, if applicable, the family, commercial, contractual, or corporate relationships between significant shareholders, to the extent known to the company, unless they are immaterial or result from the ordinary course of business:

Related individual or company name	Type of relationship	Brief description
Fundacion Bancaria Caixa d'Estalvis i Pensions de Barcelona ("la Caixa")	Contractual and commercial	Commercial or corporate relationships between Fundació Bancaria Caixa d'Estalvis i Pensions de Barcelona (la Caixa) and Repsol, S.A. are expressed in the reports of these companies. Previous shareholders agreement was finished on September 21, 2016. See par. A.6.
Repsol, S.A.	Contractual and commercial	Commercial or corporate relationships between Fundació Bancaria Caixa d'Estalvis i Pensions de Barcelona (la Caixa) and Repsol, S.A. are expressed in the reports of these companies. Previous shareholders agreement was finished on September 21, 2016. See par. A.6.

A.5 State, if applicable, the commercial, contractual, or corporate relationships between significant shareholders and the company and/or its group, unless they are immaterial or result from the ordinary course of business:

Related individual or company name	Type of relationship	Brief description
Fundacion Bancaria Caixa d'Estalvis i Pensions de Barcelona ("la Caixa")	Commercial	Existing relationships derive from ordinary commercial traffic and are referred to in par. D.2 and in annual accounts.
Repsol, S.A.	Commercial	Existing relationships derive from ordinary commercial traffic and are referred to in par. D.2 and in annual accounts.
Société Nationale pour la Recherche, la Production, le Transport, la Transformation et la Commercialisation des Hydrocarbures	Commercial	Existing relationships derive from ordinary commercial traffic.

A.6 State whether any private (paracorporate) shareholders' agreements affecting the company pursuant to the provisions of sections 530 and 531 of the Companies Act (Ley de Sociedades de Capital) have been reported to the company. If so, briefly describe them and list the shareholders bound by the agreement:

Yes

Participants in the private shareholders' agreement	% of share capital affected	Brief description of the agreement
Criteria Caixa, S.A.U Repsol, S.A. Gip III Canary 1, S.À R.L.	64.52	Participants have agreed some commitments related to the Corporate Governance of the Company whose purpose is the composition of the Board of Directors and its Committees as detailed below.

State whether the company is aware of the existence of concerted actions among its shareholders. If so, briefly describe them:

No

Expressly state whether any of such agreements, arrangements, or concerted actions have been modified or terminated during the financial year:

According to the relevant facts published as a result of the Purchase Contract of shares dated 12 September 2016 between Repsol SA and Criteria Caixa SAU on the one hand and Gip III Canary 1, S.À RL on the other, Criteria Caixa and Repsol agreed to terminate the Agreement between them in relation to their participation in Gas Natural SDG, SA dated 11 January 2000, as amended on 16 May 2002, 16 December 2002 and 20 June 2003, under which both parties exercised joint control over Gas Natural SDG, SA. That termination was subject to the condition precedent to the actual transfer of the shares in question to Gip III Canary 1, S.À R.L, a circumstance which occurred on 21 September 2016.

Relevant facts Nos. 242611 and 242612, both dated September 12, 2016 and Nos. 242957 and 24963, both dated September 21, 2016.

As expressed in the aforementioned relevant facts, Repsol SA, Criteria Caixa SAU and Gip III Canary 1, S.À RL, as shareholders of the Company, agreed to exercise the rights inherent to their status as such with full autonomy and in the manner they deem most convenient at any time, stating that the agreement reached does not involve concerted action.

In this agreement, these companies assumed certain commitments related to the corporate governance of the Company. In particular, the companies committed to make their best efforts to ensure, to the extent legally possible: (i) That each one of them has a representation in the Board of Directors proportional to the percentage of its participation in the share capital; (ii) that the chairmanship of the Company is non-executive and corresponds to one of the Directors appointed by the party that has a stake in the Company's capital significantly higher than the rest, which is currently Criteria, and that there are two Vice-Presidents Non-executive directors who are employed by appointed Directors at the proposal of Repsol and GIP respectively, while the presidency is occupied by a director on a proposal from Criteria; (iii) that the Executive Committee be made up of 10 members, 2 appointed by Criteria (including, where appropriate, the Chairman of the Board), 2 by Repsol, 2 by GIP, 3 Independent Directors and 1 Executive Director; (iv) the Audit Committee has 7 members, 1 appointed by Criteria, 1 by Repsol, 1 by GIP and 4 by Independent Directors; (v) that the Appointments and Remuneration Committee is made up of five members, 1 appointed by Criteria, 1 by Repsol, 1 by GIP and 2 by Independent Directors and (vi) that in the event of changes in the total number of members of the Board of Directors of the Company or in the participation of the Parties in the Company's share capital, the Company shall adopt the necessary measures to adapt the composition of the Board of Directors So as to maintain the balance between the directors appointed by each of them in accordance with the principle of proportional representation.

A.7 State whether there is any individual or legal entity that exercises or may exercise control over the company pursuant to section 5 of the Securities Market Act (Ley del Mercado de Valores). If so, identify it:

No

A.8 Complete the following tables about the company's treasury shares:

As of year-end:

Number of direct shares	Number of indirect shares*	Total % of share capital
750,545	0	0.08%

*Through

Individual or company name of direct holder of the interest	Number of direct shares
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Explain any significant changes, pursuant to the provisions of Royal Decree 1362/2007, that have occurred during the financial year:

A.9 Describe the terms and conditions and the duration of the powers currently in force given by the shareholders to the board of directors in order to issue, repurchase, or transfer own shares of the company.

The General Shareholders' Meeting of May 14, 2015, in its fourteenth item on the Agenda, authorized the Board of Directors to agree on a period of not more than 5 years to acquire the shares of the Company, subject to the following conditions:

Fourteenth.- Authorization to the Board of Directors for the derivative acquisition of own shares, directly or through companies of the Gas Natural Sdg, SA Group, in the terms agreed by the General Meeting and with the legally established limits, without giving effect to the authorization Agreed by the Ordinary General Meeting of April 20, 2010.

Fourteenth 1.- Leave the authorization granted to the Board of Directors by the General Shareholders' Meeting held on April 20, 2010, in order to acquire shares of the Company for pecuniary interest, in the unused portion.

Fourteenth 2.- To authorize the Board of Directors so that, within a period not exceeding five years, it may acquire, for one or more times, for a consideration, up to a maximum of 10% of the capital stock or the maximum amount resulting from application in accordance with current legislation at the time of acquisition, shares of the Company that are fully paid up, without the nominal value of shares acquired directly or indirectly, in addition to those already held by the Company and its subsidiaries exceeding 10% of the subscribed capital, or any other legally established. The minimum and maximum purchase price will be the quotation on the Spanish stock exchanges' Continuous Market with an oscillation of more or less than 5%.

In the event that the shares are not listed, the maximum and minimum acquisition price will be indicated between one-half and two times the book value of the shares, in accordance with the latest audited consolidated balance sheet. The Board of Directors is empowered to delegate this authorization to the Executive Committee or to the person or persons it deems convenient. This authorization is understood to extend to the acquisition of shares of the Company by controlled companies.

Likewise, the General Shareholders' Meeting of April 20, 2012, in its tenth item of the Agenda, adopted the following agreement:

Ten.- Authorization to the Board of Directors, with power of substitution in the Executive Committee, in accordance with the provisions of article 297.1 b) of the Capital Companies Act, so that, within a maximum period of five (5) years, If it deems it advisable, to increase the share capital up to the maximum amount corresponding to half of the share capital at the time of authorization, with an incomplete subscription forecast, issuing ordinary shares, privileged or redeemable shares, voting or not voting, with premium or without premium, in one or more times and in the opportunity and amount that considers appropriate, including the power to eliminate, as the case may be, preferential subscription rights, rewriting the corresponding articles of the Articles of Association and leaving effect the authorization agreed by the General Meeting of April 20, 2010.

Ten

- 1) Taking into account the current figure of the share capital, to authorize the Board of Directors, with power of substitution in the Executive Committee, to increase the share capital by FOUR HUNDRED AND NINETY FIVE MILLION EIGHT HUNDRED AND THIRTY SIX THOUSAND SIXTY AND NINE EUROS (495,836. 069.- €.) within five (5) years, as from this date, by means of cash disbursement, in one or more times in the opportunity and amount that the same decides, issuing ordinary shares, privileged or redeemable shares, with voting or non-voting, with a premium or without a premium, without the need for a new authorization from the General Meeting, as well as to modify the articles of the Bylaws that may be necessary for the increase or increases of capital made pursuant to said authorization , with an incomplete subscription forecast, all in accordance with what is established in article 297.1 b) of the Capital Companies Act, without giving effect to the authorization agreed by the General Meeting of April 20, 2010.
- 2) The Board of Directors, with power of substitution in the Executive Committee, is expressly empowered to exclude, in whole or in part, the pre-emptive subscription right in relation to any or all of the issues that it may agree upon based on this authorization.

3) As a result of the previous agreement, to amend the Transitory Article of the Articles of Association, which will be drafted as follows:

“Temporary Article Delegation to the Board of Directors

The Company’s Board of Directors is empowered, within a maximum period of five (5) years as from today, to increase capital by FOUR HUNDRED NINETY-FIVE MILLION, EIGHT HUNDRED THIRTY-SIX THOUSAND, AND SIXTY-NINE EURO (495,836,069 euro) on one or more occasions, when and in the amount it so determines, by issuing voting or non-voting common, preference or redeemable shares, at a premium or otherwise, to be paid in cash, without the need for further shareholder approval, including where appropriate the power to totally or partially override pre-emptive subscription rights, and to amend the Articles of Association as required as a result of any capital increase(s) undertaken by virtue of the aforementioned authorisation, allowing for incomplete subscription, in conformity with the provisions of Article 153.1.b) of the Spanish Capital Companies Act; this power may be sub-delegated to the Executive Committee.”

A.9 bis Estimated free-float:

	%
Estimated free-float	31.39

A.10 State whether there are any restrictions on the transfer of securities and/or any restrictions on voting rights. In particular, disclose the existence of any restrictions that might hinder a takeover of the company through the acquisition of its shares in the market.

Yes

Description of restrictions

As a company that includes certain regulated and quasi-regulated assets and activities in the Group, the acquisition of shares of Gas Natural SDG, S.A. may be subject to the provisions of Additional Provision Nine of Law 3/2013, of June 4, creating the Comisión Nacional de los Mercados y Competencia (National Commission on Markets and Competition).

Due to its nature as main operator in the gas and electricity markets, the holding of its shares is subject to the restrictions established in article 34 of Decree-Law 6/2000 of Urgent Measures to intensify competition in the markets of goods and services.

A.11 State whether the shareholders acting at a general shareholders’ meeting have approved the adoption of breakthrough measures in the event of a takeover bid pursuant to the provisions of Law 6/2007.

No

If applicable, explain the approved measures and the terms on which the restrictions will become ineffective:

A.12 State whether the company has issued securities that are not traded on a regulated market within the European Community.

No

If applicable, specify the different classes of shares, if any, and the rights and obligations attaching to each class of shares.

B. General Shareholder's Meeting

B.1 State and, if applicable, describe whether there are differences with the minimum requirements set out in the Companies Act in connection with the quorum needed to hold a valid general shareholders' meeting.

No

B.2 State and, if applicable, describe any differences from the rules set out in the Companies Act for the adoption of corporate resolutions:

No

Describe how they differ from the rules provided by the Companies Act.

B.3 State the rules applicable to the amendment of the by-laws of the company. In particular, disclose the majorities provided for amending the by-laws, and any rules provided for the protection of the rights of the shareholders in the amendment of the by-laws.

The amendment to the Articles of Association is regulated by Articles 24, 32 and 68 of the Articles of Association and Article 2 of the Regulations of the General Meeting.

The shareholders, assembled at a duly convened Shareholders' Meeting, shall resolve upon the matters within its competence by simple majority vote in general. Accordingly, a motion will be deemed to have been adopted if the votes in favour of the capital present or represented exceed the votes against.

All shareholders, including dissidents and those that have not taken part in the Meeting, are subject to the resolutions of the Shareholders' Meeting.

For the valid ratification at ordinary or extraordinary Shareholders' Meetings of bond issues, an increase or decrease in capital, the suppression or curtailment of pre-emptive subscription rights in issues of new shares or convertible bonds and the transformation, merger, demerger, transfer en bloc of assets and liabilities, the transfer of registered office abroad and in general any amendment to the Company's Articles of Association, the attendance of shareholders, in person or by proxy, holding at least fifty per cent (50%) of the subscribed voting share capital will be necessary at first call. When the Meeting is convened for a second time, the shareholders present or represented owning twenty-five per cent (25%) of the aforesaid capital shall suffice.

Amendments to the Articles of Association require the approval of the Shareholders' Meeting subject to the following requirements:

- 1) That the Board of Directors or, where appropriate, the shareholders responsible for the proposal, draw up a written report to justify the proposed amendment.
- 2) The notice of the Shareholders' Meeting must clearly set out the proposed amendment and state that all shareholders are entitled to examine the full text of the proposed amendment and the report in connection with same at the registered offices and on the corporate web site, and to obtain a copy or have it delivered to them free of charge.
- 3) The decision must be adopted by the Shareholders' Meeting as provided in these Articles of Association.
- 4) The decision must be expressed in a public instrument, registered with the Mercantile Registry and published in the Official Bulletin of the Mercantile Registry.

B.4 State the data on attendance at the general shareholder's meetings held during the financial year referred to in this report and those of the prior financial year:

Date of General Shareholders' Meeting	% of shareholders present in person	% of shareholders represented by proxy	Attendance data		% Total
			% absentee voting		
			Electronic voting	Others	
14/05/2015	68.57	11.96	0	0	80.53
04/05/2016	68.67	8.77	0	0	77.44

B.5 State whether there are any by-law restrictions requiring a minimum number of shares to attend the general shareholders' meeting.

Yes

Number of shares required to attend the general shareholder's meeting

100

B.6 Section deleted.

B.7 State the address and method for accessing the company's website to access information regarding corporate governance and other information regarding general shareholders' meetings that must be made available to the shareholders through the company's website.

Information regarding Corporate Governance can be accessed at this address:
www.gasnaturalfenosa.com – Shareholders and Investor – Corporate Governance.

Information regarding the general shareholders' meeting of the Company can be accessed at this address:
www.gasnaturalfenosa.com – General Shareholder's Meeting.

C. Structure Of The Company's Management

C.1 Board of directors

C.1.1 Maximum and minimum number of directors set forth in the by-laws:

Maximum number of directors	20
Minimum number of directors	10

C.1.2 Complete the following table identifying the members of the board:

Individual or company name of the director	Representative of director	Type	Position on the board	Date of first appointment	Date of last appointment	Election procedure
Mr. Isidro Faine Casas	–	Proprietary	President	18/05/2015	18/05/2015	General Shareholder's Meeting
Mr. Josu Jon Imaz San Miguel	–	Proprietary	Vicepresident 1º	21/09/2016	21/09/2016	Cooptation
Mr. William Alan Woodburn	–	Proprietary	Vicepresident 2º	30/09/2016	30/09/2016	Cooptation
Mr. Rafael Villaseca Marco	–	Executive	Chairman/Ceo	28/01/2005	14/05/2015	General Shareholder's Meeting
Mr. Ramón Adell Ramón	–	Independent	Director	18/06/2010	14/05/2015	General Shareholder's Meeting
Mr. Enrique Alcántara-García Irazoqui	–	Proprietary	Director	27/06/1991	11/04/2014	General Shareholder's Meeting
Mr. Xabier Añoveros Trías de Bes	–	Independent	Director	20/04/2012	14/05/2015	General Shareholder's Meeting
Mr. Marcelino Armenter Vidal	–	Proprietary	Director	21/09/2016	21/09/2016	Cooptation
Mr. Mario Armero Montes	–	Proprietary	Director	21/09/2016	21/09/2016	Cooptation
Mr. Francisco Belil Creixell	–	Independent	Director	14/05/2015	14/05/2015	General Shareholder's Meeting
Mrs. Benita María Ferrero-Waldner	–	Independent	Director	14/05/2015	14/05/2015	General Shareholder's Meeting
Mr. Alejandro García-Bragado Dalmau	–	Proprietary	Director	21/09/2016	21/09/2016	Cooptation
Mrs. Cristina Garmendia Mendizábal	–	Independent	Director	14/05/2015	14/05/2015	General Shareholder's Meeting
Mrs. Helena Herrero Starkie	–	Independent	Director	04/05/2016	04/05/2016	General Shareholder's Meeting
Mr. Miguel Martínez San Martín	–	Proprietary	Director	14/05/2015	14/05/2015	General Shareholder's Meeting
Mr. Rajaram Rao	–	Proprietary	Director	21/09/2016	21/09/2016	Cooptation
Mr. Luis Suárez de Lezo Mantilla	–	Proprietary	Director	26/02/2010	11/04/2014	General Shareholder's Meeting
Total number of directors						17

State the vacancies on the board of directors during the reporting period:

Individual or company name of director	Class of director at time of vacancy	Date of vacancy
Mr. Salvador Gabarró Serra	Executive	21/09/2016
Mr. Emiliano López Achurra	Independent	04/05/2016
Mr. Antonio Brufau Niubó	Proprietary	21/09/2016
Mr. Demetrio Carceller Arce	Proprietary	15/09/2016
Mr. Heribert Padrol Munté	Proprietary	21/09/2016
Mr. Juan Rosell Lastortras	Proprietary	20/09/2016
Mr. Miguel Valls Maseda	Independent	21/09/2016

C.1.3 Complete the following tables about the members of the board and each member's status:

Executive Directors

Individual or company name of director	Position within the company's structure
Mr. Rafael Villaseca Marco	Chairman & ceo
Total number of executive directors	1
Total % of the board	5.88

External proprietary director

Individual or company name of director	Individual or company name of the significant shareholder represented by the director or that has proposed the director's appointment
Mr. Enrique Alcántara-García Irazoqui	Criteria Caixa, S.A.U.
Mr. Marcelino Armenter Vidal	Criteria Caixa, S.A.U.
Mr. Isidro Faine Casas	Criteria Caixa, S.A.U.
Mr. Alejandro García-Bragado Dalmau	Criteria Caixa, S.A.U.
Mr. Josu Jon Imaz San Miguel	Repsol, S.A.
Mr. Miguel Martínez San Martín	Repsol, S.A.
Mr. Luís Suarez De Lezo Mantilla	Repsol, S.A.
Mr. Mario Armero Montes	Gip III Canary 1 S. À R.L.
Mr. Rajaram Rao	Gip III Canary 1 S. À R.L.
Mr. William Alan Woodburn	Gip III Canary 1 S. À R.L.
Total number of proprietary directors	10
% total directors	58.82

External independent directors

Individual or company name of director	Profile
Mr. Ramón Adell Ramón	Professor of Financial Economics and Accounting at the University of Barcelona
Mr. Xabier Añoveros Trías de Bes	Doctorate in Law
Mr. Francisco Belil Creixell	Senior Engineer
Mrs. Benita María Ferrero-Waldner	Doctorate in Law
Mrs. Cristina Garmendia Mendizábal	Doctorate in Biology
Mrs. Helena Herrero Starkie	Degree in Chemical Sciences
Total number of independent director	6
Total % of the board	35.29

State whether any director classified as independent receives from the company or its group any amount or benefit for items other than director remuneration, or maintains or has maintained during the last financial year a business relationship with the company or with any company of its group, whether in the director's own name or as a significant shareholder, director, or senior officer of an entity that maintains or has maintained such relationship.

If applicable, include a reasoned statement of the director regarding the reasons for which it is believed that such director can carry out the duties thereof as an independent director.

Other external director

Identify the other external directors and describe the reasons why they cannot be considered proprietary or independent directors as well as their ties, whether with the company, its management, or its shareholders:

State the changes, if any, in the class of each director during the period:

C.1.4 Complete the following table with information regarding the number of female directors for the last 4 financial years, as well as the status of such directors:

	Number of female Directors				% of total directors of each class			
	Financial year t	Financial year t-1	Financial year t-2	Financial year t-3	Financial year t	Financial year t-1	Financial year t-2	Financial year t-3
Executive	0	0	0	0	0	0	0	0
Proprietary	0	0	0	0	0	0	0	0
Independent	3	2	0	0	17.65	11.76	0	0
Other external	0	0	0	0	0	0	0	0
Total	3	2	0	0	17.65	11.76	0	0

C.1.5 Explain any measures adopted to include on the board of directors a number of women that allows for a balanced presence of men and women.

Explanation of the measures

The Company is firmly committed to the principle of diversity in the composition of its Board of Directors and due respect to the right of shareholders to make proposals for the appointment of Directors that they deem appropriate in accordance with the legal mandate of proportional representation. Therefore, as far as gender diversity is concerned, just as the Board of Directors is respectful of the proposals of proprietary directors received from shareholders, in contrast to independent directors, the proposal corresponds to the Appointments and Remuneration. The latter has adopted an active approach to achieving such diversity in recent renovations. As a consequence, in the proposal to the 2015 Shareholders' Meeting, half of the new independent directors were men and the other half were women and at the 2016 Shareholders' Meeting, since there was only one renewal, it was decided that the only counselor to propose was a woman. The result is that there has been a short period of time between the independent directors.

C.1.6 Explain any measures approved by the appointments committee in order for selection procedures to be free of any implied bias that hinders the selection of female directors, and in order for the company to deliberately search for women who meet the professional profile that is sought and include them among potential candidates:

Explanation of the measures

The Appointments and Remuneration Committee is charged with the task of reviewing the necessary skills in the candidates who must fill each vacancy, meeting the requirements for each category of Directors and the process of incorporating the new members, reports or proposals where appropriate. The responsibility of ensuring that when new vacancies are filled, the selection procedures are free from any implied bias entailing any kind of discrimination and, in particular, from any bias that may hinder the selection of female directors including, in the same conditions among the potential candidates, women who meet the profile sought.

If there are few or no female directors despite any measures adopted, describe the reasons for such result:

Explanation of the reasons

The female Directors account for 17.64% of the total number of Directors. The Company gradually incorporates female Directors to its Board of Directors as a manifestation of its commitment to diversity in the composition of the Board, one of whose most relevant manifestations is the gender diversity, since it has moved from 0 Directors in 2014 to 3 Directors in 2016, and it has been possible that in a short term there is parity among the Independent Directors.

C.1.6 bis Explain the conclusions of the appointments committee regarding verification of compliance with the director selection policy. Particularly explain how said policy is promoting the goal that the number of female directors represents at least 30% of all members of the board of directors by 2020.

Explanations about the conclusions

The Appointments and Remuneration Committee has verified the Directors' Selection Policy and has concluded that it is in accordance with a very defined shareholder structure that imposes respect for certain legal requirements of respect for the principle of proportional representation of shareholders, Which should be made compatible with the Corporate Governance recommendations. The Appointments and Remuneration Committee is satisfied that the achievements of the 2016 Shareholders' Meeting have been maintained in the restructuring of corporate governance in September 2016.

C.1.7 Explain the form of representation on the board of shareholders with significant holdings.

Of the four significant shareholders that the Company currently has, only three of them have proprietary Directors. Criteria Caixa, S.A.U. has four Proprietary Directors, Repsol, S.A. And Gip III Canary, 1 S À R.L. each of them has three Proprietary Directors and Société Nationale pour la Recherche, la Production, le Transport, Transformation et la Commercialization does not have any proprietary Director. This representation is fully consistent with the principle of proportional representation.

C.1.8 Explain, if applicable, the reasons why proprietary directors have been appointed at the proposal of shareholders whose shareholding interest is less than 3% of share capital.

Individual or company name of the shareholder	Reason
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State whether there has been no answer to formal petitions for presence on the board received from shareholders whose shareholding interest is equal to or greater than that of others at whose proposal proprietary directors have been appointed. If so, describe the reasons why such petitions have not been answered:

No

C.1.9 State whether any director has withdrawn from the position as such before the expiration of the director's term of office, whether the director has given reasons to the board and by what means, and in the event that the director gave reasons in writing, describe at least the reasons given thereby:

Name of director	Reason for withdrawal
Mr. Salvador Gabarró Serra	Change in the shareholding structure
Mr. Heribert Padrol Munté	Change in the shareholding structure
Mr. Antonio Brufau Niubó	Change in the shareholding structure
Mr. Demetrio Carceller Arce	Change in the shareholding structure
Mr. Juan Rosell Lastortras	See paragraph H
Mr. Miguel Valls Maseda	Change in the shareholding structure

C.1.10 State any powers delegated to the CEO(s):

Name or company name of Director	Brief description
Mr. Rafael Villaseca Marco	He has delegated broad powers of representation and administration according to the characteristics and needs of the position of CEO.

C.1.11 Identify any members of the board who are directors or officers of companies within the listed company's group:

C.1.12 Identify the directors of your company, if any, who are members of the board of directors of other companies listed on official stock exchanges other than those of your group, which have been reported to your company:

Individual or company name of the director	Name of listed company	Position
Mr. Isidro Fainé Casas	Telefónica, S.A.	Vicepresident
Mr. Isidro Fainé Casas	The Bank of East Asia	Director
Mr. Isidro Fainé Casas	Suez Environnement Company, S.A.	Director
Mr. Josu Jon Imaz San Miguel	Repsol, S.A.	Ceo
Mr. Ramón Adell Ramón	Oryzon Genomics, S.A.	Director
Mr. Marcelino Armenter Vidal	Abertis Infraestructuras, S.A.	Director
Mr. Mario Armero Montes	Compañía Logística de Hidrocarburos, S.A.	Director
Mrs. Benita Ferrero-Waldner	Munich Reinsurance CO	Director
Mrs. Cristina Garmendia Mendizábal	Compañía de Distribución Integral Logista Holdings, S.A.	Director
Mrs. Cristina Garmendia Mendizábal	Corporación Financiera Alba, S.A.	Director
Mrs. Cristina Garmendia Mendizábal	Sygnis AG	President
Mr. Luis Suárez de Lezo	Repsol, S.A.	Secretary of the Board/Board Member

C.1.13 State and, if applicable, explain whether the regulations of the board have established rules regarding the maximum number of boards of which its directors may be members:

No

Explanation of rules

C.1.14 Section deleted.

C.1.15 State the overall remuneration of the board of directors:

Remuneration of the board of directors (thousands of euros)	7,655
Amount of pension rights accumulated by the directors (thousands of euro)	3,241
Amount of pension rights accumulated by former directors (thousands of euro)	0

C.1.16 Identify the members of the company's senior management who are not executive directors and state the total remuneration accruing to them during the financial year:

Name or company name	Position/s
Mr. Carlos Javier Álvarez Fernández	Chief Financial Office
Mr. Sergio Aranda Moreno	Managing Director for Latin America
Mr. Carlos Ayuso Salinas	Director of Internal Audit, Compliance and Control
Mr. Antonio Basolas Tena	Managing Director of Strategy and Development
Mr. José María Egea Krauel	Managing Director of Energy Planning
Mr. Manuel Fernández Álvarez	Managing Director of Wholesale Energy Business
Mr. Manuel García Cobaleda	Legal Services General Manager and Company Secretary
Mr. Jordi García Tabernero	Managing Director of Communication and Institutional Relations
Mr. Daniel López Jordà	Managing Director of Retail Energy Business
Mr. Antoni Peris Mingot	Managing Director of Regulated Business
Mrs. Rosa M ^a Sanz García	Managing Director of People and Resources
Total senior management remuneration (in thousands of euros)	9,445

C.1.17 Describe any significant relationships, other than the ones contemplated in the prior item, of the members of the board of directors linking them to significant shareholders and/or companies within their group:

Individual or company name of director	Company name of the Significant shareholder	Position
Mr. Josu Jon Imaz San Miguel	Repsol, S.A.	CEO
Mr. Josu Jon Imaz San Miguel	Repsol Oli & Gas Canada Inc.	President
Mr. Isidro Fainé Casas	Criteria Caixa, S.A.U.	President
Mr. Marcelino Armenter Vidal	Caixa Capital Risc S.G.E.C.R., S.A.	President
Mr. Alejandro García-Bragado Dalmau	Criteria Caixa, S.A.U.	First Vice President
Mr. Luís Suárez de Lezo Mantilla	Repsol, S.A.	Secretary of The Board/Board Member

Describe any significant relationships, other than the ones contemplated in the prior item, of the members of the board of directors linking them to significant shareholders and/or companies within their group:

Individual or company name of related director	Individual or company name of related significant shareholder	Description of relationship
Mr. Isidro Fainé Casas	Fundación Bancaria Caixa D'estalvis i Pensions de Barcelona (la Caixa)	Chairman of The Board of Trustees
Mr. Luis Suarez De Lezo Mantilla	Repsol, S.A.	Secretary of The Board
Mr. Miguel Martínez San Martín	Repsol, S.A.	Cfo and Corporate Development
Mr. Marcelino Armenter Vidal	Fundación Bancaria Caixa D'estalvis i Pensions de Barcelona (la Caixa)	Managing Director Criteria Caixa, S.A.U.
Mr. Rajaram Rao	Global Infrastructure Partners III	Shareholder
Mr. William Alan Woodburn	Global Infrastructure Partners III	Shareholder

C.1.18 State whether the regulations of the board have been amended during the financial year:

Yes

Description of changes

Modifications have been introduced in September 2016 which have affected two areas:

1. Establishment of reinforced majorities for the adoption of agreements on certain matters (art 10): acquisition or disposal of assets for more than 500 million euros, approval of budgets and strategic plan, dividend policy, financing agreements or contracts of Gas supply of more than 500 million euros, other material contracts or CAPEX investments of more than 200 million euros, material modifications in accounting or tax policies and reformulation of accounts. Art. 5 establishes a reservation of these matters to the full Council.
2. The number of members of the Executive Committee and the ¿? Committee has been modified to make compatible the principle of proportional representation of shareholders with full respect for the requirements contained in the Law of Capital Companies regarding the presence of independents in said Committees. To this end, the maximum number of members of the Executive Committee (Article 30) and the number of members of the Executive Committee (Article 32) have been extended to 10. (See Section C.2.5 below).

C.1.19 State the procedures for the selection, appointment, re-election, evaluation, and removal of directors. Describe the competent bodies, the procedures to be followed, and the criteria applied in each of such procedures.

The procedures for the selection, appointment, re-election, evaluation, and removal of directors are established in Articles 41 and 42 of Articles of Association and in articles 4, 11 to 15 and 31 of Regulations of the Board of Directors.

1.- Appointment of Board Members:

The Board Members shall be designated by the General Shareholders Meeting or by the Board of Directors, in accordance with the provisions of the Corporate Enterprises Act and in the Articles of Association of the Company.

The Board Members that are designated must be persons that, in addition to their compliance with all legal requirements and all terms provided for under the Articles of Association in respect of the appointment thereof, are prestigious and well known persons that have adequate knowledge and professional expertise in respect of the exercise of their functions. The proposals for the appointment of Board Members that the Board of Directors submits to the General Shareholders Meeting for consideration and the decisions for the appointment thereof that are adopted by the General Shareholders Meeting by virtue of the co-option powers that are legally available thereto, must be preceded by a proposal from the Appointments and Remuneration Committee in the case of Independent Board Members or by a report for the for the rest of the Board Members. When the Board diverges from recommendations of said Committee, the reasons for said divergence must be justified and formally recorded in the Minutes of the meeting.

The updated professional and biographical profile of all of the Board Members shall be published on the Company's web page, together with other Boards of Directors to which they belong, whether or not listed companies, as well as the category of the Board Member, as applicable, and, in the case of Proprietary Board Members, it shall be necessary to also state the shareholder that they represent or with which they are related, the date of their first appointment as a Board Member of the Company, as well as the subsequent dates of appointment and the shares of the Company and the share options that are held thereby.

The Board shall establish orientation programs that provide the new Board Members with the necessary knowledge regarding the Company and the corporate governance rules thereof for the adequate performance of the functions thereof. Furthermore, the Board shall provide the Board Members with knowledge upgrade programs as and when required.

2. Re-election of Board Members:

The Board Members shall exercise their position during the maximum term of three years, and may be re-elected. The Board Members designated pursuant to the co-option system shall exercise their positions subject to the terms provided for under applicable legislation.

The Appointments and Remuneration Committee, which is responsible for the evaluation of the quality of the work and the commitment to their positions of the Board Members that have been proposed during the preceding mandate, must, necessarily, propose, in the case of Independent Board Members and must inform in respect of the rest of the Board Members, regarding the proposal for the re-election of Board Members that the Board of Directors decides to present to the General Shareholders Meeting.

Independent directors will not be in the charge for a period of more than 12 years.

3. Evaluation:

According to Article 4.5. of Regulations of the Board of Directors, the Board will evaluate periodically its performance, as well as the performance of the different Committees.

4. Removal of Board Members:

The Board Members shall be removed from office when their respective terms, for which they were appointed, have elapsed and in all other situations, when required pursuant to the provisions of the Corporate Enterprises Act, the Articles of Association and these Regulations.

The Board Members must present their resignation from the Board of Directors and must formalize, if the Board deems necessary, their corresponding formal resignation from office in the following situations:

- a) When the Executive Board Members cease to exercise their executive functions.
- b) When the Board Members are subject to any of the situations of disqualification or prohibition as provided for under applicable law, under the Articles of Association or under these Regulations.
- c) When the Board Members seriously breach their obligations as Board Members, thereby placing the interests of the Company at risk.
- d) When the reason for which the Board Members were appointed as Independent Board Members, Executive Board Members or Proprietary Board Members no longer exists.

After the Board Members have been removed from office, said persons may not render their services to a competitor company during the period of two years, except in the case that the Board of Directors waives said obligation or reduces the term of the restraint of trade covenant.

When an Independent Board Member is removed from office prior to the conclusion of the mandate for which he or she was appointed, the reasons for said removal from office must be explained in a letter addressed to the rest of the Board Members. The removal of the Board Members shall be notified as relevant information.

C.1.20 Explain the extent to which the self-evaluation of the board has given rise to significant changes in its internal organization and regarding the procedures applicable to its activities:

Description of changes

The Board of Director's self-assessment has not led to major changes in the internal organization and procedures applicable to its activities. The Board concludes in its report that during the 2016 financial year it has functioned with expected normality, fully exercising its powers with respect to the legislation and the regulations governing the organization and functioning of the Board Regulations.

Irrespective of the fact that the Chairman of the Board and the Managing Director have intervened in all matters submitted to the Board, it is worth noting that the diversity of profiles of the different members of the Board of Directors has resulted in their interventions highlighted in matters such as:

Mr. Antonio Brufau Niubó: monitoring of investments, special attention in foreign countries.

Mr. Ramón Adell Ramón: audit and annual accounts.

Mr. Enrique Alcántara-García Irazoqui: rating of the Company.

Mr. Xabier Añoveros Trías de Bes: Strategy Plan.

Mr. Francisco Belil Creixell: growing businesses.

Mr. Demetrio Carceller Arce: international investments.

Mrs. Benita María Ferrero-Waldner: commitments in EU and business in Asia and India. Electricaribe.

Mrs. Cristina Garmendia Mendizábal: investments in IT. Electricaribe.

Mr. Emiliano López Achurra: political and economic worldwide background.

Mr. Miguel Martínez San Martín: Brent and dollar development, as well as Company rating.

Mr. Heribert Padrol Munté: Tax policy.

Mr. Joan Rosell Lastortras: Dividend policy.

Mr. Luis Suárez de Lezo Mantilla: Strategy Plan.

Mr. Miguel Valls Maseda: Remuneration policy.

Mr. Mario Armero Montes: Legal strategy in Colombia.

Mr. Marcelino Armenter Vidal: Economic issues.

Mr. Rajaram Rao: reporting to the Board and economic information.

Mr. Josu Jon Imaz San Miguel: medium- and long-term development of markets.

Mr. William Alan Woodburn: health and safety, environmental and operational efficiency.

Mr. Alejandro García-Bragado Dalmau: corporate governance.

Mrs. Helena Herrero Starkie: technology and operational innovation.

C.1.20 bis Describe the process of self-evaluation and the areas evaluated by the board of directors, as it may be assisted by an external consultant, regarding diversity in its composition and powers, the operation and composition of its committees, the performance of the chairman of the board and chief executive officer, and the performance and contribution of each director.

C.1.20 ter List any business relationships of the consultant or any company of its group with the company or any company of its group.

C.1.21 State the circumstances under which the resignation of directors is mandatory.

The Directors shall cease to hold office for the term for which they were appointed, unless re-elected and when the General Meeting decides to use the powers it holds. Likewise, they shall cease in all other cases in which they may do so in accordance with the Law, the Articles of Association and the Regulations of the Board of Directors.

The Board Members must present their resignation from the Board of Directors and must formalize, if the Board deems necessary, their corresponding formal resignation from office in the following situations:

- a) When the Executive Board Members cease to exercise their executive functions.
- b) When the Board Members are subject to any of the situations of disqualification or prohibition as provided for under applicable law, under the Articles of Association or under these Regulations.
- c) When the Board Members seriously breach their obligations as Board Members, thereby placing the interests of the Company at risk.
- d) When the reason for which the Board Members were appointed as Independent Board Members, Executive Board Members or Proprietary Board Members no longer exists.

C.1.22 Section deleted.

C.1.23 Are qualified majorities, different from the statutory majorities, required to adopt any type of decision?

Yes

If so, describe the differences.

Description of differences

Article 10.4 of Regulations of the Board of Directors provides as follows:

"4. The resolutions and decisions must be adopted with the favorable vote of the absolute majority of the Board Members that are either present or represented thereat, unless the Corporate Enterprises Act, the Articles of Association or these Regulations provide for the need for a qualified majority. The written voting procedures, without a meeting session, shall only be possible when none of the Board Members are opposed to this voting procedure and provided that the requirements provided for under the Companies Register Regulations are satisfied.

In particular, the favorable vote of at least two thirds of the Board Members, present or represented, shall be necessary for the valid adoption of the resolutions and decisions regarding the following aspects, that are reserved for the plenary session of the Board and, accordingly, are not able to be delegated

- a) The acquisition or disposal of assets that belong to the Company (irrespective of the legal nature of said operations and, in particular, although said operations are carried out by means of merger or split-off operations or any other subsidiary company operations) for a sum that exceeds 500,000, 000 Euros, unless the approval thereof corresponds to the General Shareholders Meeting or are carried out in execution of the budget or the strategic or business plan of the Company.
- b) The approval of the budget and the strategic or business plan of the Company.
- c) The modification of the dividends distribution policy and the approval of a new dividends distribution policy.
- d) The formalization, modification, renewal, non-renewal or termination by the Company of financing or refinancing contracts for a sum that exceeds 500, 000,000 Euros.

- e) The formalization, modification, renewal, non-renewal or termination by the Company of any material contract, other than the contracts provided for under paragraph d) hereinabove, the amount of which exceeds 500,000,000 Euros in the case of gas procurement contracts and which exceeds 200,000,000 Euros in the case of other contracts.
- f) Any material modifications to the accounting or tax criteria and policies of the Company, unless they are the result of modifications to applicable legislation or of the application of directives or criteria established by competent public authorities.
- g) The redrafting of the annual accounts of the Company, unless said redrafting is the result of any legislative modification or of the application of directives or criteria established by competent public authorities.
- h) Capital investments (CAPEX) not provided for in the annual budget of the Company that exceed 200,000,000 Euros.
- i) The modification of this paragraph i), the modification of the aspects and terms of paragraphs a) to h) hereinabove or the modification of the qualified majority voting requirements provided for in respect thereof.

C.1.24 Explain whether there are specific requirements, other than the requirements relating to directors, to be appointed chairman of the board of directors.

No

C.1.25 State whether the chair has a tie-breaking vote:

No

C.1.26 State whether the by-laws or the regulations of the board set forth any age limit for directors:

No

C.1.27 State whether the by-laws or the regulations of the Board establish any limit on the term of office for independent directors that is different than the term provided by regulatory provisions:

No

C.1.28 State whether there are formal rules for proxy-voting at meetings of the board of directors, the manner of doing so, and especially the maximum number of proxies that a director may hold, as well as whether any restriction has been established regarding the categories of directors to whom proxies may be granted beyond the restrictions imposed by law. If so, briefly describe such rules.

According to Article 47, second paragraph, of Articles of Association: "Directors unable to attend may appoint another Director to act on their behalf, with no limit applying to the number of Directors that may be represented by another. Proxies must be granted in writing. Non-executive directors may grant proxy only to another non-executive director."

On the other hand, Article 10.3 of Regulations of the Board of Directors provides: "Each Board Member may confer his or her proxy representation upon another Board Member, without any limitation as to the number of proxy representations that may be held by the Board Members. The proxy representation of the absent Board Members may be formalised by any documented procedure whatsoever, including that of telegrams, e-mail, telex or facsimile addressed to the Chairman or the Secretary of the Board, a sufficient period of time beforehand."

C.1.29 State the number of meetings that the board of directors has held during the financial year. In addition, specify the number of times the board has met, if any, at which the chair was not in attendance. Proxies granted with specific instructions shall be counted as attendance.

Number of meetings of the board	15
Number of meetings of the board at which the chair was not in attendance	0

If the chair is an executive director, state the number of meetings held without the presence in person or by proxy of any executive director and chaired by the lead independent director.

Number of meetings	0
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State the number of meetings held by the different committees of the board of directors during the financial year:

Number of meetings of the Executive Committee	6
Number of meetings of the Audit Committee	7
Number of meetings of the Appointments and Remuneration Committee	8
Number of meetings of the appointments Committee	
Number of meetings of the Remuneration Committee	
Number of meetings of Committee _____	

C.1.30 State the number of meetings that the board of directors has held during the financial year with the attendance of all of its members. Proxies granted with specific instructions shall be counted as attendance:

Number of meetings with the attendance of the directors	9
% in attendance of total votes during the financial year	94.51

C.1.31 State whether the annual individual accounts and the annual consolidated accounts that are submitted to the board for approval are previously certified:

Yes

Identify, if applicable, the person/persons that has/have certified the annual individual and consolidated accounts of the company for preparation by the board:

Name	Position
Mr. Carlos Javier Álvarez Fernández	Chief Financial Officer

C.1.32 Explain the mechanisms, if any, adopted by the board of directors to avoid any qualifications in the audit report on the annual individual and consolidated accounts prepared by the board of directors and submitted to the shareholders at the general shareholders' meeting.

Article 7 of the Regulation of the Board of Directors provides as follows:

"1.- After the Board has received the reports issued by the Economic and Financial Department and by the Audit Committee, and after the pertinent clarifications in respect thereof, the Board of Directors shall draft, in clear and precise terms, that facilitate the adequate understanding of the content thereof, both the individual and consolidated Annual Accounts and Management Report. The Board of Directors shall ensure that the foregoing represent the true and fair image of the equity, the financial situation and the results of the Company, in accordance with the provisions of the Corporate Enterprises Act.

2.- Except in the case of any express declaration to the contrary, which must be formalized by way of formal Certificate, it shall be understood that, prior to the formalization of the Annual Accounts, as required pursuant to the Corporate Enterprises Act, the Board of Directors and each one of the members thereof, has been provided with all of the information necessary for the formalization thereof, and any necessary qualifications shall be included therein, as the case may be.

3.- The Board of Directors shall use their best endeavors to draft the accounts in such a way so that the accounts auditor of the Company is not required to include any qualifications whatsoever to the accounts. Notwithstanding the foregoing, when the Board of Directors considers that it must maintain its own criteria, the Board shall publicly explain the terms and scope of the discrepancy"

Prior to its submission to the Audit Committee and subsequently to the Board of Directors, the Company's Accounts are certified by the Economics and Finance Director General.

Pursuant to those established in article 51 bis of the Articles of Association and in the Capital Companies Act, the Audit Committee is responsible for, inter alia, the functions of informing the General Meeting of shareholders on matters arising in relation to matters within the competence of the Committee and, in particular, on the outcome of the audit, explaining how it has contributed to the integrity of the financial information and the role that the Committee has played in that process, process of preparation and presentation of the mandatory financial information and to present recommendations or proposals to the Board of Directors, aimed at safeguarding its integrity.

In addition, the Board of Directors of the Company has entrusted the Audit Committee with other powers to ensure that the Board of Directors seeks to present the accounts to the General Shareholders' Meeting without limitations or qualifications in the Audit Report and, in exceptional cases where there are exceptions, both the Chairman of the Committee and the Auditors explain to the shareholders the content and scope of such limitations.

C.1.33 Is the secretary of the board a director?

No

If the secretary is not a director, complete the following table:

Individual or Company name of the Secretary	Representative
Mr. Manuel García Cobaleda	

C.1.34 Section deleted.

C.1.35 State the mechanisms, if any, used by the company to preserve the independence of auditors, financial analysts, investment banks, and rating agencies.

Among the legal duties of the Audit Committee are to establish the appropriate relations with the external auditor to receive information on issues that may threaten its independence, for its consideration by the committee, and any others related to the process, and where appropriate the authorization of services other than those prohibited under the conditions set out in Articles 5 (4) and 6.2 (b) of Regulation (EU) No 537 / 2014, of April 16, and as provided for in section 3 of Chapter IV of Title I of Law 22/2015, of July 20, Audit of Accounts, on the regime of independence, as well as those other communications provided for in the statutory audit and auditing standards. In any case, they must receive annually from the external auditors the declaration of their independence in relation to the entity or entities related to it directly or indirectly, as well as the detailed and individualized information of the additional services of any kind provided and the corresponding fees received of these entities by the external auditor or by the persons or entities related to it in accordance with the provisions of the regulations governing the audit activity.

It is also the function of the Audit Committee to issue annually, prior to the issuance of the audit report, a report that will express an opinion on whether the independence of auditors or audit firms is compromised. This report must contain, in any case, the reasoned assessment of the provision of each and every one of the additional services referred to in the previous letter, individually considered and as a whole, other than statutory audit and in relation to the regime of independence or with the regulations regulating the audit activity.

The Board of Directors has also entrusted the following functions to the Audit Committee: ensuring that the remuneration of the external auditor for their work does not compromise their quality or independence and ensure that the company and the external auditor respect the rules in force on the provision of services other than audit services, limits on the concentration of the auditor's business and, in general, on the other rules on the independence of auditors.

Additionally, Article 6.4 of the Council Regulation provides that "The Board of Directors shall ensure that a direct relationship is maintained with the members of the senior management bodies of the Company and with the Auditors thereof. The objective, professional and permanent nature of said relationship shall strictly respect the independence of the Auditors."

The principles underlying the Company's relationship with financial analysts and investment banks are based on transparency, simultaneity and non-discrimination, as well as the existence of specific and distinct partners for each group.

In addition, the Company pays particular attention not to compromise or interfere in the independence of financial analysts with respect to the services provided by investment banks, in accordance with the internal codes of conduct established by them and aimed at the separation of their Analytical and advisory services.

C.1.36 State whether the Company has changed the external auditor during the financial year. If so, identify the incoming and the outgoing auditor:

No

If there has been any disagreement with the outgoing auditor, provide an explanation thereof:

C.1.37 State whether the audit firm performs other non-audit work for the company and/or its group. If so, state the amount of the fees paid for such work and the percentage they represent of the aggregate fees charged to the company and/or its group:

Yes

	Company	Group	Total
Amount of other non-audit work (thousands of euros)	0	233	233
Amount of non-audit work / Aggregate amount billed by the audit firm (%)	0	5.8	4.7

C.1.38 State whether the audit report on the annual accounts for the prior financial year has observations or qualifications. If so, state the reasons given by the chair of the audit committee to explain the content and scope of such observations or qualifications.

No

C.1.39 State the consecutive number of years for which the current audit firm has been auditing the annual accounts of the company and/or its group. In addition, state the percentage represented by such number of financial years audited by the current audit firm with respect to the total number of financial years in which the annual accounts have been audited:

	Company	Group
Number of continuous financial years	26	26
Number of years audited by the current audit firm/ Number of years in which the company has been audited (%)	100	100

C.1.40 State whether there is any procedure for directors to hire external advisory services, and if so, describe it:

Yes

Describe the procedure

Article 21 of Regulations of the Board of Directors provides as follows:

"1.-The Board Members shall have access, through the Chairman, and, as the case may be, through the Secretary, to all of the services of the Company and may compile and receive, with the broadest possible powers, the information and advisory services that may be required in relation to any aspect of the Company whatsoever. The right to information shall be extended to the subsidiary companies and shall be channelled through the Chairman or the Secretary of the Board of Directors or of the corresponding Committees of the Board, where the information shall be directly provided thereto, and the Board Members shall be provided with the appropriate liaisons or any measures necessary for the analysis thereof. 2.- Furthermore, the Board Members shall have the right to propose to the Board of Directors that the Company contract, at the cost and expense thereof, the legal advisors, accountants, technical professionals, financial advisors, commercial professionals or any other professional whatsoever that they consider necessary for the interests of the Company in order to assist the Board Members in the exercise of their functions, when related to specific problems of certain relevance and complexity that are associated with the exercise of their positions. 3.- Both the request for access as well as the proposal that are referred to under paragraphs 1 and 2 of this Article, must be notified to the Chairman of the Company through the Secretary of the Board. The Board of Directors may veto the approval of the proposal that is referred to under paragraph 2 of this Article if the Board considers that said proposal is unnecessary for the performance of the functions of the Board Member, or that the sum thereof is disproportionate in relation to the importance of the problem and the assets and revenue of the Company, or, finally, that said technical support or advisory services could be adequately provided by experts and technical staff of the Company."

C.1.41 State whether there is any procedure for directors to obtain sufficiently in advance the information required to prepare for meetings of management-level decision-making bodies and, if so, describe it:

Yes

Describe the procedure

Article 9, points 2 and 3, of the Regulations of the Board of Directors:

"2.-The notification of the ordinary meeting sessions of the Board shall be carried out by the Chairman, or by the Secretary or Deputy Secretary, under the instructions of the Chairman, and shall be carried out by any of the notification channels that are provided for under the Articles of Association, and said documentation shall be forwarded by way of e-mail, provided that the recipient Board Member has provided an e-mail address for said purposes. The meeting notification shall include the place at which the meeting is to be held and the agenda thereto and shall be issued, except in exceptional cases, at least 48 hours prior to the meeting. Prior to each meeting, the Board Members shall be provided with the information and documentation considered to be pertinent or relevant in relation to the matters to be discussed at the meeting of the Board. Furthermore, the Board Members shall be provided with the Minutes of the previous meeting, whether or not approved. The Chairman shall be responsible for establishing the agenda for the meetings, except in the case of the compulsory meeting pursuant to paragraph 1 hereinabove, in which case the agenda for the meeting shall include the aspects set out by the Board Members that have requested the meeting of the Board. The constitution of the Board shall be valid, without the prior notification thereof, if all of the Board Members are either present or duly represented and provided that they unanimously accept the holding of the meeting of the Board. The meeting sessions of the Board of Directors shall normally be held at the registered office of the Company, however may also be held at any other place that may be determined by the Chairman and must be set out in the meeting notification.

3.- Furthermore, the Board may be held in several different rooms, simultaneously, provided that the interactivity and intercommunication between said rooms in real time is ensured by way of audio-visual or telephonic means which, accordingly, provide for a single meeting session to be simultaneously carried out. In said situations, the meeting notification shall set out the connection system to be used and, if applicable, the places in which the necessary technical resources shall be available in order to attend and participate at the meeting. The resolutions shall be deemed to be adopted at the place where the Chairman is physically present."

The procedure followed is to refer, usually one week in advance, to the date of the meeting, the agenda and any information that is available and may be useful for a more accurate knowledge of the matters to be discussed at the Board meeting.

Likewise, during the meeting, officers whose affairs are treated are available to be called - and, often, made use of - so that the Directors can request clarifications, data or opinions in relation to the points dealt with in the session.

Finally, Directors may request additional information that they deem necessary for the exercise of their functions through the Board Secretariat.

C.1.42 State whether the company has established any rules requiring directors to inform the company—and, if applicable, resign from their position—in cases in which the credit and reputation of the company may be damaged, and if so provide a detailed description:

Yes

Explain the rules

Pursuant to Article 16.3 (e) of the Board Regulations, the Director is subject to the duty of loyalty under the terms established in current legislation and, in particular, the Director shall inform the Company of any kind of judicial, administrative or Any nature in which it is implied that, because of its importance, could seriously affect the reputation of the Company. The Board shall examine the matter and take such measures as may be desirable in the interest of the Company with the required urgency.

The Board Members must present their resignation from the Board of Directors and must formalize, if the Board deems necessary, their corresponding formal resignation from office in the following situations:

- a) When the Executive Board Members cease to exercise their executive functions.
- b) When the Board Members are subject to any of the situations of disqualification or prohibition as provided for under applicable law, under the Articles of Association or under these Regulations.
- c) When the Board Members seriously breach their obligations as Board Members, thereby placing the interests of the Company at risk.
- d) When the reason for which the Board Members were appointed as Independent Board Members, Executive Board Members or Proprietary Board Members no longer exists.

C.1.43 State whether any member of the board of directors has informed the company that such member has become subject to an order for further criminal prosecution upon indictment or that an order for the commencement of an oral trial has been issued against such member for the commission of any of the crimes contemplated in section 213 of the Companies Act:

No

State whether the board of directors has analysed the case. If so, provide a duly substantiated explanation of the decision adopted regarding whether or not the director should remain in office or, if applicable, describe the actions taken by the board of directors through the date of this report or that it plans to take.

No

C.1.44 Describe the significant agreements entered into by the company that go into effect, are amended, or terminate in the event of a change in control at the company as a result of a takeover bid, and effects thereof.

An important part of the investments with partners outside the group contain clauses of change of control that allow the other partner to choose to acquire the shares in case of change of control of the holding company of the group Gas Natural Fenosa.

On the other hand, most of the debt that includes a change of control clause, either by acquiring more than 50% of the voting shares or by obtaining the right to appoint the majority of the members of the Board of Directors of Gas Natural, are subject to additional conditions such as a significant reduction in the credit rating or rating caused by the change of control; material damage to the creditor; entails a material adverse change in the solvency or ability to perform the contract. These clauses represent the repayment of the debt, although they usually have a longer period than the one granted in cases of early ruling; in some cases the granting of guarantees is contemplated as an alternative to reimbursement.

Specifically, the bonds issued, in an approximate volume of 12,000 Million Euros, as is usual in the euromarket, would be subject to early maturity, provided that this change of control caused a three-step or three full notches fall in at least two of the three qualifications it had and all ratings fell below "investment grade" and whenever the Rating Agency expressed that the reduction of the credit rating is motivated by the change of control.

There are also loans for an amount of approx. 2,500 million Euros which could be subject to early repayment in the event of a change of control, most of this amount linked to infrastructure financing with funds from the European Investment Bank. Financing that was taken for the acquisition of Unión Fenosa. They also require a reduction in the rating and have special repayment terms that are longer than those of early termination cases.

Most of the change control clauses are linked to the occurrence of damage to creditors or significant reductions in rating. Most of the change in control is excluded if any of the current shareholders hold relevant interests in the company jointly with a third party. Some contract provides for the granting of guarantees as an alternative to reimbursement of the amount arranged and generally have special debt repayment terms that are longer than those of early termination cases.

C.1.45 Identify on an aggregate basis and provide a detailed description of the agreements between the company and its management level and decision-making positions or employees that provide for indemnities, guarantee or "golden parachute" clauses upon resignation or termination without cause, or if the contractual relationship is terminated as a result of a takeover bid or other type of transaction.

Number of beneficiaries 30

Type of beneficiary Description of agreement

Management Committee and other officers

The Chief Executive's contract was amended in October 2016 regarding the causes and termination regime, with the said clause of the contract being amended and extending its duration to its entire mandate as a Director of the Company.

The CEO's contract establishes an indemnity in the amount of three annuities of the total remuneration at the date of the contractual modification for certain cases of extinction of the contractual relationship: by decision of the company, unless very serious breach and culpable of his professional obligations which causes serious prejudice to the interests of Gas Natural SDG SA, by decision of the Chief Executive Officer or by termination of the contract. In addition, and in the case of a post-contractual non-competition agreement for one year, an indemnity equivalent to one full compensation annuity is established.

The contracts signed with the members of the Management Committee contain a clause that establishes a minimum indemnity of two annual remuneration in certain cases of extinction of the relationship, which include certain cases of change of control, dismissal unfairly or the assumptions contemplated in the articles . 40, 41 or 50 of the Workers' Statute. Likewise, the contracts signed with the members of the Management Committee and the Director of Internal Audit contain a clause that establishes an indemnity equivalent to an annuity of fixed remuneration for post-contractual non-competition for a period of two years.

On the other hand, compensation agreements exist with sixteen other managers, equivalent to a fixed annuity for non-post-contractual competition for a period of two years. In addition, twelve directors who partially agree with the previous ones have compensation agreements whose amounts entitle them to receive a minimum compensation of one fixed annuity in one case and two annual remuneration in others in certain cases of termination of the relationship, which include unfair dismissal or the assumptions contemplated in arts. 40, 41 or 50 of the Worker's Statute.

State whether such agreements must be reported to and/or approved by the decision-making bodies of the company or its group:

	Board of directors	General Shareholder's Meeting
Decision-making body approving the provisions	Yes	No
Is information about these provisions provided to the shareholders at the general shareholders' meeting?	Yes	No

C.2 Committees of the board of directors

C.2.1 Describe all of the committees of the board of directors, the members thereof, and the proportion of executive, proprietary, independent, and other external directors of which they are comprised:

Executive Committee

Nombre	Cargo	Tipología
Mr. Isidro Fainé Casas	Chairman	Proprietary
Mr. Ramón Adell Ramón	Member	Independent
Mr. Marcelino Armenter Vidal	Member	Proprietary
Mr. Francisco Belil Creixell	Member	Independent
Mrs. Benita María Ferrero-Waldner	Member	Independent
Mr. Josu Jon Imaz San Miguel	Member	Proprietary
Mr. Miguel Martínez San Martín	Member	Proprietary
Mr. Rajaram Rao	Member	Proprietary
Mr. Rafael Villaseca Marco	Member	Executive
Mr. William Alan Woodburn	Member	Proprietary

% executive directors	10
% proprietary directors	60
% independent directors	30
% other external directors	-

Explain the duties assigned to this committee, describe the procedures and rules of organization and operation thereof, and summarize the most significant activities thereof during the year.

a) Functions of the executive committee:

Aspects that are ordinarily not able to be delegated, however that may be adopted by the Executive Committee or by the Managing Director(s), by reasons of urgency, that have been duly justified, and that must be ratified at the first meeting of the Board of Directors that is held after the adoption of the decision.

- a) The approval of the management objectives, the annual financing plan, the investments and financing policy, the corporate social responsibility policy.
- b) The determination of the policy for the control and management of risks, including tax risks, and the supervision of the internal information and control systems.
- c) The determination of the corporate governance policy of the Company and of the Group of which the Company is the parent company; the organization and functioning thereof and, in particular, the approval and modification of the Regulations thereof.
- d) The approval of the financial information that, by reason that the Company is a listed company, must be periodically published by the Company.
- e) The definition of the structure of the group of companies of which the Company is the parent company.
- f) The approval of all types of investments and operations that, by reason of the significant sum or the special characteristics thereof, constitute strategic operations or are the subject of special tax risks, unless the approval thereof corresponds to the General Shareholders Meeting.
- g) The approval of the creation or acquisition of shareholdings in other special purpose entities or companies registered in countries or territories that are considered to be tax havens, as well as any other analogous transactions or operations that, by reason of their complexity, may undermine the transparency of the Company and its Group.
- h) The approval, subject to the prior report of the Audit Committee, of the operations that the Company or any of its Group companies carry out with Board Members, in the terms established in applicable legislation, or with shareholders that hold, either individually or jointly with other shareholders, a significant shareholding in the share capital of the Company, including shareholders that are represented on the Board of Directors of the Company or of other companies that form part of the corporate Group thereof or with any related-parties thereof.
- i) The determination of the tax strategy of the Company.

Aspects for which the resolutions or decisions thereof may be adopted, indistinctly, by the Board of Directors or by the Executive Committee.

- a) The definition of the general structure of delegations and empowerments.
- b) The incorporation of new companies or entities or the variation of the shareholdings in already existing companies.
- c) The approval of merger, take-over, split-off, integration or winding-up operations, with or without liquidation, for which any of the companies of the Group have any interests whatsoever.
- d) The disposal of shareholdings in the share capital of companies or of other fixed assets by any Group company.
- e) The approval of the investment projects to be implemented by any Group company.
- f) The approval of the programs for the issue and renewal of series of promissory notes, of debentures or of other similar securities by any Group company.
- g) The approval of financial operations, to be carried out by any Group company, that are not included in the Annual Financing Plan.
- h) The provision of guarantees and bonds by Group companies in order to guarantee the obligations of entities that do not belong to the Group, or that have, if they do belong to the Group, external partners.
- i) The assignment of rights regarding the commercial name and trademarks, as well as in respect of patents, technology and any other modality of industrial property that belongs to any Group company.
- j) The approval of the appointment and removal of the Trustees and other positions of the GAS NATURAL FENOSA FOUNDATION and of the natural persons legal representatives of GAS NATURAL SDG, S.A. in the situations in which GAS NATURAL SDG, S.A. is designated as the corporate director of any other company. Approval of contributions to sponsorship or patronage activities.
- k) The formalization of commercial, industrial or financial agreements that are of a relevant importance for the Group and that represent any modification, change or review of the current Strategic Plan or Annual Budget.

In relation to the aspects set out under paragraphs b), c), d), e), g), h) and i), the approval of the Board of Directors or the Executive Committee shall be required in relation to the resolutions or decisions that, by reason of the nature or amount thereof, are of special relevance for the Group. An operation shall be deemed to be of special relevance when the economic importance of the operation exceeds 15 million Euros, except in relation to paragraphs h) and i), in which case said limit shall be that of 5 million Euros and in respect of paragraph j), for which said limit shall be that of 200,000 Euros.

Unless any other regime is approved upon the adoption of the corresponding resolution or decision, it shall be considered that an investment or operation does not require any additional approval in the case of any deviation of the operation, when said deviation does not exceed 10% or a further 15 million Euros above of the amount authorised by the Board or, as the case may be, by the Executive Committee.

When necessary, the resolutions of the Board of Directors and of the Executive Committee must be adopted subject to the prior report of the pertinent Committee.

b) Procedures and rules of organization and operation:

The Executive Committee shall be comprised by the Chairman of the Board of Directors and by a maximum of another nine Board Members, that shall belong to the categories provided for under Article 3 of these Regulations, and shall be of a similar proportion to that of the existing Board of Directors. The designation of the members of the Executive Committee shall require the favorable vote of at least two thirds of the members of the Board.

The Chairman of the Board of Directors shall act as the Chairman of the Executive Committee and the Secretary of the Board shall act as the Secretary thereof, that may be substituted by the Deputy Secretary.

The Executive Committee shall be deemed to be validly constituted when half plus one of the members thereof are either present or represented.

The members of the Executive Committee shall be removed from office when they cease to be Board Members or when the Board removes them from the Executive Committee. The vacancies on the Executive Committee shall be newly designated as soon as practicable by the Board of Directors.

The permanent delegation of powers by the Board of Directors in favour of the Executive Committee shall include all of the powers of the Board, with the exception of the powers that are not able to be delegated, whether pursuant to legal provisions or the Articles of Association or pursuant to these Regulations.

The Executive Committee, which shall be called by the Chairman thereof, shall meet, whenever deemed necessary by the Chairman thereof or at the prior request of at least 1/3 of the members thereof. The Secretary shall draft the Minutes of the resolutions and decisions adopted at the meeting session thereof, which shall be detailed at the next plenary session of the Board of Directors.

In the cases in which, in the judgement of the Chairman or of the majority of the members of the Executive Committee, the importance of the matter so requires, the resolutions and decisions adopted by the Committee shall be submitted for the ratification of the plenary session of the Board.

The foregoing shall also be applicable to the matters that the Board had forwarded to the Executive Committee for the study and analysis thereof, whereby the Board reserves the right to adopt the final decision in relation thereto.

In all other cases, the resolutions and decisions adopted by the Executive Committee shall be valid and binding, without the need for any subsequent ratification thereof by the plenary session of the Board, without prejudice to the provisions of Article 5 of these Regulations.

The provisions of these Regulations in relation to the functioning of the Board of Directors shall, to the extent possible, also be applicable to the Executive Committee.

c) Most important activities during 2016

In the exercise of its powers, during the 2016 financial year it has analyzed, informed and / or adopted agreements on, among other things:

- > Quality and efficiency of its operation.
- > Various investment proposals.
- > Financial operations.
- > Status reports on different issues.

State whether the composition of the executive committee reflects the participation of the different directors within the board based on their class:

Yes

Audit Committee

Nombre	Cargo	Tipología
Mr. Ramón Adell Ramón	Chairman	Independent
Mr. Enrique Alcántara-García Irazoqui	Member	Proprietary
Mr. Xabier Añoveros Trías de Bes	Member	Independent
Mrs. Cristina Garmendia Mendizábal	Member	Independent
Mrs. Helena Herrero Starkie	Member	Independent
Mr. Rajaram Rao	Member	Proprietary
Mr. Luís Suárez de Lezo Mantilla	Member	Proprietary
% proprietary directors		42.86
% independent directors		57.14
% other external directors		–

Explain the duties assigned to this committee, describe the procedures and rules of organisation and operation thereof, and summarise the most significant activities thereof during the year.

a) Functions of Audit Committee:

The Committee has the powers established by the Law and those entrusted to it by the Board of Directors in general or in particular.

On November 27, 2015, the Board of Directors has entrusted the following functions:

- > Prepare the report on the independence of the Auditor.
- > Prepare the Report on the functioning of the Audit Committee.
- > Prepare the Report on related-party transactions.
- > Prepare the Report on corporate social responsibility policy.
- > Ensure that the Board of Directors seeks to present the accounts to the General Meeting of Shareholders without limitations or qualifications in the Audit Report and that, in the exceptional cases in which there are qualifications, both the Chairman of the Committee and the Auditors, clarify to shareholders the content and scope of such limitations.
- > In relation to information and control systems:
 - a) To supervise the preparation process and the integrity of the financial information relating to the company and, as the case may be, to the group, reviewing compliance with regulatory requirements, adequate delimitation of the consolidation perimeter and correct application of the accountant criteria.
 - (b) Ensure the independence of the unit that assumes the internal audit function; Approve the orientation and its work plans, ensuring that its activity is focused mainly on the relevant risks of society; Receive periodic information on their activities; And verify that senior management takes into account the conclusions and recommendations of its reports. To propose to the Chairman of the Board of Directors the selection, appointment, re-election and dismissal of the person in charge of the internal audit service, as well as to propose the budget for that service, with the last decision corresponding to the Chairman of the Board of Directors.
 - (c) Establish and supervise a mechanism that allows employees to communicate, on a confidential basis and, if it is possible and considered appropriate, anonymous, irregularities of potential significance, especially financial and accounting, that they notice within the company.

- > In relation to the external auditor.
 - a) In case of resignation of the external auditor, examine the circumstances that motivated it.
 - (b) Ensure that the remuneration of the external auditor for their work does not compromise their quality or independence.
 - (c) Supervise that the company reports as a relevant fact to the National Securities Market Commission the change of auditor and accompany it with a statement on the possible existence of disagreements with the outgoing auditor and, if they existed, on their content.
 - (d) Ensure that the external auditor holds a meeting with the board of directors annually to inform him of the work performed and of the evolution of the accounting and risk situation of the company.
 - (e) Ensure that the company and the external auditor comply with the current rules on the provision of non-audit services, the limits on the concentration of the auditor's business and, in general, the other rules on the independence of auditors.
- > Call any employee or manager of the Company, and even arrange for them to appear without the presence of any other manager.
- > Analyze and inform the Board of Directors about the economic conditions and the accounting impact and, in particular, where applicable, on the exchange ratio, in relation to the operations of structural and corporate modifications that, by their nature or quantity, have special relevance. Those transactions whose net value exceeds the value of 25% of the assets included in the last approved balance sheet of the Company shall be deemed to be relevant.
- > In relation to the supervision of compliance with the corporate governance rules, the Codes of Conduct and the corporate social responsibility policy.
 - a) The supervision of compliance with the internal codes of conduct and the corporate governance rules of the company.
 - (b) Supervision of the communication strategy and relationship with shareholders and investors, including small and medium shareholders.
 - (c) The periodic evaluation of the adequacy of the corporate governance system of the company, in order to fulfill its mission of promoting social interest and taking into account, as appropriate, the legitimate interests of the remaining interest groups.
 - (d) Monitoring and evaluation of the processes of relationship with the different stakeholders.
 - (e) The evaluation of all matters related to non-financial risks of the company - including operational, technological, legal, social, environmental, political and reputational.
 - (f) Coordination of the non-financial information and diversity reporting process, in accordance with applicable regulations and international reference standards.

b) Procedures and rules of organization and operation

The Audit Committee shall be comprised by a minimum of three and a maximum of seven Board Members, that shall be designated by the Board of Directors from among the Non Executive Board Members, and at least one of the Non-Executive Board Members thereof shall be designated taking into account his or her knowledge and expertise in accounting or audit fields, or in both fields. The members thereof shall be removed from office when they cease to be Board Members or when the Board removes them from the Audit Committee or by reason of the expiry of the period of three years after their appointment, however the members thereof may be re-elected.

The majority of the members of the Committee shall be Independent Board Members, from among which, the Board of Directors shall designate the Chairman of the Audit Committee, who shall not have a casting vote. The Secretary of the Board of Directors shall act as the Secretary of the Committee.

The Committee, which shall be called by the Chairman thereof, shall meet as often as necessary in order to issue reports or proposals in relation to its functions or when deemed necessary by the Chairman thereof, or at the prior request of at least two of the members thereof and, shall meet at least four times a year. The meeting notification must be issued at least two days prior to the date set down for the meeting thereof, except in the case of any justified and reasoned urgency. The meetings shall ordinarily take place at the registered office of the Company. The Committee may invite any manager or employee that it deems necessary to attend the meetings.

c) Most important activities during 2016

In the exercise of its powers, during the 2016 financial year it has informed and/or adopted proposals on, among other things:

- > Quality and efficiency of its operation.
- > External audit of individual and consolidated annual accounts.
- > Economic information.
- > Appointment of Auditors.
- > Tax status report.
- > Independence of Auditor.
- > Related-party transactions.

Identify the director who is a member of the audit committee and who has been appointed taking into account the director's knowledge and experience in the areas of accounting, audit, or both, and report the number of years that the chair of this committee has held office.

Name of director with experience	Mr. Ramón Adell Ramón
Number of years during which chair has held the position	2

Appointments and remuneration committee

Name	Position	Class
Mr. Francisco Belil Creixell	Chairman	Independent
Mr. Alejandro García-Bragado Dalmau	Member	Proprietary
Mrs. Cristina Garmendia Mendizábal	Member	Independent
Mr. Miguel Martínez San Martín	Member	Proprietary
Mr. William Alan Woodburn	Member	Proprietary

% proprietary directors	60
% independent directors	40
% other external directors	-

Explain the duties assigned to this committee, describe the procedures and rules of organisation and operation thereof, and summarise the most significant activities thereof during the year.

a) Functions of the Appointments and Remuneration Committee:

The Committee has the powers established by the Law and those entrusted to it by the Board of Directors in general or in particular.

The Board of Directors has entrusted the following duties:

- > Prepare the report on the functioning of the Appointments and Remuneration Committee.
- > Verify the policy for the selection of Directors and report it in the Annual Corporate Governance Report.
- > By delegation to be given by the Chairman of the Board, organize and coordinate the periodic evaluation of the Board and the first executive manager of the Company.
- > Prepare the report on the functioning of the Board of Directors.
- > To propose to the Board of Directors the basic conditions of the contracts of the senior managers.
- > Verify compliance with the remuneration policy established by the Company.
- > Periodically review the remuneration policy applied to directors and senior managers, including remuneration systems with actions and their application, as well as to ensure that their individual remuneration is proportionate to the remuneration of other directors and senior executives of the company.
- > Ensure that any conflicts of interest do not undermine the independence of the external advice provided to the commission.
- > Verify information on the remuneration of directors and senior executives contained in the various corporate documents, including the annual report on directors' compensation.
- > By agreement of the Board of Directors of January 29, 2016, it was entrusted to exercise all the powers in matters of corporate social responsibility that until that date were exercised by the Audit Committee.

b) Procedures and rules of organization and operation:

The Appointments and Remuneration Committee shall be comprised by a minimum of three and a maximum of five Board Members that shall be designated by the Board of Directors from among the Non-Executive Board Members, taking into account the knowledge and skills thereof. The members thereof shall be removed from office when they cease to be Board Members or when the Board of Directors removes them from the Appointments and Remuneration Committee or by reason of the expiry of the period of three years after their appointment, however the members thereof may be re-elected.

At least two members of the Appointments and Remuneration Committee shall be Independent Board Members and, from among the Independent Board Members thereof, the Board of Directors shall designate the Chairman of the Appointments and Remuneration Committee, who shall not have a casting vote. The Secretary of the Board of Directors shall act as the Secretary of the Committee.

The Committee, which shall be called by the Chairman thereof, shall meet as often as necessary in order to issue reports or proposals in relation to its functions or when deemed necessary by the Chairman thereof, or at the prior request of at least two of the members thereof. The meeting of the Committee shall be called by the Chairman, at least two days prior to the date set down for the meeting thereof, except in the case of any justified and reasoned urgency. The meetings shall ordinarily take place at the registered office of the Company. The Committee may invite any manager or employee that it deems necessary to attend the meetings.

c) Most important activities during 2016:

In the exercise of its powers, during the 2016 financial year it has informed and/or adopted proposals on, among other things:

- > Annual report on the remuneration of Directors.
- > Degree of achievement of the Group's objectives.
- > Remuneration of employees.
- > Quality and efficiency of its operation.
- > Re-election, ratification or appointment of Directors.

C.2.2 Complete the following table with information regarding the number of female directors comprising the committees of the board of directors for the last four financial years:

	Number of female directors							
	Financial year 2015 Number %		Financial year 2014 Number %		Financial year 2013 Number %		Financial year 2012 Number %	
Executive Committee	1	10	0	0	0	0	0	0
Audit Committee	2	28.57	0	0	0	0	0	0
Appointments and Remuneration Committee	1	20	1	33	0	0	0	0

C.2.3 Section deleted.

C.2.4 Section deleted.

C.2.5 State, if applicable, the existence of regulations of the board committees, where such regulations may be consulted, and the amendments made during the financial year. Also state if any annual report of the activities performed by each committee has been voluntarily prepared.

The Committees are regulated under the Articles of Association and the Regulation regarding the organization and functioning of the Board of Directors and its Committees of Gas Natural SDG, S.A.

Both documents are published in the website of the Company (www.gasnaturalfenosa.com) >Shareholders and Investors>Corporate Governance>Governing Regulations.

During 2016, the following articles related to said Committees have been modified: Articles 5, 30 and 32 of the Regulations of the Board of Directors, with a view to making the principle of proportional representation of shareholders compatible with the existence of an adequate number of independent Directors in full Respect to the current legislation.

Thus, the number of members of the Executive Committee is 10, of which 60% (six directors) are proprietary directors (2 appointed by Criteria Caixa, SAU, 2 by Repsol, SA and 2 by GIP III Canary 1, S .À RL), or that is in line with the shareholding that each of these Companies holds in GAS NATURAL SDG. The number of members of the Audit Committee is 7, of which 4, the majority, are independent and 3 proprietors, one representing each of the shareholders with stakes of 20% or more. The Appointments and Remuneration Committee has 5 members, of which 3 (60%) represent each of the shareholders with 20% or more shareholding and 2 (40%) are independent.

Both the Executive Committee and the Audit Committee and the Appointments and Remuneration Committee have produced a report on the quality and effectiveness of their operation during the previous year.

C.2.6 Section deleted.

D. Related-party transactions and intragroup transactions

D.1 Explain any procedures for approving related-party and intragroup transactions.

Procedure for the approval of related-party transactions

According to art. 5.II of the Regulations of the Board of Directors, powers of the Board which may not be delegated but may be adopted by the Executive Committee or by the Chief Executive Officer on duly justified grounds of urgency and which shall be ratified by the first Board of Directors following the adoption of the decision, one of them is the approval, following a report by the Audit Committee, on the operations carried out by the Company or its group companies with directors, under the terms established in current legislation, or with shareholders holding, individually or in concert with others, of a significant shareholding, including shareholders represented in the Board of Directors of the Company or other companies that are part of the same group or with persons related to them.

Moreover, art. 6.5 of the Regulations of the Board indicates that the Board of Directors will include in the Annual Report and in the Annual Corporate Governance Report information on transactions with significant shareholders (total volume of transactions and nature of the most relevant ones) so that other shareholders may know its scope and importance.

On 30 September 2011 the Board of Directors, following a favorable report from the Appointments and Remuneration Committee (then competent), agreed to grant a generic authorization to the related polyethylene network purchase transactions of Repsol Butano, S.A. which are carried out under normal market conditions. This authorization is executed by the General Director of Regulated Businesses.

The Board of Directors on 25 May 2012, following a favorable report from the Nominating and Compensation Committee (then competent), granted a generic authorization for ordinary operations carried out under market conditions with Caixabank, S.A., or with any entity belonging to "la Caixa" Group relating to: opening of current bank accounts, temporary financial investments generated by cash surpluses from current operations, management of receipts at collection, various payments related to usual operations (payroll, Taxes, social security, suppliers and others of a similar nature), issuance of VISA and equivalent cards, purchase and sale of currency in cash or in advance before payment and collection of invoices in foreign currency approved, confirmation of letters of credit, of interest rate derivatives, as well as ISDA and CMOF contracts, as well as any other of a similar nature, which cover all or some of the foregoing transactions). This authorization is executed by the Economics and Finance Director General.

Following a favorable report from the Audit Committee, the Board of Directors on July 22, 2016 adopted the agreement on the realization under the ISDA framework of operations with Repsol, S.A., relating to OTC of electricity, gas and CO₂. This authorization is executed by the General Director of Wholesale Energy Businesses.

D.2 Describe those transactions that are significant due to the amount or subject-matter thereof between the company or entities of its group and the company's significant shareholders:

Individual or company name of the significant shareholder	Individual or company name of the company or entity within its group	Nature of the relationship	Type of transaction	Amount (thousands of euros)
Fundación Bancaria Caixa d'estalvis i Pensions de Barcelona (la Caixa)	Gas Natural SDG, S.A.	Commercial	Interest charged	2,752
Fundación Bancaria Caixa d'estalvis i Pensions de Barcelona (la Caixa)	Gas Natural SDG, S.A.	Commercial	Interest accrued but not paid	47
Fundación Bancaria Caixa d'estalvis i Pensions de Barcelona (la Caixa)	Gas Natural SDG, S.A.	Commercial	Contributions to pension plans and life insurance	24,541
Fundación Bancaria Caixa d'estalvis i Pensions De Barcelona (la Caixa)	Gas Natural SDG, S.A.	Commercial	Services received	15,160
Fundación Bancaria Caixa d'estalvis i Pensions de Barcelona (la Caixa)	Gas Natural SDG, S.A.	Commercial	Interest paid	247
Fundación Bancaria Caixa d'estalvis i Pensions de Barcelona (la Caixa)	Gas Natural SDG, S.A.	Commercial	Provision of services	462
Fundación Bancaria Caixa d'estalvis i Pensions de Barcelona (la Caixa)	Gas Natural SDG, S.A.	Commercial	Sales of finished or non-finished goods	1,243
Fundación Bancaria Caixa d'estalvis i Pensions de Barcelona (la Caixa)	Gas Natural SDG, S.A.	Commercial	Financing agreements: other	513,062
Fundación Bancaria Caixa d'estalvis i Pensions de Barcelona (la Caixa)	Gas Natural Sdg, S.a.	Commercial	Sales of intangible assets	274,528
Fundación Bancaria Caixa d'estalvis i Pensions de Barcelona (la Caixa)	Gas Natural SDG, S.A.	Commercial	Financing agreements: loans	123,316
Fundación Bancaria Caixa d'estalvis i Pensions de Barcelona (la Caixa)	Gas Natural SDG, S.A.	Commercial	Guarantees	100,000
Fundación Bancaria Caixa d'estalvis i Pensions de Barcelona (la Caixa)	Gas Natural SDG, S.A.	Commercial	Management contracts	480,720
Fundación Bancaria Caixa d'estalvis i Pensions de Barcelona (la Caixa)	Gas Natural SDG, S.A.	Commercial	Dividends and other distributed benefits	424,923

Individual or company name of the significant shareholder	Individual or company name of the company or entity within its group	Nature of the relationship	Type of transaction	Amount (thousands of euros)
Repsol, S.A.	Gas Natural SDG, S.A.	Commercial	Services received	8,853
Repsol, S.A.	Gas Natural SDG, S.A.	Commercial	Purchase of finished or non-finished goods	236,845
Repsol, S.A.	Gas Natural SDG, S.A.	Commercial	Provision of services	1,363
Repsol, S.A.	Gas Natural SDG, S.A.	Commercial	Sales of finished or non-finished goods	694,196
Repsol, S.A.	Gas Natural SDG, S.A.	Commercial	Purchase of fix assets or goods	424,651
Repsol, S.A.	Gas Natural SDG, S.A.	Commercial	Dividends and other distributed benefits	367,291
Gip III Canary 1, S.À R.L.	Gas Natural SDG, S.A.	Commercial	Dividends and other distributed benefits	66,045

D.3 Describe those transactions that are significant due to the amount or subject-matter thereof between the company or entities of its group and the company's directors or officers:

Individual or company name of directors or officers	Individual or company name of related party	Relation	Nature of the relationship	Amount (thousands of euros)
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D.4 Report the significant transactions made by the company with other entities belonging to the same group, provided they are not eliminated in the preparation of the consolidated accounts and they are not part of the ordinary course of business of the company as to their purpose and conditions.

In any case, report any intragroup transaction with entities established in countries or territories considered to be tax havens:

Name of the entity within the group	Brief description of the transaction	Amount (thousands of euros)
Global Power Generation, S.A.	Dividendos percibidos de Buenergía Gas & Power, Ltd.	6,036

D.5 State the amount of transactions with other related parties.

0 (thousands of Euros)

D.6 Describe the mechanisms used to detect, determine, and resolve potential conflicts of interest between the company and/or its group, and its directors, officers, or significant shareholders.

1. Directors:

According to the Regulations of the Board of Directors:

The Board Members are subject to the duty of loyalty in the terms established under applicable legislation and, in particular:

- > The Board Members must abstain from participating in the deliberations and voting procedures in relation to resolutions or decisions in which he or she or any related party is subject to any direct or indirect conflict of interest. The foregoing shall exclude the obligation to abstain from resolutions or decisions that affect the Board Member in his or her capacity of director of the Company, such as the designation or revocation thereof in relation to positions within the governing body or other similar positions.
- > Furthermore, the Board Member must adopt the measures necessary in order to avoid situations in which his or her interests, whether directly or indirectly in relation to any third-party, may be subject to any conflict of interest with the Company's interests and with his or her duties to the Company.
- > In their capacities of loyal and prudent representatives of the Company, the Board Members must inform the Company of the shares of the Company that they hold, whether directly or indirectly through companies in which they hold a significant shareholding, in accordance with the procedure and the other formalities established for investments in shares of Gas Natural SDG, S.A. and the subsidiary companies thereof.
- > The Board Members must notify the Company of any significant changes to their professional situation and any changes that affect the nature or category in which the Board Members are classified.
- > The Board Members shall inform the Company of any type of legal or administrative claim whatsoever or of any facts that may relate to the Board Members that, by reason of the importance thereof, may seriously affect the reputation of the Company. The Board shall examine the situation and shall adopt the measures that are required in the interests of the Company, with the required urgency.

The Board of Directors shall, at all times, use its best endeavours to avoid that the Proprietary Board Members exercise their powers or position in order to obtain equity advantages without the adequate consideration or balancing entry, in benefit of the shareholder that has proposed the appointment of the Proprietary Board Members.

The Board Members must abstain from carrying out activities, either on their own behalf or for any third party, that would constitute effective competition, whether real or potential, with the Company or that, in any other way whatsoever, would create any permanent conflict of interest with the Company. In particular, Board Members must not perform, either directly or indirectly, any positions of any nature at competitor companies or entities of Gas Natural SDG S.A. or of any company of its Group, and must not provide, in favour of said companies or entities, any representation or advisory services whatsoever. A company or entity shall be deemed to constitute a competitor of Gas Natural SDG, S.A., when it is engaged, whether directly or indirectly, or through its Group companies, in activities included within the corporate activities of Gas Natural SDG, S.A.

2. Directors and senior officers:

Moreover, the Internal Code of Conduct in connection with the Securities Markets of Gas Natural SDG, S.A., establishes in its section 6 the information that the Directors and executives of the entity must provide in respect of conflicts of interest:

“6.1. The parties bound by this Internal Code of Conduct are obliged to notify the Secretary of the Board of Directors of Gas Natural SDG, S.A. of any conflicts of interest that might arise with the companies in which they have an interest or with their personal or family property or with any other factor that might interfere with the performance of the activities covered by this Code.

If there are doubts as to whether or not there is a conflict of interest, the bound parties must consult with the Secretary of the Board of Directors of Gas Natural SDG, S.A., who will issue a decision in writing. The Secretary may refer the matter to the Nomination and Remuneration Committee when he/she considers it advisable because of the magnitude of the matter.

Parties affected by possible conflicts of interest must keep the information up to date and report any change or cessation of the situation that they reported previously.

6.2. Affected persons must abstain from participating in the adoption of any decision that might be affected by the conflict of interest with the Company.”

3. Significant shareholders:

The Board of Directors, following a report by the Audit Committee, approves the operations carried out by the Company or its group companies with Board Members, under the terms established by current legislation, or with individual shareholders, individually or in concert with others, a significant participation, including shareholders represented on the Board of Directors of the Company or other companies that are part of the same group or with persons related to them.

D.7 Is more than one company of the group listed in Spain?

No

Identify the subsidiaries listed in Spain:

E. Control systems and risk management

E.1 Explain the scope of the Risk Management System of the company including all tax aspects thereof.

The Risk Management System is an integral system that is continuously operative, that consolidates the management activities per area or business unit or activity, subsidiaries, geographic zones and support areas (such as, for example, human resources, marketing or management control) at a corporate level, and quantifies the impact of the main risk factors and also guarantees the homogeneity for the criteria used to measure said risk factors.

The purpose thereof is to forecast any potential deviations in relation to the global targets and to guarantee that the decision-making process takes into consideration an adequate balance between risk and returns, from the perspective of both the marginal contribution to the global portfolio as well as in relation to each one of the different businesses.

The purpose of the risk management system at Gas Natural Fenosa is to guarantee the predictability and sustainability of the operative and financial performance of the Company.

E.2 State the bodies of the company that are responsible for the drafting and implementation of the Risk Management System including all tax aspects thereof.

Audit Committee

The Audit Committee is the highest supervisory body for the efficacy of the internal control and of the risk management systems of the Company. The Committee ensures that the foregoing systems identify the different types of risk and the measures established to mitigate and manage said risks if indeed they occur in the form of effective losses or damages to the Company.

Risk Analysis Committee

The Risk Analysis Committee is responsible for determining and reviewing the target Risk Profile of the Company. The Committee ensures that said risk profile is aligned with the strategic position of the Company and protects the interests of the interest groups thereof. Furthermore, the Committee ensures that all members of the organisation understand and accept their responsibility for the identification, assessment and management of the most relevant risks.

Risk Units

The Risk Units report directly to the Economic and Financial Department, which provides said Department with the corporate vision necessary for the carrying out of its functions, without prejudice to the fact that specific Wholesale Business Risk and Retail Business Risk management units also report to the Economic and Financial Department, in close contact with the business units that have the highest exposure to risk by reason of their profile and turnover.

The purpose of the Risk Units is to externalise exposure to the uncertainties and to internalise the levels of exposure to risk in the decision-making processes of senior management, as an instrument for the effective selection of returns. The Risk Units are responsible for coordinating the different agents involved in risk management. The monitoring and assessment of the exposure to risk pursuant to an integrated approach enables the Company to maximise the efficacy of its decision-making procedures, by optimising the returns/risk binomial.

The Risk Units are responsible for ensuring the maintenance of the global risk profile, as well as for the permanent measurement and control of the risk.

The Businesses

The Businesses are responsible for risk management within their pertinent areas. The Businesses identify the trends and positions that may imply risk and reports said risks to the Risk Units, and they also apply the management directives and criteria issued by the Risk Units.

The risk management is based upon a series of key concepts which include the concept of the Risk Profile, which is considered to mean the level of exposure to the uncertainty as a result of the joint incidence of different categories of risk identified by Gas Natural Fenosa.

Other corporate areas

Other corporate areas are responsible for the monitoring and management of certain risks, by reason of the specific nature and the particularities of the management mechanisms thereof. For example, the Environmental and Quality Control Department, that is responsible for the environmental risk and climate change, and the Reputation and Sustainability Department, that manages reputational risks. The foregoing areas operate in coordination with the Risk Units.

E.3 State the main risks, including all tax risks, that the company is subject to in relation to its business targets.

	Description	Risk Management
Market risk		
Price of gas	Volatility in international markets that determine the price of gas.	Physical and financial hedging.
Price of electricity	Volatility of electricity markets in Spain and Portugal.	Physical and financial hedging. Optimisation of the electricity generation assets.
Volume of gas	Deviation between the supply and demand of gas.	Optimisation of contracts and assets. Trading.
Volume of electricity	Reduction of the available thermal generation gap.	Optimisation of the electricity marketing/generation balance.
Regulation	Exposure to the review of the recognised criteria and of profitability levels for regulated activities.	Intensification of the communication with regulatory authorities. Adjustment of efficiencies and investments at recognised rates.
Exchange rate	Volatility in the international currency markets.	Geographic and macro-economic diversification through inflation rates. Hedging by way of financing in local currencies and derivatives.
Interest rate and credit spread	Volatility in the financing facility rates.	Financial hedging. Diversification of the financing sources.
Tax	Ambiguity or subjectivity in the interpretation of the applicable tax regulations, or by the substantiation modification thereof.	Queries to independent expert bodies. Contracting of first tier consultancy firms. Ratification of the Code of Good Tax Practices. Allocation of provisions with prudent criteria.

	Descripción	Gestión
Credit risk		
Credit	Potential increase of payment default, conditional upon economy recovery in Spain.	Analysis of the solvency of customers to define specific contractual terms and conditions. Debt recovery procedures. Systematization of the calculation of the economic capital.
Operational risk		
Operational risk: image and reputation	Deterioration of the perception of Gas Natural Fenosa from different interest groups.	Identification and monitoring of potential reputational events. Communication transparency.
Operational risk: insurable	Accidents, damages or unavailability of the assets of Gas Natural Fenosa.	Continuous improvement plans.
Operational risk: the environment	Damages to the natural and/or social environment. Trends of environmental regulation.	Emergency plans in facilities subject to risk of environmental accidents.
Operational risk: climate change	Trends of environmental factors as a result of climate change. Regulation to combat climate change.	Participation in clean Development Mechanisms. Frequent communication with regulatory authorities.

E.4 State whether the company has a tolerance level in relation to the risk, including tax risks.

The Company has tolerance levels established at a corporate level for the main types of risk.

The risk assessment process begins with the identification of the risks, generally by the businesses that are exposed thereto. Said identification takes place at the time at which the exposure exists. Notwithstanding the foregoing, on an annual basis the Risk Units carry out a detailed review of the risks in order to guarantee the correct identification of all of the exposures, whether current or potential risks.

The Risk Units are responsible for carrying out the assessment of the identified risks, in light of:

- a) Position at risk: Definition and characteristics.
- b) Impact variables.
- c) Qualitative and quantitative severity in the case of the occurrence of the risk.
- d) Probability of the risk taking place.
- e) Risk mitigation controls and mechanisms used and the efficacy thereof.

Finally, a tolerance level shall be proposed for the types of risks identified, that shall be approved by the Risk Analysis Committee.

E.5 State which risks, including tax risks, have taken place during the year.

The main risk that has occurred during the year is related to the tensions that exist in respect of the prices of commodities, and in particular of crude oil and derivatives, and from the pool in Spain. Furthermore, during the first half-year period the main South American currencies have also devaluated.

Notwithstanding the foregoing, the risk control mechanisms have enabled the Company to keep the impact thereof within the established tolerance range, defined by means of the current risk limits.

E.6 Explain the response and supervision plans for the main risks of the entity, including tax risks.

The risks regarding the performance of Gas Natural Fenosa are set out in the Risks Map of the Company. Said map is the main communication instrument for the Audit and Control Committee in respect of its risks supervision functions of the Company.

At an operational level, the Risk Units and other specific areas (Regulation, Environment, Electricity Generation) carry out periodic measurements of the trends of the main risks, and set out the pertinent indications in the case that any exposure levels or trends are detected that may exceed the established tolerances.

F. Internal Risk Control And Management Systems In Relation To The Process For The Issue Of Financial Reporting (ICSFR)

Describe the mechanisms that comprise the risk control and management systems in relation to the process for the issue of financial reporting (ICSFR) of your company.

F.1 Control of the Company

State, including the main characteristics thereof, at least:

F1.1 Which bodies and/or functions are responsible for: (i) the existence and maintenance of an adequate and effective ICSFR; (ii) the implementation thereof; and (iii) the supervision thereof.

Gas Natural Fenosa has defined its Internal Control System on Financial Reporting (hereinafter, "ICSFR") in the "General Guidelines of the Internal Control System on Financial Reporting (ICSFR) of Gas Natural Fenosa".

As part of the ICSFR, Gas Natural Fenosa has defined, in the aforementioned General Guidelines, the responsibilities model thereof. Said model is defined in relation to the following five ambits of responsibility:

- > Board of Directors: Is responsible for the existence of an adequate and effective ICSFR, the supervision of which is delegated upon the Audit Committee.

The Regulations regarding the Organisation and Functioning of the Board of Directors of Gas Natural SDG, S.A. and its Committees, in Article 5, paragraph II thereof, provides that the determination of the policy for the control and management of risks, including tax risks, and the supervision of the internal reporting and control systems is, among other functions, an aspect that is ordinarily no able to be delegated by the Board of Directors.

- > Audit Committee: This Committee is, *inter alia*, responsible for the supervision of the ICSFR. Article 32, paragraph 2 of the Regulations of the Board of Directors states that the Committee shall have the powers that are provided for under the Corporate Enterprises Act and the powers that are generally or specifically conferred by the Board of Directors. Thus, the Corporate Enterprises Act, at Section 529 *quaterdecies* thereof, states, at paragraph 4.b), that the Audit Committee shall have the function of supervising the efficacy of the internal control of the company, the internal auditing and the risk management systems, as well as the function of discussing with the accounts auditor the significant weaknesses of the internal control system detected during the audit. In particular and in relation to the reporting and control systems, the Audit Committee is responsible for, *inter alia*, the supervision of the process for the drafting and for the integrity of the financial reporting of the Company and, as the case may be, the group, and for reviewing the compliance of the required guidelines, the adequate delimitation of the scope of the consolidated accounts and the correct application of the accounting criteria. For the carrying out of part of the foregoing functions the Audit Committee is supported by the Internal Auditing, Compliance and Control Unit.
- > Economic and Financial Department: Is responsible for the design, implementation and functioning of the ICSFR. For the carrying out of this function, the Economic and Financial Department is supported by the Internal Control on Financial Reporting Unit.
- > Internal Auditing, Compliance and Control Unit. In general, this unit is responsible for supporting the Audit Committee in the supervision and continuous assessment of the efficacy of the Internal Control System in all aspects of Gas Natural Fenosa, by providing a methodical and rigorous approach for the monitoring and improvement of the processes and for the assessment of the operational risks and controls associated thereto, including the risks and controls that correspond to the ICSFR and to the Crime Prevention Model.
- > Business units and corporate units involved in the process for the drafting of financial reporting. They are responsible for executing the processes and for maintaining the daily operations and ensuring that the implemented control activities are performed.

F1.2 Whether, especially in relation to the process for the drafting of the financial reporting, the following elements exist:

- > **Departments and/or mechanisms responsible for: (i) the design and review of the organisational structure; (ii) clearly defining the lines of responsibility and authority, with an adequate distribution of tasks and functions; and (iii) ensuring that sufficient procedures exist for the correct dissemination thereof within the company.**

The design and review of the organisational structure of the senior management, as well as the definition of the lines of responsibility are carried out by the Board of Directors, by means of the Managing Director and by the Appointments and Remuneration Committee.

In order to guarantee the adequate management of the economic and financial reporting of the group, the Economic and Financial Department has developed, as part of the ICSFR, a technical instruction that consists of a map of interrelationships (reporting flows) regarding the process of the drafting of the financial reporting which sets out the communications between the Economic and Financial Department, the different process managers and the persons responsible for the source or the application of the financial reporting and that is referred to as "Map of interrelationships regarding the financial reporting of Gas Natural Fenosa".

Accordingly, Gas Natural Fenosa has taken into account six different aspects for the drafting of the map of interrelationships regarding the processes for the drafting of the financial reporting:

- (i) the information necessary for the drafting of the financial reporting;
- (ii) the persons responsible for the source or the application of the financial reporting and
- (iii) the distribution of tasks among the different organisational units
- (iv) the scope of said distribution to all of the companies within the group
- (v) the frequency of the reporting of the information
- (vi) the information systems that are involved in the drafting process and for the issue of the financial reporting;

Accordingly, by means of the map of interrelationships of Gas Natural Fenosa, the processes that relate to the drafting of the financial reporting are clearly defined, including both the operational processes with relevant impacts regarding the financial reporting as well as the processes related to the administration and accounting area, and the persons responsible for said information.

- > **Code of conduct, approval body, degree of dissemination and instruction, principles and values included therein (stating whether special mentions exist regarding the registration of operations and the drafting of financial reporting), body responsible for analysing breaches and for proposing corrective actions and sanctions.**

The commitments of the senior management of Gas Natural Fenosa include their undertaking to use their best endeavours to ensure that the operations are carried out within the context of ethical professional practices, and not only through the implementation of mechanisms for the purpose of preventing and detecting fraudulent conduct committed by employees, or inappropriate practices that may imply sanctions, fines or that may damage the image of Gas Natural Fenosa, but rather through by enhancing the importance of the ethical values and principles of integrity among their professional staff.

Accordingly, Gas Natural Fenosa has implemented a Code of Conduct (hereinafter, the "Code of Ethics"), that was approved by the Board of Directors at its meeting held on 31 March 2005, that is binding upon all of the employees of Gas Natural SDG, S.A. and all of the subsidiary companies in which Gas Natural Fenosa controls the management activities thereof. The updates and modifications of the Code of Ethics are carried out by the Board of Directors of Gas Natural SDG, S.A.

As from the ratification thereof, the Code of Ethics has been modified on four occasions, the most recent of which took place on 27 June 2014, in order to update the code and to incorporate new commitments assumed by Gas Natural Fenosa in relation to the entry into force of the reform of the Spanish Criminal Code (Act 5/2010), the implementation of a Crime Prevention Model within the Group, the issue of the Anti-Corruption Policy of Gas Natural Fenosa and in order to adapt the code to the best practices of Corporate Responsibility.

The Code of Ethics sets out the general ethical principles of Gas Natural Fenosa, that define the values to be followed in practice throughout the organisation and that include: (i) Purpose (ii) scope of application (implication of all of the members of Gas Natural Fenosa); (iii) fundamental principles of conduct at Gas Natural Fenosa (declaration of the style of government of the group); (iv) conduct guidelines (declaration of the key values of Gas Natural Fenosa); (v) acceptance and compliance of the Code; (vi) Code of Ethics Committee and (vii) term.

The Code of Ethics considers integrity and responsibility in the exercise of professional activities to constitute a fundamental general criteria for conduct at Gas Natural Fenosa. In particular, the Code of Ethics establishes a series of conduct guidelines that are to a greater or lesser extent related to the reliability of the financial reporting and with the compliance of applicable regulations, and in particular:

- Respect for legality, human rights and ethical values. (Section 4.1)

“Gas Natural Fenosa is committed to acting at all times in accordance with applicable legislation, with the internal Regulatory System established with internationally accepted ethical practices, with complete respect for human rights and public liberties (...)”

- Treatment of information and knowledge (Section 4.11):

“All employees who enter information of any type into the group’s computer systems must ensure its rigour and reliability.

In particular, all financial transactions of the group must be shown clearly and accurately in the corresponding records, through the corresponding Accounting Accounts, and in all operations that are conducted, including all income and incurred expenses.

Employees of Gas Natural Fenosa will abstain from any practices that contravene the commitment to clearly and accurately reflect all the financial transactions in the group’s Accounts.”

Furthermore, Gas Natural Fenosa has established an Anti-Corruption Policy, which was approved by the Steering Committee at its meeting held on 3 March 2014, and modified at the meeting held on 24 November 2015, which is binding upon all of the employees of all of the companies that comprise the Gas Natural Fenosa group and in which Gas Natural Fenosa holds majority shareholdings as well as the companies in which Gas Natural Fenosa is responsible for the operations and/or management thereof. The Policy is understood to be an extension of Chapter 4.7. “Corruption and bribery” of the Code of Ethics of the group and the purpose thereof is to establish the principles that must be adhered to by all of the employees and directors of the companies of Gas Natural Fenosa in relation to the prevention, detection, investigation and remedy of any corrupt practice within the organisation.

Furthermore, Gas Natural Fenosa has an Internal Code of Conduct for aspects related to the Securities Market, that has also been approved by the Board of Directors of the Company.

In July 2005 the Code of Ethics Committee of Gas Natural Fenosa was established with the principal mission of promoting the dissemination and application of the Code of Ethics within the entire group and for providing a communication channel for all employees in order to receive queries and notifications regarding breaches of the Code and of the Anti-Corruption Policy.

In order that the Code of Ethics Committee is able to exercise its functions in an objective and independent manner, the Committee is chaired by the Internal Auditing, Compliance and Control Unit and is formed by representatives of different units involved in the monitoring of compliance of the Code of Ethics and the Anti-Corruption Policy.

The Committee reports regularly to senior management and to the Audit Committee. The purpose thereof is to provide reports and recommendations, and to propose corrective actions to the units responsible for the provision of solutions to the problems related to the practical application of the Code of Ethics and of the Anti-Corruption Policy and furthermore to act as a liaison between said units and the employees.

The sanctionary regime, where necessary, is established by the Human Resources Unit.

Furthermore, the Code of Ethics Committee may propose, and in fact has done so on several occasions, updated of the terms of the Code. Said updates are, first of all, approved by the Audit Committee and, thereafter, ratified by the Board of Directors.

Moreover, Local Code of Ethics Committees have been established that are responsible for promoting the dissemination and application of the Code in certain countries in which Gas Natural Fenosa operates, namely, in Argentina, Brazil, Chile, Mexico, Colombia, Panama, Italy and Moldavia.

In order to promote not only the exercise of said responsibility but also the knowledge and dissemination of the Code of Ethics, the Code of Ethics is available in 9 languages:

- Externally: the corporate website of Gas Natural Fenosa.
- Internally, on the Naturalnet group platform.

Furthermore, online training courses have been developed through the Corporate University of Gas Natural Fenosa, that are obligatory for all of the employees of Gas Natural Fenosa.

Gas Natural Fenosa, through the Code of Ethics Committee, periodically carries out Declaration of Compliance of the Code of Ethics and Anti-Corruption Policy campaigns, in order to establish the conduct guidelines that are expected of all employees, as well as to disseminate the mechanisms that exist for carrying our queries and notifications, and to periodically formalise the commitment of all of the employees of the group in accordance with the ethical guidelines and principles of integrity.

Gas Natural Fenosa, in order to promote the knowledge of the Code of Ethics among its suppliers and collaborating companies includes in its General Contracting Terms and Conditions a clause that promotes among its suppliers practices in harmony with the conduct guidelines included in the Code of Ethics of Gas Natural Fenosa, and the suppliers are notified of where they may obtain a copy of the Code of Ethics of the group, and are also provided with information regarding the queries and notifications channels for aspects related to the Code of Ethics. Furthermore, in 2016 the Code of Ethics for Suppliers was approved and published, the purpose of which is to establish the guidelines that must govern the ethical behaviour of suppliers, contractors and external collaborators of Gas Natural Fenosa. Said Code sets out the commitments provided for under the United Nations Global Compact as well as under the Code of Ethics, the Human Rights Policy, the Corporate Responsibility Policy and the Anti-Corruption Policy of Gas Natural Fenosa.

➤ **Complaints channel, that provides for the notification to the Audit Committee of financial and accounting irregularities, as well as potential breaches of the Code of Conduct and irregular activities within the organisation, and state whether said channel is confidential.**

At Gas Natural Fenosa the concept of professional ethics is centered upon integrity and professional responsibility, where the concept of integrity is understood to mean ethical, honourable and good faith actions and the concept of professional responsibility is understood to mean proactive and efficient actions for excellence, quality and professional service.

As provided for under Article 32.2 of the Regulations of the Board of Directors and its Committees, "the Audit Committee shall have the powers that are provided for under the Corporate Enterprises Act and the powers that are generally or specifically conferred by the Board of Directors". Accordingly, the powers of the Audit Committee include the power to "establish and supervise a mechanism that enables employees to communicate, confidentially and, if possible and if considered appropriate, anonymously, any potentially significant irregularities, in particular of a financial and accounting nature within the company".

In harmony with the foregoing, the Board of Directors, at its meeting held on 31 March 2006, established that the notifications received through the notification procedure for breaches of the Code of Ethics of Gas Natural Fenosa, related to fraudulent practices, audits or deficiencies in the accounting and internal control thereof, shall be directly notified to the Audit Committee.

As a mechanism for obtaining a higher degree of internal control regarding compliance with the principles included in the Code of Ethics, in July 2005 the Code of Ethics Committee of Gas Natural Fenosa was established, whereby one of the main functions thereof is to provide and supervise a communication channel for all employees in order to receive queries and notifications of breaches of the Code, and accordingly to facilitate the resolution of disputes related to the application of the Code of Ethics and of the Anti-Corruption Policy and to draft reports for the governing bodies of Gas Natural Fenosa in relation to the dissemination and compliance of the Code of Ethics and of the Anti-Corruption Policy, and the activities of the Committee itself.

The aforementioned communication channel constitutes an open channel (e-mail, fax, postal mail and internal mail) between the Code of Ethics Committee and all of the employees of Gas Natural Fenosa in order to notify of aspects related to the Code. This channel enables all of the employees of the group, suppliers and collaborating companies to obtain or provide information regarding any aspects related to the Code of Ethics and Anti-Corruption Policy. Said parties may also contact the Code of Ethics Committee in order to notify the Committee confidentially and in good faith of conduct that breaches the Code. And all of the foregoing outside the normal reporting mechanisms for employees.

All of the communications between the Code of Ethics Committee and the employees of Gas Natural Fenosa are absolutely confidential, and adhere to the limitations established under the Spanish Data Protection Act 15/1999, of 13 December. Accordingly, the Chairman of the Committee (The Internal Auditing, Compliance and Control Director) is the only member thereof, in first instance, that is authorised to access all of the information regarding all of the queries and notifications received from the group through the query and notification procedure. Furthermore, the notifications related to fraudulent practices, audits or deficiencies in accounting or internal control processes are directly notified to the Audit Committee.

The foregoing queries and notifications are considered and resolved by the Code of Ethics Committee.

In the 2016 Corporate Responsibility Report of Gas Natural Fenosa further information is provided regarding the Code of Ethics, the Anti-Corruption Policy, the activities of the Code of Ethics Committee and the use of the communication channel.

➤ **Training programs and periodic updates for the staff involved in the drafting and review of the financial reporting, as well as in the assessment of the ICSFR, that covers, at least, accounting rules, audits, internal control and risk management.**

The need have sufficiently qualified and up to date professionals involved in the preparation and review of the financial reporting, as well as in the assessment of the ICSFR, means that it is necessary to develop an adequate training plan, such that the people responsible for each area have the necessary knowledge in order to be able to carry out the different functions included within the processes for the preparation and review of the financial reporting.

Accordingly, Gas Natural Fenosa has a Corporate University, that is responsible for the knowledge and development management of people throughout the Company. The Corporate University has a quality control management system in accordance with Standard ISO 9001:2008 that was renewed in 2016 and that obtained the CLIP accreditation in 2003 which was last renewed in 2013 for a period of five years. Said certification acknowledges the quality of the training and development processes of people in corporate education organisations.

The objectives of the Corporate University include, among others: ensure knowledge management in a multinational and multicultural organisation; accompany the business in relation to the main plans of the group; position the organisation as a leader in training within the energy sector; guarantee that employees obtain the technical knowledge and the necessary skills in order to fulfil the established strategic objectives and to transmit and share experiences and best practices that exist at the Company. Accordingly, the Corporate University is a place to meet, debate and where people are trained that promotes innovation and excellence in the development of talent so that our professionals can fulfil the objectives of the Company.

The content of the programs are structured through Training Schedules. said schedules take advantage of training synergies and furthermore cover the development needs in an ordered, complete, stable and sustainable manner. The schedules are comprised of three blocks: context knowledge (general and specific to all schedules), functional knowledge (specific to the position or profile) and skills (based upon the 24 skills of the Leadership Model).

In 2014 the "Programa Savia" [Savia Program] was established, which is a training program the purpose of which is to strengthen the current role of managers, that must be the change agents in relation to the global implementation of the new processes associated with the strategic challenges. In 2015 the second phase of the program was commenced, Savia 2.0, which was focused upon the experience of customers and on change management. In 2016 the program has continued, and during that year was focused on cooperation and empowerment. The program consists of two days of on-site training that is then complemented with online training via a dynamic and innovative methodology. Moreover, in November 2015, the first edition of Savia was extended to Chile, for 504 participants.

Another of the relevant programs is "Compromiso con la Seguridad y Salud" [Health and Safety Commitment]. Gas Natural Fenosa has consolidated its position as a leader in Health and Safety after the implementation of an ambitious program aimed at carrying out a deep and significant cultural change that commenced in 2012. The Corporate University has supported the Company during this process with the foregoing program. In 2016, in terms of Occupational Hazards Prevention, Health and Safety approximately 240,000 hours of training have been imparted to over 12,500 employees, with over 55,500 participations in different training activities. Thanks to the foregoing plan, the accident frequency and severity indices have dropped by 30% and the number of working days lost by reason of workplace accidents has also been reduced.

In September 2015, as part of the "Proyecto CeX" [CeX Project] (Customer Experience) the "Programa Advocacy," Embajadores del Cambio [Advocacy Program, Change Ambassadors] was implemented. Within the new culture of situating the customer at the centre of all operations, 270 ambassadors of the brand and corporate culture of Gas Natural Fenosa were selected, of which 18 were selected from the Economic and Financial Department. The mission of the ambassadors is to transmit our values both within their labour as well as their personal contexts and environments and become authentic change agents that promote the holistic vision of customers. Currently this program has been extended to all of the employees within Spain.

On the other hand, the specific knowledge for the economic and financial has several objectives, including, to homogenise the economic and financial processes carried out within any ambit of the organisation; the updating of the accounting, tax, financial, risk management and management control criteria as well as the international regulations and technical knowledge of the tax area; as well as to provide sufficient knowledge regarding the valuation of companies, financial derivatives and the analysis of financial statements.

In total, in 2016 over 200 professionals from the Economic and Financial Department carried out over 6,000 hours of training in relation to specific content, including, among other aspects, audit regulations, tax aspects, specialisation in finances, accounting, international financial reporting standards, management control and tax reforms.

F.2 Risk assessment of the financial reporting

State, at least:

F.2.1 What are the main characteristics of the process for the identification of risks, including risks of error or fraudulent practices, in relation to:

› **Whether the process exists and is documented.**

The approach adopted by Gas Natural Fenosa to carry out the process for the identification and analysis of the risks of the financial reporting is set out in three inter-related matrices:

- The definition matrix of the scope of the financial reporting
- The matrix for the risks associated with the financial reporting
- The control activities matrix of the financial reporting

The purpose of the definition matrix of the scope of the financial reporting is to identify the accounts and the breakdowns that have a significant associated risk, the potential impact of which in the financial reporting of the group is substantial and requires, accordingly, special attention. Accordingly, in the process for the identification of the significant accounts and breakdowns a series of quantitative variables have been taken into account (balance and variation of the account) as well as qualitative variables (complexity of the transactions; changes and complexity of the regulations; need to use estimations or forecasts; application of judgements and qualitative importance of the information). The methodology for the drafting of the scope matrix has been set out in a technical instruction called "Definition matrix of the scope of the financial reporting of Gas Natural Fenosa".

For each one of the significant accounts/breakdowns set out in the definition matrix of the scope, the critical processes and sub-processes have been defined that impact the accounts/breakdowns and the risks have been identified that may generate errors in the financial reporting, and the objectives for control of the existence and occurrence thereof; integrity; valuation; presentation, breakdown and comparability; and rights and obligations, are covered in the "Matrix for the risks associated with the process of the drafting and issue of the financial reporting of Gas Natural Fenosa".

Within the risks identification process defined by Gas Natural Fenosa in the ICSFR, the problem related to fraudulent practices has been considered as a highly relevant element. Accordingly, the fraud risk control policy of Gas Natural Fenosa is based upon three basic aspects:

- Fraud prevention.
- Fraud detection.
- Investigation and management of the fraud situations.

Preventive anti-fraud controls have been defined, from the perspective of financial reporting, that are classified in two categories. The so-called active controls, considered as barriers that restrict or prevent persons that may try to commit fraud from having access to the valuable assets. On the other hand, the passive controls aim to prevent fraud by way of dissuasive measures.

Finally, both the general control activities as well as the process control activities, that consist of the policies and procedures included throughout the stages of the process for the preparation of the financial reporting and that ensure the reliability thereof, are set out in the "Control activities matrix of the financial reporting of Gas Natural Fenosa".

The ICSFR of Gas natural Fenosa is a dynamic system, and accordingly the periodic update thereof constitutes a fundamental process in order to fulfil at all times the purposes thereof, that is to say, in order to ensure that the financial reporting of the group is reliable. In particular, the definition matrix of the scope thereof is updated on an annual basis.

➤ **Whether the process covers all of the objectives of the financial reporting, (existence and occurrence; integrity; valuation; presentation, breakdown and comparability; and rights and obligations), whether it is updated and of so, how often.**

Gas Natural Fenosa, aware of the need for and the importance of a tool that ensures the adequate control of the management of the ICSFR, implemented in 2013 the SAP GRC Process Control application, for the integral management of the documentation, and the assessment and supervision of the internal control of the processes of Gas Natural Fenosa. Said implementation, carried out within the framework of the efficiency enhancement program of Gas Natural Fenosa, was carried out, initially, in all of the Spanish companies in which Gas Natural Fenosa holds a majority shareholding as well as in the companies in which Gas Natural Fenosa is responsible for the operations and/or management thereof. In 2014 the implementation of the SAP GRC Process Control tool was carried out in Colombia and in the Shared Economic and Financial Services Centre of South America; in 2015 the implementation was extended to other countries of the group, such as Mexico and France; and in 2016 the tool was implemented in Holland and the progressive implementation thereof is scheduled in the countries where Gas Natural Fenosa operates. For the implementation of SAP GRC Process Control, both within Spain as well as at an international level, Gas Natural Fenosa has received the support of the users responsible for the key controls of the ICSFR and of the Internal Auditing, Compliance and Control Unit.

It is noteworthy to mention that, during the year 2015, the scope of the corporate ICSFR model was extended to the countries which have recently been included within the group, such as Chile, as a result of the acquisition in November 2014 of the Chilean group Compañía General de Electricidad, S.A. (CGE). This incorporation strengthens and enhances the Internal Control in Gas Natural Fenosa.

With the exception of the definition matrix of the scope, the ICSFR model of Gas Natural Fenosa is integrated within SAP GRC Process Control. This tool identifies the General Environment Controls and the General Computer Controls, together with the critical processes, their associated risks, as well as the control activities that mitigate said risks, that are set out in the aforementioned risks and controls matrices. Furthermore, the units responsible for the carrying out of the control activities are identified and integrated in the processes structure.

The following benefits are provided through the implementation of SAP GRC Process Control:

- It centralises all of the documentation and management of the ICSFR of Gas Natural Fenosa in a homogeneous manner.
- It integrates the internal control of the financial reporting in the business and corporate processes, thereby enabling each organisational unit to carry out, periodically, the assessment of their controls, with the provision of the necessary documentary evidence, and, annually, to carry out the internal certification process of the ICSFR.
- It uses workflows and forms for the management of the control activities, for the documentation of the evidence of the execution thereof and for the action plans.
- It provides for access to documentation that evidences the controls of the processes and displays the immediate result of the assessment in a user-friendly manner .
- It constitutes a support tool for the supervision process of the ICSFR by the Internal Auditing, Compliance and Control Unit.
- It provides for the provision and support of the information required for both the external and internal reporting of the ICSFR.

After the implementation of SAP GRC Process Control in April 2013, during the subsequent years the requests for assessment of the controls have been carried out in accordance with the established timetable, and the documentary evidence of the execution of the controls has been requested from the units involved in the ICSFR, in accordance with the established frequency. Said assessment makes it possible, if applicable, to identify and inform about weaknesses and the necessary action plans.

➤ **The existence of a process for the identification of the scope of the consolidated accounts, taking into account, among other aspects, the possible existence of complex corporate structures, instrumental or special purpose (SPV) entities.**

The identified critical processes include the process for the identification of the scope of the consolidated accounts of Gas Natural Fenosa, that has been described in a technical instruction called "Consolidated Accounts Procedures of the Gas Natural Fenosa group". Said document sets out the process for the monthly update of the scope of the consolidated accounts, in accordance with the corporate operations of the period, and the units involved therein are defined. This process of identification and update of the scope of the consolidated accounts is of fundamental importance for the drafting of the consolidated financial reporting of Gas Natural Fenosa.

➤ **Whether the process takes into account the effects of other types of risks (operational, technological, financial, legal, reputational, environmental risks, etc.) to the extent that they affect the financial statements.**

The risks matrix identifies the risks associated with the fulfilment of the objectives of financial reporting, taking into account in said identification the effects of other types of risks (for example: operational, technological, financial, reputational risks, etc.) that form part of the Corporate Risks Map of Gas Natural Fenosa.

➤ **Which governing body of the company supervises the process.**

The supervision of the efficacy of the ICSFR is the responsibility of the Audit Committee. For the performance of this function, the Audit Committee receives the support of the Internal Auditing, Compliance and Control Unit and the External Audit (see section F.5).

F.3 Control activities

State, together with the main characteristics thereof, whether at least the following aspects exist:

F.3.1 Procedures for the revision and authorisation of the financial reporting and the description of the ICSFR, to be published in the securities markets, stating the parties responsible for said procedures, as well as the descriptive documentation of the activities and controls flows (including those related to fraud risk) of the different types of transactions that may substantially affect the financial statements, including the procedure for the closing of the accounts and the specific review of the relevant judgements, estimations, valuations and forecasts.

Gas Natural Fenosa carries out periodic reviews of the financial reporting that is drafted, as well as of the description of the ICSFR, in accordance with the different levels of responsibility that guarantee the quality thereof.

By way of initial review, the persons responsible for the closing of the accounts of each company of Gas Natural Fenosa review the financial reporting drafted in order to ensure that it is reliable.

Furthermore, the financial reporting of Gas Natural Fenosa is periodically reviewed by the manager of the Economic and Financial Department, who identifies possible deviations. Accordingly, the Economic and Financial Department reports the regulated financial reporting to the Audit Committee, and ensures the transparency and accuracy of the information and mentions the internal control systems and the accounting criteria applied.

Furthermore, the Economic and Financial Department also reports on:

- > the main accounting principles, judgements, estimations and processes used for the drafting of the economic and financial reporting and the financial statements,
- > the companies that form part of the scope of the consolidated accounts of the group,
- > the main risks and contingencies and the hedging thereof by means of provisions,
- > the tax situation of the group and the main tax policies applied in the Companies Income Tax declarations,
- > the procedure for the selection of the external auditor,
- > the efficacy and efficiency of the Internal Control System on Financial Reporting (ICSFR) and the certification process regarding the key controls, as well as the action plans for improvements that have resulted from said process.
- > the Risks Control Policies and Systems at Gas Natural Fenosa, as well as the relevant aspects associated to the drafting, definition and conclusions of the Corporate Risks Map of Gas Natural Fenosa..

Finally, the Chief Financial Officer (CFO) certifies the reasonableness of the individual and consolidated annual accounts that are presented to the Board of Directors for approval.

On the other hand, as is set out in the "General Guidelines for the Internal Control System on Financial Reporting (ICSFR) of Gas Natural Fenosa", the control activities defined by the group in the ICSFR comply with the fundamental objective of ensuring that the financial reporting of Gas Natural Fenosa represents the true and faithful image of the group.

The control activities defined in the ICSFR include both general controls as well as controls of the critical processes.

The general controls are mechanisms that, although they do not provide for a sufficient degree of control over the processes of the group, nonetheless provide for the fulfilment of a series of key objectives for an effective ICSFR, that is to say, they describe the policies and directives designed in order to protect the ICSFR of Gas Natural Fenosa as a whole.

On the other hand, all of the identified critical processes have been documented by means of the control activities matrix as well as by the corresponding technical instructions that describe the processes. In the management tool of the ICSFR, SAP GRC Process Control, the critical processes are identified, as well as their associated risks and the control activities that mitigate said risks, together with the documentation that describes said processes. Accordingly, Gas Natural Fenosa has identified all of the necessary processes for the drafting of the financial reporting, for which relevant judgements, estimations, valuations and forecasts have been used, all of which are considered to be critical. On a periodic basis, the Audit Committee is notified of the main hypotheses applied in order to estimate the financial reporting that depend upon relevant judgements, valuations and forecasts.

The following information has been included within the critical processes and control activities documentation included within SAP GRC Process Control:

- › Description of the process.
- › Diagram of the reporting flows of the process.
- › Map of the systems that are involved in the process.
- › Description of the financial reporting risks associated with the different control processes and objectives
- › Definition of the control activities for the mitigation of the identified risks and the attributes thereof.
- › Description of the persons or units responsible for the processes and the control activities.

Moreover, in the definition of the control activities the following control activities classifications have been identified, in light of the following five criteria:

- › Scope: Depending upon the scope of the control activities, the activities may be divided into:
 - General control activities.
 - Process control activities.
- › Implementation: the control activities have been classified into implemented and non-implemented activities.
- › Degree of automation: Depending upon the degree of automation of the control activities, the activities may be divided into automatic and manual activities.
- › Nature of the activity: Depending upon the nature of the control activities, the activities may be divided into preventive or detection activities.
- › Frequency: Depending upon the recurrence of the activity over time, for example: annual, weekly, monthly, daily, etc.

Finally, in the ICSFR of Gas Natural Fenosa the annual internal certification model has been defined for the controls identified in the critical processes, that must be carried out by the business and corporate units involved in the process of the drafting of the financial reporting. The Financial Reporting Internal Control Unit is responsible for the implementation and monitoring of this certification process. To carry out this internal certification process, the units involved use the functions integrated within the SAP GRC Process Control tool for the management of the ICSFR of Gas Natural Fenosa (see section F.2.1).

In turn, the Internal Auditing, Compliance and Control Unit is responsible for reviewing and assessing the conclusions regarding compliance and efficacy that result from the annual internal certifications process of the units responsible for the controls, of the identification of the weaknesses and of the action plans.

F3.2. Policies and procedures for the internal control of the information systems (including, access security, change control, operational aspects, continuous operability and segregation of the functions) that support the relevant processes of the company in relation to the drafting and publication of the financial reporting.

For the critical processes associated with the drafting and publication of the financial reporting of Gas Natural Fenosa that have been defined in the ICSFR of the group, the control activities have been identified that operate in the information systems, both for the systems that are directly used for the preparation of financial reporting as well as for the systems that are relevant in the control process of transactions that are set out therein.

Generally speaking, within the information systems map of Gas Natural Fenosa, a series of policies have been defined and implemented in order to guarantee the following aspects:

- > Access security both for the data as well as for the applications.
- > The control regarding changes to the applications.
- > The correct procedures for the use of the applications.
- > The availability of the data and the continuity of the applications.
- > An adequate segregation of the functions.

a) Access security:

A series of measures have been defined at different levels in order to guarantee the confidentiality and to avoid the unauthorised access both to the data as well as to the applications. The management and authentication of the majority of the internal users is centralised in the Directories of OIM (Oracle Identity Manager), that ensures the confidentiality thereof.

The Company has two main DPC (Data Processing Centres) in Madrid, that provide for the availability of the information systems in the case of any contingency. Only authorised personnel are able to access said facilities, and all access is logged and, subsequently, reviewed in order to analyse any anomaly.

The communications with said systems include systems such as Firewall, IPS (Intrusion Prevention System) and antivirus systems in order to enhance the internal control against threats.

Moreover, the Company is currently working on the creation and updating of the BRS (Business Recovery Systems) of the main information systems, for the recovery of interrupted critical functions.

Finally, at an application, operational system and database level, the user-password combination is used as a preventive control. At a data level, profiles have been defined that limit access thereto. Gas Natural Fenosa is developing a project for the definition and implementation of a users/roles/profiles matrix for the enhancement of the segregation of functions that ensures the procedures for access to systems and data.

b) Change control:

A change management methodology has been developed and implemented based upon best practices, which establishes the checks and validations necessary in order to limit the risk in said process.

The main aspects thereof are set out hereinbelow:

- > Approval by the Technical Committee, Changes Committee and Business.
- > Carrying out of tests in different environments, prior to the production phase.

- Specific environments for the development and test tasks.
- Rollback procedures.
- Segregation of functions in the majority of the environments between the development and production equipment.
- Monitoring and control in any phase of development.
- User manuals and training courses.
- Periodic maintenance of the documentation regarding changes.

c) Operability:

In order to guarantee that the operations are correctly carried out, said operations are monitored on four different levels:

- All of the interfaces between systems are monitored so as to ensure the correct execution thereof.
- At a perimeter level, different availability indicators exist so as to avoid any communications interruptions.
- Automatic validations regarding the data entered so that the data is checked against the expected data in light of the nature, type thereof, etc.
- Of the infrastructures that support the applications.

Furthermore, an internal Help Desk service exists that final users may use and they have available a management tool in order to report any type of incident.

d) Availability and continuity:

The majority of the systems have a high degree of local availability, and the servers thereof are situated in the same DPC, and in certain cases, in the support DPC for critical aspects. The high availability of the information systems provides for the availability thereof in the case of incidents.

Furthermore, a backup copy of the data is periodically carried out, that is temporarily kept in a safe place based upon the legal requirements established for each one of the systems. The data is copied and stored in different locations which prevents any information loss. To restore and recover said data, a specific procedure exists, although periodic tests are not carried out.

e) Segregation of functions:

Access to the information systems is defined based upon roles and profiles that define the functionalities that must be available to users. Said profiles are used in order to limit the access of users to the information systems.

f) Regulatory compliance: LOPD (Spanish Data Protection Act):

Gas Natural Fenosa complies with the Spanish Data Protection Act in order to guarantee and protect the personal data of its employees and customers based upon the provisions of the Data Protection Act 15/1999, of 13 December.

The data controller of each file that contains personal data shall ensure legal compliance at Gas Natural Fenosa by:

- Registering the files at the Spanish Data Protection Agency ("AEPD") of all of the files that include personal data.
- Ensuring that the data is adequate and accurate and is managed proportionally in relation to the purpose for which it was obtained.

- › Guaranteeing the due compliance of the duties of secrecy and security.
- › Notifying the interested parties of the compilation thereof and obtaining the consent thereof for the processing of the data.
- › Guaranteeing the exercise of the rights of access, correction, cancellation and challenge.
- › Ensuring that all legal provisions are complied with in relation to the relationships with third parties that provide services with access to personal data, establishing by means of contract that the data processor shall process the data in accordance with the instructions of the data controller of the file, shall not apply or use the data for any other purposes other than that which is set out in the contract, shall not disclose said data, not even for the purposes of the storage thereof, to any other persons (the same security measures as applied by the data controller must be applied thereto).
- › Compliance with the sector legislation applicable to Gas Natural Fenosa.

Based upon Section 9 of the LOPD, that conditions the security measures to the state of technology, Gas Natural Fenosa adopts the technical measures that guarantee the security of the personal data and avoids the alteration, loss, or unauthorised processing or access thereto in order to guarantee the confidentiality, integrity and availability of the data.

Pursuant to Section 96 of the LOPD, Gas Natural Fenosa carried out biennial audits of its information systems in order to comply with the provisions of the Data Protection Regulations, as well as the data protection procedures and instructions.

F.3.3 Internal control policies and procedures for the supervision of the activities subcontracted to third parties, as well as the assessment, calculation or valuation aspects thereof that are commissioned to independent experts, that may substantially affect the financial statements.

Gas Natural Fenosa has developed a series of policies and procedures in order to supervise the management of the activities subcontracted to third parties, all of which have been approved by the levels established in the group, which include, the existence of “General Guidelines for External Contracting”, “General Guidelines regarding the Quality of Suppliers” and the procedures that are established therein, and the “Counterparty Due Diligence Procedure (corruption and reputational risks)”.

In this context, Gas Natural Fenosa has established in the “General Guidelines for External Contracting” the general principles that must be applied for all awards and contracting of works, goods and services carried out by the group, that guarantees an efficient and quality homogeneous model for the management of the Procurements process at Gas Natural Fenosa.

The foregoing Guidelines also establish, generally speaking, the responsibilities of the different units in the contracting process, which include the Procurements Department as the area responsible for promoting the creation of long-term relationships of trust and confidence with suppliers by establishing objective and impartial mechanisms of assessment and selection and ensuring that the supply chain complies with the principles provided for in the Code of Ethics for Suppliers, that the suppliers, as from 2016, must ratify and the terms of which are sourced from the Code of Ethics of Gas Natural Fenosa, from the Human Rights Policy, from the Health and Safety Policy, from the Anti-Corruption Policy, as well as from internationally recognised principles of good governance. The aforementioned Guidelines creates the obligation for the initial evaluation of all potential suppliers prior to the participation thereof within a procurements process, by which the Company evaluates, *inter alia*, legal, financial, quality, safety and security, environmental and corporate responsibility aspects, and also carries out the periodic evaluation thereof. In certain critical processes an additional level of control is required, that is referred to as “certification”, which is supported by documentary evidence and/or audits in order to secure the quality of the goods and services that are acquired.

For said purposes, Gas Natural Fenosa has developed, in the “General Guidelines regarding the Quality of Suppliers” and in the relevant procedures thereof, the basic principles that govern the evaluation and certification process of the suppliers of the group, which include the establishment of procedures and controls that guarantee the compliance of requirements set out in the specifications by potential suppliers and awarded contractors and furthermore also requires the certification of the suppliers of certain services or materials identified as of high risk (Operating Risk, Legal Risk, Health and Safety Risk, Quality Risk, and Environmental-Social-Governance Risk). The certification process may reveal anomalies that require a corrective action plan, or that result in the non-certification of a supplier, that shall prevent the supplier from rendering services to Gas Natural Fenosa.

Furthermore, the measurement of performance is carried out by means of satisfaction surveys of the service provided by suppliers that carry out high risk activities, with special attention on the Health and Safety aspects. The necessary corrective measures or action plans are established, as the case may be.

The main areas that affect critical processes of the financial reporting that Gas Natural Fenosa has subcontracted to third parties are:

- > Certain processes of the Systems area
- > Meter reading and measurement processes
- > Certain Customer Services processes
- > Logistics operator
- > Payslip and staff management process.
- > Site management and maintenance works of the distribution business
- > Certain services provided to customers of the Retail business

Furthermore, the Business Units carry out the supervision and the quality control of their suppliers in order to determine whether they fulfil the required levels of quality for the execution of the works. Alternatively, they forward their proposals for the removal of the certifications/ accreditation for suppliers/products/persons as a result of any deficiencies in the performance of the services or products.

Gas Natural Fenosa contracts experts for activities that support valuations, judgements or accounting calculations, solely and exclusively when said experts are registered in the corresponding Professional Colleges, or equivalent accreditation, and provided that they declare their independence and are internationally renowned companies.

Furthermore, Gas Natural Fenosa has defined the "Counterparty Due Diligence Procedure" that, in general, aims to provide hedging coverage for the main legal and reputational risks that affect business relationships with third parties and, in particular, the coverage of crimes associated with corruption risks.

The Internal Auditing, Compliance and Control Unit of Gas Natural Fenosa audits the processes and the correct application of the Procurement, Quality of Suppliers and Counterparty Due Diligence Procedures and in the case that breaches are detected the corresponding corrective actions are carried out.

F.4 Information and communication

State, together with the main characteristics thereof, whether at least the following aspects exist:

F.4.1 A specific function for the purpose of defining and keeping up to date the accounting policies (accounting policy area or department) and for resolving doubts or disputes in relation to the interpretation thereof, while maintaining fluid communication with the persons and units responsible for the operations within the organisation, as well as an updated accounting policies manual that is provided to the units pursuant to which the company operates.

The Economic and Financial Department is responsible, through the Accounting Planning and External Audit Unit, among other functions, for keeping up to date the accounting policies applicable to the group. Accordingly, it is responsible for the updating of the "Accounting Plan of Gas Natural Fenosa", that includes the accounting criteria and the accounts plan of the group, as well as for the analysis of the accounting changes that may affect the financial reporting of Gas Natural Fenosa.

The updating of the "Accounting Plan of Gas Natural Fenosa" is carried out on an annual basis, and the most recent update thereof was carried out in December 2016. The updates review both the accounting criteria based upon changes to the applicable IFRS-EU regulations as well as the accounting structure of the group, ensuring the traceability between the individual accounts plans of the subsidiaries of the group and the accounts plan of Gas Natural Fenosa, that constitutes the basis for the drafting of the different financial reporting to be provided to external bodies as well as the Management Control information.

After the Accounting Plan has been updated, it is disseminated to all of the staff of the organisation via the intranet of Gas Natural Fenosa. Furthermore, and after the updated accounting plan has been published on the intranet, an online alert is sent to users that access the intranet that notifies all staff of said update.

On the other hand, the Accounting Planning and External Audit Unit is responsible for analysing the IFRS-EU regulatory changes that may significantly affect the financial statements and for notifying the managers of Gas Natural Fenosa that are affected by said regulatory changes. The foregoing Unit is also responsible for resolving the doubts and questions regarding the accounting classification of certain transactions that may be raised by the financial reporting staff of Gas Natural Fenosa.

F.4.2 Mechanisms for the capture and preparation of the financial reporting with homogeneous formats, that are applicable and used by all of the units of the company or group, that support the main financial statements and the notes, as well as the information that is set out regarding the ICSFR.

The integral economic and financial management model of Gas Natural Fenosa ensures the uniformity of the administrative and accounting processes by means of the centralisation of the accounting activities and the economic administration in Shared Economic and Financial Services Centres ("CSCs") and through the use of SAP as a support system in the majority of the companies that form part of the group. The rest of the companies that do not use SAP are required to adhere to the criteria established by the group in order to ensure the uniformity of said processes.

Said model is characterised, fundamentally, by the fact that:

- > it constitutes a single model for all countries and businesses;
- > it incorporates the legal, tax, commercial and regulatory requirements of each one of the countries;
- > it incorporates the internal control requirements;
- > it constitutes the basis for obtaining the information that is provided to Senior Management and to official bodies;
- > it is supported by a specific organisational model as well as specific economic and financial processes and computer systems for all countries and businesses;

The IFRS-EU financial statements of each country are directly obtained through the local account-group account assignment and the registration of the IFRS-EU adjustments in the SAP application.

As part of the ICSFR of the group, the map of interrelationships regarding the drafting of the financial reporting of Gas Natural Fenosa has been defined. Said map sets out, among other things, the computer systems that are involved in the process for the drafting and issue of the financial reporting both from the perspective of the individual accounting close as well as from the consolidated accounting close perspective.

Accordingly, in relation to the drafting process of the financial reporting of Gas Natural Fenosa, the application SAP BPC is used, that is the SAP tool for the management of the consolidated process.

The information is automatically and directly loaded into said system, after the month has been closed.

Both of the foregoing tools provide support for the consolidation process and for Management Control in relation to tasks such as:

- > Standardisation of the information.
- > Validation of the information.

The drafting of the economic information, both of the financial reporting, as well as of the management information is centralised in the Integrated Reporting Centre, that ensures the integration, homogeneity, coherence and rationalisation of the reporting of Gas Natural Fenosa.

Furthermore, Gas Natural Fenosa has local accounts plans in order to comply with the accounting, tax, commercial and regulatory requirements established under the specific legislation of the countries in which the group operates. Said local accounts plans are grouped together to complete the unified and homogeneous group accounts plan for the purposes of the consolidated accounts and financial reporting.

F.5 Supervision of the functioning of the system

State, including the main characteristics thereof, at least:

F.5.1 The supervision activities of the ICSFR carried out by the Audit Committee as well as whether the company has an internal auditing function that includes activities that provide support to the Committee in relation to its supervision activities for the internal control system, including the ICSFR. Furthermore, state the scope of the assessment of the ICSFR carried out during the year and the procedure by which the person or unit responsible for carrying out the assessment notifies of the results thereof, whether the company has an action plan that details the potential corrective measures, and whether the impact thereof has been taken into consideration in relation to the financial reporting.

The Audit Committee has the powers that are provided for at law as well as the specific or general powers that are delegated upon it by the Board of Directors. The powers thereof include the following:

- Supervise the drafting process, the presentation and the integrity of the financial reporting of the Company and, as the case may be, of the group, and to review the compliance with the regulatory requirements, the adequate delimitation of the scope of the consolidated accounts and the correct application of the accounting criteria.
- Supervise the efficacy of the internal control of the Company, the internal auditing and the risk management systems, including the tax risks, as well as to discuss with the accounts auditor the significant weaknesses of the internal control system detected during the carrying out of the audit.
- Notify the General Shareholders Meeting regarding the questions that are raised thereby in relation to the aspects for which the Committee is responsible.
- To forward to the Board of Directors the proposals for the selection, appointment, re-election and replacement of the external auditor, as well as the terms and conditions for the contracting thereof and to regularly obtain from the external auditor information regarding the audit plan and the execution thereof, and furthermore to preserve the independence thereof in the exercise of its functions.
- Establish the necessary relationships with the external auditor in order to obtain information regarding the questions that may jeopardise the independence thereof, for the examination thereof by the Committee, and any other questions related to the accounts audit process, as well as any other communications provided for under applicable accounts audit legislation and in the audit regulations. In any event, the Committee must receive, annually, from the external auditors the declaration of their independence in relation to any directly or indirectly related parties, as well as the information regarding the additional services of any type whatsoever provided thereby and the corresponding professional fees received from said entities by the external auditor or by the persons or related parties thereof, in accordance with the provisions of accounts audit legislation.
- Annually issue, prior to the release of the accounts audit report, a report that sets out an opinion regarding the independence of the accounts auditor. Said report must contain, in any circumstances, the valuation of the provision of the additional services referred to under the preceding paragraph, both individually and as a whole, other than for the legal audit and in relation to the regime of independence or the audit regulations.
- Ensure the independence of the unit that assumes the internal auditing functions; approve the orientation and the work plans thereof, ensuring that the activities thereof are mainly focused toward the relevant risks of the Company; to receive periodic information regarding the activities thereof; and to verify that senior management take into account the conclusions and recommendations of

its reports. To propose to the Chairman of the Board of Directors the selection, appointment, re-election and removal of the internal auditing service manager, as well as to propose the budget for said service, however the final decision shall be adopted by the Chairman of the Board of Directors.

The Audit Committee shall obtain, in order to be able perform its activities, the information and documentation provided by the Internal Auditing, Compliance and Control Unit and by the Economic and Financial Department.

The functions of the Internal Auditing, Compliance and Control Unit has been established at Gas Natural Fenosa as independent and objective assessment activities, and accordingly the Internal Auditing, Compliance and Control Units, in turn, reports to the Audit Committee and to the Managing Director of GAS NATURAL SDG, S.A.

The mission thereof is to ensure the continuous review and the improvement of the internal control system of the group, as well as to ensure the compliance with external and internal regulations and with the established control models in order to safeguard the efficacy and efficiency of the operations, and to mitigate the main risks in each of the different ambits of the group, in particular the operational, corruption, fraud and legal risks. Furthermore, it is responsible for the management of the Crime Prevention Model and of the Code of Ethics Model of Gas Natural Fenosa and for reporting regarding the internal auditing activities to the Audit Committee.

In the performance of its activities, Internal Auditing carries out the methodical review of the internal control systems of the processes of the group in all of the different aspects thereof, as well as the assessment of the controls and the operational risks associated with said processes (including those established in the ICSFR and in the Crime Prevention Model), through the definition and implementation of the "Annual Internal Audit Plan", in order to improve the efficacy and efficiency thereof. Furthermore, it supports senior management through the fulfilment of its objectives.

The final objective is to safeguard the efficacy and efficiency of the operations and to mitigate the main risks in each one of the ambits of Gas Natural Fenosa, in particular in relation to operational, corruption, fraud and legal risks.

The "Strategic Audit Plan" (with a time frame of five years) and the annual internal audit plans are drafted taking into account, fundamentally, the "Corporate Strategic Plan", the risk areas included in the Corporate Risks Map, the scope matrix of the Internal Control System on Financial Reporting (ICSFR), the operational risks maps, the results of the audits of previous years, and the proposals of the Audit and Control Committee and from top-tier management.

In accordance with the Strategic Audit Plan, the Internal Control System on Financial Reporting (ICSFR) of Gas Natural Fenosa shall be completely supervised by Internal Auditing within the period of five years.

The methodology for the assessment of operational risks is in accordance with best corporate governance practices, based on the conceptual framework of the COSO Report (Committee of Sponsoring Organisations of the Treadway Commission) and on the basis of the types of risks defined in the company's Corporate Risk Map.

The operational risks associated with the processes are prioritised by assessing their incidence, relative importance and degree of control. Depending on the findings, the company designs an action plan with corrective measures that enables mitigation of residual risks identified with a potential impact above the tolerable or accepted risk established.

Internal Auditing is supported by the implementation of a SAP environment corporate application which it uses to manage and document internal audit projects in accordance with the defined methodology.

Specifically, and in relation to the Internal Control System on Financial Reporting (ICSFR), Internal Auditing is responsible for:

- > Validating the correct design of the ICSFR, in accordance with the basic principles of the model approved by the Audit Committee.
- > Supervising the efficacy and suitability of the control policies and procedures implemented (with the complete implementation thereof over five years).
- > Reviewing and assessing the conclusions regarding the compliance and efficacy of the ICSFR from the internal certificates of the business and corporate units responsible for the controls (with the complete implementation thereof over five years).
- > Assessing and communicating the results obtained in the general supervision process of the ICSFR and from the controls over the ICSFR processes.

In relation to the Crime Prevention Model, the Internal Auditing, Compliance and Control Area is responsible for the annual supervision thereof in order to reasonably ensure the efficacy and efficiency of the Model for the prevention, identification or mitigation of crimes provided for under applicable legislation.

The main processes reviewed by Internal Auditing during 2016 were as follows:

> Business processes

- Gas Distribution: Meter Reading and Determination of Consumption, Customer Acquisition and Commissioning, Construction of Networks, Emergency Responses, Gas Distribution Warehouse Management, Management of Irregularities and Fraud.
- Electricity Distribution: Electricity Distribution Warehouse Management, Operations, Service Provision, Medium and Low Voltage Development, Network Maintenance, Meter Reading.
- Electricity Generation: Operation and Maintenance of Electricity Generation Assets, Warehouse Management.
- Retail Market: Customer Acquisition and Electricity Facilities Contracting.
- Wholesale Market and Global Accounts: Management of the Loss of Industrial Customers, Management and Optimisation of Gas Logistics
- Provisioning and Transport: Procurements of GNL
- Exploration and Production: Exploration/Production.
- Energy Management: Estimation of the demand and Purchase of Retail Electricity, CO2 Markets, Electricity Generation Sale

> Strategic and support processes

- Customer Services: Collection, Billing, Debt Collection Management, Customer Support, Meter Reading and Marketing Measures
- Management of Physical Resources: Procurements within and outside the scope of consolidation, Accreditation and Monitoring of Suppliers, Counterparty Due Diligence.
- Internal Control Management: Monitoring of corrective actions, ICSFR, Data Protection Act
- Information Systems Management: Guarantee of continuity and availability of the Information Systems, Information Security, Management of Information Systems Projects.
- Human Resources Management: Human Resources Administration and Services, DPO
- Communication Management and Foreign Relations: Sponsorship, Foundations, Corporate Responsibility
- Management of Economic and Financial Resources: Treasury Stock
- Legal Consultancy and Support Services: Legal Consultancy and Support Services
- Review of the Regulatory System of the Group
- Code of Ethics
- Update of the operational risks map.

- Review of the assessment and implementation of the Productivity Plan
- Crime Prevention Model.

37% of the reviewed processes relate to the business activities within Spain and the remaining 63% correspond to the international ambit.

The controls of the previous processes related to Financial Reporting, were reviewed in accordance with the working methodology that has been set out hereinabove.

F5.2 Whether a discussion procedure exists by means of which the accounts auditor (in accordance with the provisions of the NTA), the internal audit staff and other experts may notify to senior management and the Audit Committee or directors of the company the significant internal control weaknesses identified during the processes of review of the annual accounts or during any other processes carried out thereby. Furthermore, state whether an action plan exists for the correction or mitigation of the detected weaknesses.

As provided for under Article 6.4 of the Regulations regarding the Organisation and Functioning of the Board of Directors and its Committees:

“The Board of Directors shall ensure that a direct relationship is maintained with the members of the senior management bodies of the Company and with the Auditors thereof. The objective, professional and permanent nature of said relationship shall strictly respect the independence of the Auditors”

Furthermore, Article 9 of the Regulations provide that:

“The Board shall meet at least once every two months, and, at the proposal of the Chairman, as often as the Chairman deems necessary for the proper functioning of the Company. The meeting must, necessarily, be called when requested by at least 1/3 of the Board Members, in accordance with the terms of Article 46 of the Articles of Association of the Company. During the ordinary meeting sessions of the Board, the general aspects and matters shall be discussed that are related to the businesses of the Group, the economic results, the Balance Sheet, the Cash situation and the comparison thereof with the approved budgets, the aspects and matters set out in Article 5, if applicable, and in any event the points included in the agenda to the meeting, drafted in accordance with the terms of these Regulations. During said periodic meetings, the Board shall also receive information regarding the most significant operational results and problems as well as in relation to the foreseeable situations that may be critical for the interests of the Company and the actions that the Steering Committee proposes in order to manage said situations, as the case may be (...).”

Accordingly, the members of the Board of Directors, in order to obtain the information necessary for the exercise of their functions, are supported by the Steering Committee, the specific function of which is to carry out the continuous monitoring of senior management of the group, as well as the Audit Committee, the functions of which include the analysis and supervision of the process for the drafting of the regulated financial reporting, as well as the efficacy of the internal control system.

The permanent delegation of powers by the Board of Directors in favour of the Steering Committee shall include all of the powers of the Board, with the exception of the powers that are not able to be delegated, whether pursuant to legal provisions or the Articles of Association or pursuant to these Regulations.

In accordance with the Articles of Association of the Company and the Regulations of the Board of Directors and its Committees, the Audit Committee shall be comprised by a minimum of three and a maximum of seven Board Members, that shall be designated by the Board of Directors from among the Non-Executive Board Members, and at least one of the Non-Executive Board Members thereof shall be designated taking into account his or her knowledge and expertise in accounting or audit fields, or in both fields. The members thereof shall be removed from office when they cease to be Board Members or when the Board removes them from the Audit Committee or by reason of the expiry of the period of three years after their appointment, however the members thereof may be re-elected. The majority of the members of the Committee shall be Independent Board Members. As at 31 December 2016, the Audit Committee is comprised of seven Board Members, three proprietary Board Members and four independent Board Members, one of which is the Chairman of the Audit Committee.

The Board of Directors shall elect the Chairman of the Committee, who shall not have a casting vote and who must be replaced as provided for under the Articles of Association (Article 51 bis) and as provided for at law, and who may be re-elected after the period of one year has elapsed as from the removal from office thereof. The Secretary of the Board of Directors shall act as the Secretary of the Committee.

The Committee, which shall be called by the Chairman thereof, shall meet as often as necessary in order to issue reports or proposals in relation to its functions or when deemed necessary by the Chairman thereof, or at the prior request of at least two of the members thereof and, shall meet at least four times a year. The Committee may invite any manager or employee that it deems necessary to attend the meetings.

The scope of the activities of the Audit Committee extends to:

- › Gas Natural SDG, S.A.
- › Subsidiary companies in which Gas Natural SDG, S.A. holds a majority shareholding
- › Other subsidiary and related companies, in respect of which Gas Natural SDG, S.A., in any form whatsoever, effectively controls or is responsible for the management or operations thereof.

The Internal Auditing, Compliance and Control Unit shall report to the Audit Committee, on a permanent basis, the actions adopted in order to ensure that Gas Natural Fenosa complies with all of the policies, rules and controls of the processes established by the senior management of the group.

Furthermore, the foregoing unit shall also present:

- › The Annual Internal Audit Plan for the approval of the Committee.
- › The degree of execution thereof, as well as the main conclusions and recommendations included in the Internal Audit Reports.
- › The assessment of the efficacy of the Control System for the assessment of the operational risks and of the Internal Control of the Gas Natural Fenosa group (including the risks corresponding to the ICSFR and to the Crime Prevention Model), that includes the corresponding Action Plans in order to enhance the level of internal control.
- › The degree of implementation by the audited units of the corrective measures that are included in the Audit Reports, in particular the measures proposed by the Audit Committee.

Furthermore, the Economic and Financial Department reports the regulated financial reporting to the Audit Committee, and ensures the transparency and accuracy of the information and mentions the internal control systems and the accounting criteria applied. Furthermore, the Economic and Financial Department also reports on:

- › the main accounting principles, judgements, estimations and processes used for the drafting of the economic and financial reporting and the financial statements,
- › the companies that form part of the scope of the consolidated accounts of the group,
- › the main risks and contingencies and the hedging thereof by means of provisions,
- › the tax situation of the group and the main tax policies applied in the Companies Income Tax declarations,
- › the procedure for the selection of the external auditor,

- the efficacy and efficiency of the Internal Control System on Financial Reporting (ICSFR) and the certification process regarding the key controls, as well as the action plans for improvements that have resulted from said process.
- the Risks Control Policies and Systems at Gas Natural Fenosa, as well as the relevant aspects associated to the drafting, definition and conclusions of the Corporate Risks Map of Gas Natural Fenosa.

The external auditor notifies the Audit Committee of the significant internal control weaknesses detected during the audit procedures. Furthermore, the external auditors report on the main conclusions that they have reached in relation to the review of the internal control, regarding the assessment of risks and the action plans.

Finally, the external auditor, over and above the periodic meetings with the Audit Committee, also meets with the plenary session of the Board of Directors prior to the Board of Directors drafting the annual accounts.

F.6 Other relevant information

As is described in section F.3.1. hereinabove, as part of the assessment model of the Internal Control System on Financial Reporting of Gas Natural Fenosa, an annual internal certification process has been defined by means of which, and through SAP GRC Process Control, the business and corporate units involved in the process for the drafting of the financial reporting certify that within their processes the identified controls are applied and that said controls are valid and sufficient. Moreover, said units report to the Internal Control on Financial Reporting unit of the weaknesses and/or deficiencies that they detect as well as the changes that take place within their processes in order to analyse whether said changes imply the need to develop new controls or modify the existing controls.

During the year 2016, Gas Natural Fenosa has carried out the annual internal certification process, with the result that changes in a limited number of process have been identified, however said changes have not implied the modification of the previously identified control activities, and accordingly the risks associated with the drafting of the financial reporting in the affected critical processes are considered to be covered. The main figures from said process are set out hereinbelow:

	Spain	International	Total
Business and corporate units	136	194	330
Processes identified	54	142	196
Controls certified	854	1,842	2,696

Furthermore, action plans have been identified for weaknesses in relation to the documentary evidence of controls, that amount to 40, of which 8 are for Spain. During the year 2016 a total of 59% of the action plans identified in 2015 have been resolved, and new plans have been established during 2016. In any event, the sub-processes affected by said action plans do not significantly affect the quality of the financial reporting.

F.7 Report of the external auditor

State:

F.7.1 Whether the information of the ICSFR that is released to the markets has been submitted to review by the external auditor, in which case the company must include the corresponding report as an annex. Alternatively, the reasons why no report exists must be stated

Gas Natural Fenosa has considered it appropriate to request the External Auditor to issue a report in relation to the information regarding the Internal Control System on Financial Reporting (ICSFR).

G. Degree of compliance with the Corporate Governance Recommendations

State the degree of compliance of the company in respect of the recommendations regarding the Good Governance Code of Listed Companies.

In the case that any recommendation is not complied with or is only partially complied with, a detailed explanation must be included of the reasons thereof, in order that the shareholders, investors and the market in general have sufficient information in order to assess the decisions of the company. General explanations shall not be accepted.

1. The Articles of Association of listed companies should not place an upper limit on the votes that can be cast by a single shareholder, or impose other obstacles to the takeover of the company by means of share purchases on the market.

Compliant

2. When a dominant and subsidiary company are both listed, they should provide detailed disclosure on:
 - a) The activity they engage in and any business dealings between them, as well as between the listed subsidiary and other group companies;
 - b) The mechanisms in place to resolve possible conflicts of interest.

Not applicable

3. During the General Shareholders Meeting the Chairman of the Board of Directors should verbally inform shareholders in sufficient detail of the most relevant aspects of the company's corporate governance, supplementing the written information circulated in the annual corporate governance report. In particular:
 - a) Changes taking place since the previous General Shareholders Meeting.
 - b) The specific reasons for the company not following a given Good Governance Code recommendation, and any alternative procedures applied in respect thereof.

Compliant

4. The company should draw up and implement a policy of communication and contacts with shareholders, institutional investors and proxy advisors that complies in full with market abuse regulations and accords equitable treatment to shareholders in the same position.

This policy should be disclosed on the company's website, complete with details of how it has been put into practice and the identities of the relevant interlocutors or those charged with its implementation.

Compliant

5. The Board of Directors should not make a proposal to the general meeting for the delegation of powers to issue shares or convertible securities without pre-emptive subscription rights for an amount exceeding 20% of capital at the time of such delegation.

When the Board of Directors approves the issuance of shares or convertible securities without pre-emptive subscription rights, the company should immediately post a report on its website explaining the exclusion as envisaged in company legislation.

Explain

The most recent authorisation for a share capital increase issued in favour of the Board was ratified at the General Shareholders Meeting of 20 April 2012 for a period of 5 years and up to a maximum sum of half of the share capital at the time of the authorisation.

Said authorisation included the power to revoke the pre-emptive subscription rights and the corresponding report was issued that was provided to shareholders..

6. Listed companies drawing up the following reports on a voluntary or compulsory basis should publish them on their website well in advance of the General Shareholders Meeting, even if their distribution is not obligatory:

a) Report on auditor independence.

b) Reports of the operation of the Audit Committee and the nomination and remuneration committee.

c) Audit committee report on related party transactions.

d) Report on corporate social responsibility policy.

Compliant

7. The company should broadcast its general meetings live on the corporate website.

Compliant

8. The Audit Committee should strive to ensure that the Board of Directors can present the company's accounts to the general meeting without limitations or qualifications in the auditor's report. In the exceptional case that qualifications exist, both the Chairman of the Audit Committee and the auditors should give a clear account to shareholders of their scope and content.

Compliant

9. The company should disclose its conditions and procedures for admitting share ownership, the right to attend general meetings and the exercise or delegation of voting rights, and display them permanently on its website.

Such conditions and procedures should encourage shareholders to attend and exercise their rights and be applied in a non-discriminatory manner.

Compliant

10. When an accredited shareholder exercises the right to supplement the agenda or submit new proposals prior to the general meeting, the company should:

- a) Immediately circulate the supplementary items and new proposals.
- b) Disclose the model of attendance card or proxy appointment or remote voting form duly modified so that new agenda items and alternative proposals can be voted on in the same terms as those submitted by the Board of Directors.
- c) Put all these items or alternative proposals to the vote applying the same voting rules as for those submitted by the Board of Directors, with particular regard to presumptions or deductions about the direction of votes.
- d) After the general meeting, disclose the breakdown of votes on such supplementary items or alternative proposals.

Not applicable

11. In the event that a company plans to pay for attendance at the general meeting, it should first establish a general, long-term policy in this respect.

Not applicable

12. The Board of Directors should perform its duties with unity of purpose and independent judgement, according the same treatment to all shareholders in the same position. It should be guided at all times by the company's best interest, understood as the creation of a profitable business that promotes its sustainable success over time, while maximising its economic value.

In pursuing the corporate interest, it should not only abide by laws and regulations and conduct itself according to principles of good faith, ethics and respect for commonly accepted customs and good practices, but also strive to reconcile its own interests with the legitimate interests of its employees, suppliers, clients and other stakeholders, as well as with the impact of its activities on the broader community and the natural environment.

Compliant

13. The Board of Directors should have an optimal size to promote its efficient functioning and maximise participation. The recommended range is accordingly between five and fifteen members.

Explain

Currently, the Board of Directors of Gas Natural SDG, S.A., within the minimum of 10 members and the maximum of 20 members, as provided for under Article 41 of the Articles of Association, by virtue of the resolution adopted at the General Shareholders Meeting held on 23 June 2003, is comprised of 17 members. Said number of members exceeds the number established in Recommendation 13 of the Good Governance Code by 2 members, however represents the minimum number that enables the Company to fulfil two objectives: on the one hand, to respect and abide by the legal mandate of proportional representation and, on the other hand, to have a sufficient number of independent Board Members that are able to carry out, with the sufficient degree of dedication, the numerous functions that are conferred upon them pursuant to applicable regulations and in particular, to be able to participate at the different committees which they are required to attend. In order to obtain a Board with fewer members, the principle of proportional representation would require a total of four independent Board Members which would adversely affect the working capacity thereof, for example they would all be required to be members of the Audit Committee. In any event, the number of 17 does not limit or restrict the efficient and participative functioning of the Board or of its committees in any way whatsoever.

14. The Board of Directors should approve a director selection policy that:

- a) Is concrete and verifiable.
- b) Ensures that appointment or re-election proposals are based on a prior analysis of the Board's needs; and.
- c) Favours a diversity of knowledge, experience and gender.

The results of the prior analysis of Board needs should be written up in the Nomination Committee's explanatory report, to be published when the general meeting is convened that will ratify the appointment and re-election of each director.

The director selection policy should pursue the goal of having at least 30% of total Board appointments occupied by women directors before the year 2020.

The Nomination Committee should run an annual check on compliance with the director selection policy and set out its findings in the annual corporate governance report.

Partially compliant

The director selection policy ensures that the selection procedures of the Company are not subject to any implicit bias that could imply any type of discrimination whatsoever, within the framework of the strict adherence to the right of proportional representation of the shareholders that is provided for at law. As has been set out hereinabove, the director selection policy aims to ensure adequate diversity for the composition of the Board of Directors, which means that the members of the Board have different however complementary professional profiles and experience, as the Company believes that said diversity provides for the better functioning of the Board. Within the foregoing framework, as has been set out in section C.1.6, the Board pays attention to the question of gender diversity. Although the policy does not expressly state the objective that in the year 2020 at least a third of the members of the Board are women directors, it is true that within a brief period of time (2014-2016) the percentage of women directors has increased from 0% to 17.64% and parity has been established in relation to the independent directors.

15. Proprietary and independent directors should constitute an ample majority on the Board of Directors, while the number of executive directors should be the minimum practical bearing in mind the complexity of the corporate group and the ownership interests they control.

Compliant

16. The percentage of proprietary directors out of all non-executive directors should be no greater than the proportion between the ownership stake of the shareholders they represent and the remainder of the company's capital.

This criterion can be relaxed:

- a) In large cap companies where few or no equity stakes attain the legal threshold for significant shareholdings.
- b) In companies with a plurality of shareholders represented on the Board of Directors but not otherwise related.

Compliant

17. Independent directors should be at least half of all Board Members.

However, when the company does not have a large market capitalisation, or when a large cap company has shareholders individually or concertedly controlling over 30 per cent of capital, independent directors should occupy, at least, a third of Board appointments.

Explain

As at 31 December 2016, one third of the directors are independent directors, although the Company cannot be classified as having low market capitalisation and does not have shareholders that act jointly and that control more than 30% of the share capital. Accordingly, it must be taken into account that three shareholders of the Company have shareholdings that are equal to or that exceed 20% however they do not act jointly, the representation thereof on the Board of Directors complies with the principle of proportional representation. On the other hand, it must be stated that the establishment of qualified majorities for certain matters has provided the independent directors with the capacity to block the decisions thereof.

18. Companies should disclose the following director particulars on their websites and keep them regularly updated:

- a) Background and professional experience.
- b) Directorships held in other companies, listed or otherwise, and other paid activities they engage in, of whatever nature.
- c) Statement of the director class to which they belong, in the case of proprietary directors indicating the shareholder they represent or have links with.
- d) Dates of their first appointment as a Board Member and subsequent re-elections.
- e) Shares held in the company, and any options on the same.

Compliant

19. Following verification by the Nomination Committee, the annual corporate governance report should disclose the reasons for the appointment of proprietary directors at the urging of shareholders controlling less than 3 per cent of capital; and explain any rejection of a formal request for a Board appointment from shareholders whose equity stake is equal to or greater than that of others applying successfully for a proprietary directorship.

Not applicable

20. Proprietary directors should resign when the shareholders they represent dispose of their ownership interest in its entirety. If such shareholders reduce their stakes, thereby losing some of their entitlement to proprietary directors, the latter's number should be reduced accordingly.

Compliant

21. The Board of Directors should not propose the removal of independent directors before the expiry of their tenure as mandated by the Articles of Association, except where they find just cause, based on a proposal from the Nomination Committee. In particular, just cause will be presumed when directors take up new posts or responsibilities that prevent them allocating sufficient time to the work of a Board Member, or are in breach of their fiduciary duties or come under one of the disqualifying grounds for classification as independent enumerated in the applicable legislation.

The removal of independent directors may also be proposed when a takeover bid, merger or similar corporate transaction alters the company's capital structure, provided the changes in Board Membership ensue from the proportionality criterion set out in recommendation 16.

Compliant

22. Companies should establish rules obliging directors to disclose any circumstance that might harm the organisation's name or reputation, tendering their resignation as the case may be, and, in particular, to inform the Board of Directors of any criminal charges brought against them and the progress of any subsequent trial.

The moment a director is indicted or tried for any of the offences stated in company legislation, the Board of Directors should open an investigation and, in light of the particular circumstances, decide whether or not he or she should be called on to resign. The Board of Directors should give a reasoned account of all such determinations in the annual corporate governance report.

Compliant

23. Directors should express their clear opposition when they feel a proposal submitted for the Board's approval might damage the corporate interest. In particular, independents and other directors not subject to potential conflicts of interest should strenuously challenge any decision that could harm the interests of shareholders lacking Board representation.

When the Board of Directors makes material or reiterated decisions about which a director has expressed serious reservations, then he or she must draw the pertinent conclusions. Directors resigning for such causes should set out their reasons in the letter referred to in the next recommendation.

The terms of this recommendation also apply to the Secretary of the Board of Directors, even if he or she is not a director.

Compliant

24. Directors who give up their place before their tenure expires, through resignation or otherwise, should state their reasons in a letter to be sent to all members of the Board of Directors. Whether or not such resignation is disclosed as a material event, the motivating factors should be explained in the annual corporate governance report.

Compliant

25. The Nomination Committee should ensure that non-executive directors have sufficient time available to discharge their responsibilities effectively.

The Board of Directors regulations should lay down the maximum number of company boards on which directors can serve.

Partially compliant

In light of the extensive participation and attendance by the members of the Board at the meeting sessions of the governing bodies, the Company has not yet established rules regarding the number of company boards on which directors can serve, without prejudice to the fact that the Company has verified the adequate functioning of the Board of Directors, both in terms of the number of meetings, that have exceeded the recommended number, as well as in qualitative terms.

26. The Board of Directors should meet with the necessary frequency to properly perform its functions, eight times a year at least, in accordance with a calendar and agendas set at the start of the year, to which each director may propose the addition of initially unscheduled items.

Partially compliant

Pursuant to the provisions of Article 9 of the Regulations of the Board of Directors, 1/3 of the directors may propose other points to be included in the Agenda for the meeting of the Board. In relation to the number of meetings, the number of meetings exceed the number provided for in the recommendation and said meetings have been held in accordance with the schedule approved by the Board itself.

27. Director absences should be kept to a strict minimum and quantified in the annual corporate governance report. In the event of absence, directors should delegate their powers of representation with the appropriate instructions.

Compliant

28. When Directors or the Secretary express concerns about some proposal or, in the case of directors, about the company's performance, and such concerns are not resolved at the meeting, they should be recorded in the minute book if the person expressing them so requests.

Compliant

29. The company should provide suitable channels for directors to obtain the advice they need to carry out their duties, extending if necessary to external assistance at the company's expense.

Compliant

30. Regardless of the knowledge directors must possess to carry out their duties, they should also be offered refresher programmes when circumstances so advise.

Compliant

31. The agendas of Board meetings should clearly indicate on which points directors must arrive at a decision, so they can study the matter beforehand or gather together the material they need.

For reasons of urgency, the Chairman may wish to present decisions or resolutions for Board approval that were not on the meeting agenda. In such exceptional circumstances, their inclusion will require the express prior consent, duly minuted, of the majority of directors present.

Compliant

32. Directors should be regularly informed of movements in share ownership and of the views of major shareholders, investors and rating agencies on the company and its group.

Compliant

33. The Chairman, as the person charged with the efficient functioning of the Board of Directors, in addition to the functions assigned by law and the company's Articles of Association, should prepare and submit to the Board of Directors a schedule of meeting dates and agendas; organise and coordinate regular evaluations of the Board of Directors and, where appropriate, the company's chief executive officer; exercise leadership of the Board of Directors and be accountable for its proper functioning; ensure that sufficient time is given to the discussion of strategic issues, and approve and review refresher courses for each director, when circumstances so advise.

Compliant

34. When a lead independent director has been appointed, the Articles of Association or Board of Directors regulations should grant him or her the following powers over and above those conferred by law: chair the Board of Directors in the absence of the Chairman or Deputy Chairman, if applicable; give voice to the concerns of non-executive directors; maintain contacts with investors and shareholders to hear their views and develop a balanced understanding of their concerns, especially those to do with the company's corporate governance; and coordinate the Chairman's succession plan.

Not applicable

35. The Secretary of the Board of Directors should strive to ensure that the Board's actions and decisions are informed by the governance recommendations of the Good Governance Code of relevance to the company.

Compliant

36. The plenary session of the Board of Directors should conduct an annual evaluation, adopting, where necessary, an action plan to correct weakness detected in:

a) The quality and efficiency of the Board's operation.

b) The performance and membership of its committees.

c) The diversity of Board Membership and competences

d) The performance of the Chairman of the Board of Directors and the company's chief executive.

e) The performance and contribution of individual directors, with particular attention to the Chairmen of Board committees.

The evaluation of Board committees should start from the reports they send the Board of Directors, while that of the Board of Directors itself should start from the report of the Nomination Committee.

Every three years, the Board of Directors should engage an external facilitator to aid in the evaluation process. This facilitator's independence should be verified by the Nomination Committee.

Any business dealings that the facilitator or members of its corporate group maintain with the company or members of its corporate group should be detailed in the annual corporate governance report.

The process followed and areas evaluated should be detailed in the annual corporate governance report.

Partially compliant

The Board of Directors, once a year, makes its self-assessment, which assesses the quality and efficiency of its operation, the diversity in its composition, its powers as a collegiate body, the performance of the Chairman and the Managing Director and the functioning and the composition of its commissions. Although this analysis considers the contributions made by the different Directors in general, an individualized report of the performance of each one of them is not made. Is for this reason alone because it said that this recommendation is partially fulfilled.

37. When a Steering Committee exists, its membership mix by director class should resemble that of the Board of Directors. The Secretary of the Board of Directors should also act as Secretary to the Steering Committee.

Compliant

38. The Board of Directors should be kept fully informed of the business transacted and decisions made by the Steering Committee. To this end, all Board Members should receive a copy of the committee's minutes.

Partially compliant

At each meeting of the Board the matters that have been discussed at the Steering Committee, at the Audit Committee and at the Appointments and Remuneration Committee are set out. The Minutes of the Committees are provided to the members thereof for their approval and are available to all of the directors.

However, above all, the Secretary begins each meeting session of the Board of Directors by setting out all of the matters discussed, as well as the decisions adopted, not only by the Steering Committee but also by all of the Committees that have been held as from the last plenary session of the Board. This system is more effective than the system provided for in the recommendation as it enables the plenary session of the Board to understand (i) in real time and not with a month's delay, of all of the matters discussed and (ii) not only the matters discussed at the Steering Committee, but rather all of the matters discussed at all of the Committees.

39. All members of the Audit Committee, particularly its Chairman, should be appointed with regard to their knowledge and experience in accounting, auditing and risk management matters. A majority of committee places should be held by independent directors.

Compliant

40. Listed companies should have a unit in charge of the internal audit function, under the supervision of the Audit Committee, to monitor the effectiveness of reporting and control systems. This unit should report functionally to the Board's non-executive Chairman or the Chairman of the Audit Committee.

Partially compliant

The Internal Auditing, Compliance and Control Unit monitors and ensures, *inter alia*, the proper functioning and internal control of the reporting and control systems and reports to the Managing Director, who is the CEO. The aforementioned Internal Auditing, Compliance and Control Unit reports its activities, in turn, to the Audit Committee that also authorises the annual budget thereof.

41. The head of the unit handling the internal audit function should present an annual work programme to the Audit Committee, inform it directly of any incidents arising during its implementation and submit an activities report at the end of each year.

Compliant

42. The Audit Committee should have the following functions over and above those legally assigned:

1. With respect to internal control and reporting systems:

- a) Monitor the preparation and the integrity of the financial reporting prepared on the company and, where appropriate, the group, checking for compliance with legal provisions, the accurate demarcation of the consolidation perimeter, and the correct application of accounting principles.
- b) Monitor the independence of the unit handling the internal audit function; propose the selection, appointment, re-election and removal of the head of the internal audit service; propose the service's budget; approve its priorities and work programmes, ensuring that it focuses primarily on the main risks the company is exposed to; receive regular report-backs on its activities; and verify that senior management are acting on the findings and recommendations of its reports.
- c) Establish and supervise a mechanism whereby staff can report, confidentially and, if appropriate and feasible, anonymously, any significant irregularities that they detect in the course of their duties, in particular financial or accounting irregularities.

2. With regard to the external auditor:

- a) Investigate the issues giving rise to the resignation of the external auditor, should this come about.
- b) Ensure that the remuneration of the external auditor does not compromise its quality or independence.
- c) Ensure that the company notifies any change of external auditor to the CNMV (Spanish Securities and Exchange Commission) as a material event, accompanied by a statement of any disagreements arising with the outgoing auditor and the reasons for the same.
- d) Ensure that the external auditor has a yearly meeting with the plenary session of the Board of Directors to inform it of the work undertaken and developments in the company's risk and accounting positions.
- e) Ensure that the company and the external auditor adhere to current regulations on the provision of non-audit services, limits on the concentration of the auditor's business and other requirements concerning auditor independence.

Compliant

43. The Audit Committee should be empowered to meet with any company employee or manager, even ordering their appearance without the presence of another senior officer.

Compliant

44. The Audit Committee should be informed of any fundamental changes or corporate transactions the company is planning, so the committee can analyse the operation and report to the Board of Directors beforehand on its economic conditions and accounting impact and, when applicable, the exchange ratio proposed.

Compliant

45. Risk control and management policy should identify at least:

- a) The different types of financial and non-financial risk the company is exposed to (including operational, technological, financial, legal, social, environmental, political and reputational risks), with the inclusion under financial or economic risks of contingent liabilities and other off-balance-sheet risks.
- b) The determination of the risk level the company sees as acceptable.
- c) The measures in place to mitigate the impact of identified risk events should they occur.
- d) The internal control and reporting systems to be used to control and manage the above risks, including contingent liabilities and off-balance-sheet risks.

Compliant

46. Companies should establish a risk control and management function in the charge of one of the company's internal department or units and under the direct supervision of the Audit Committee or some other dedicated Board committee. This function should be expressly charged with the following responsibilities:

- a) Ensure that risk control and management systems are functioning correctly and, specifically, that major risks the company is exposed to are correctly identified, managed and quantified.
- b) Participate actively in the preparation of risk strategies and in key decisions about their management.
- c) Ensure that risk control and management systems are mitigating risks effectively in the frame of the policy drawn up by the Board of Directors.

Compliant

47. Appointees to the nomination and remuneration committee – or of the Nomination Committee and remuneration committee, if separately constituted – should have the right balance of knowledge, skills and experience for the functions they are called on to discharge. The majority of their members should be independent directors.

Compliant

48. Large cap companies should operate separately constituted nomination and remuneration committees.

Explain

The Company has a single Appointments and Remuneration Committee as it considers that it is not necessary or efficient to separate the functions thereof.

49. The Nomination Committee should consult with the company's Chairman and chief executive, especially on matters relating to executive directors.

When there are vacancies on the Board of Directors, any director may approach the Nomination Committee to propose candidates that it might consider suitable.

Compliant

50. The remuneration committee should operate independently and have the following functions in addition to those assigned by law:

- a) Propose to the Board of Directors the standard conditions for senior officer contracts.
- b) Monitor compliance with the remuneration policy set by the company.
- c) Periodically review the remuneration policy for directors and senior officers, including share-based remuneration systems and their application, and ensure that their individual compensation is proportionate to the amounts paid to other directors and senior officers in the company.
- d) Ensure that conflicts of interest do not undermine the independence of any external advice the committee engages.
- e) Verify the information on director and senior officer's pay contained in corporate documents, including the annual directors' remuneration statement.

Compliant

51. The remuneration committee should consult with the company's Chairman and chief executive, especially on matters relating to executive directors and senior officers.

Compliant

52. The terms of reference of supervision and control committees should be set out in the Board of Directors regulations and aligned with those governing legally mandatory Board committees as specified in the preceding sets of recommendations. They should include at least the following terms:

- a) Committees should be formed exclusively by non-executive directors, with a majority of independent directors.
- b) They should be chaired by independent directors.
- c) The Board of Directors should appoint the members of such committees with regard to the knowledge, skills and experience of its directors and each committee's terms of reference; discuss their proposals and reports; and provide report-backs on their activities and work at the first plenary session of the Board following each committee meeting.
- d) They may engage external advice, when they feel it necessary for the discharge of their functions.
- e) Meeting proceedings should be minuted and a copy made available to all Board Members.

Not applicable

53. The task of supervising compliance with corporate governance rules, internal codes of conduct and corporate social responsibility policy should be assigned to one Board committee or split between several, which could be the Audit Committee, the Nomination Committee, the corporate social responsibility committee, where one exists, or a dedicated committee established ad hoc by the Board of Directors under its powers of self-organisation, with at the least the following functions:

- a) Monitor compliance with the company's internal codes of conduct and corporate governance rules.
- b) Oversee the communication and relations strategy with shareholders and investors, including small and medium-sized shareholders.
- c) Periodically evaluate the effectiveness of the company's corporate governance system, to confirm that it is fulfilling its mission to promote the corporate interest and catering, as appropriate, to the legitimate interests of remaining stakeholders.
- d) Review the company's corporate social responsibility policy, ensuring that it is geared to value creation.
- e) Monitor corporate social responsibility strategy and practices and assess compliance in their respect.
- f) Monitor and evaluate the company's interaction with its stakeholder groups.
- g) Evaluate all aspects of the non-financial risks the company is exposed to, including operational, technological, legal, social, environmental, political and reputational risks.
- h) Coordinate non-financial and diversity reporting processes in accordance with applicable legislation and international benchmarks.

Compliant

54. The corporate social responsibility policy should state the principles or commitments the company will voluntarily adhere to in its dealings with stakeholder groups, specifying at least:

- a) The goals of its corporate social responsibility policy and the support instruments to be deployed.
- b) The corporate strategy with regard to sustainability, the environment and social issues.
- c) Concrete practices in matters relative to: shareholders, employees, clients, suppliers, social welfare issues, the environment, diversity, fiscal responsibility, respect for human rights and the prevention of illegal conducts.
- d) The methods or systems for monitoring the results of the practices referred to above, and identifying and managing related risks.
- e) The mechanisms for supervising non-financial risk, ethics and business conduct.
- f) Channels for stakeholder communication, participation and dialogue.
- g) Responsible communication practices that prevent the manipulation of information and protect the company's honour and integrity.

Compliant

55. The company should report on corporate social responsibility developments in its directors' report or in a separate document, using an internationally accepted methodology.

Compliant

56. Director remuneration should be sufficient to attract individuals with the desired profile and compensate the commitment, abilities and responsibility that the post demands, but not so high as to compromise the independent judgement of non-executive directors.

Compliant

57. Variable remuneration linked to the company and the director's performance, the award of shares, options or any other right to acquire shares or to be remunerated on the basis of share price movements, and membership of long-term savings schemes such as pension plans should be confined to executive directors.

The company may consider the share-based remuneration of non-executive directors provided they retain such shares until the end of their mandate. This condition, however, will not apply to shares that the director must dispose of to defray costs related to their acquisition.

Compliant

58. In the case of variable awards, remuneration policies should include limits and technical safeguards to ensure they reflect the professional performance of the beneficiaries and not simply the general progress of the markets or the company's sector, or circumstances of that kind.

In particular, variable remuneration items should meet the following conditions:

- a) Be subject to predetermined and measurable performance criteria that factor the risk assumed to obtain a given outcome.
- b) Promote the long-term sustainability of the company and include non-financial criteria that are relevant for the company's long-term value, such as compliance with its internal rules and procedures and its risk control and management policies.
- c) Be focused on achieving a balance between the delivery of short, medium and long-term objectives, such that performance-related pay rewards on-going achievement, maintained over sufficient time to appreciate its contribution to long-term value creation. This will ensure that performance measurement is not based solely on one-off, occasional or extraordinary events.

Compliant

59. A major part of variable remuneration components should be deferred for a long enough period to ensure that predetermined performance criteria have effectively been met

Compliant

60. Remuneration linked to company earnings should bear in mind any qualifications stated in the external auditor's report that reduce their amount.

Explain

The variable remuneration of the Managing Director does not expressly take into account the qualifications that may exist in the external auditor's report and that reduce the sum thereof, nor is the foregoing a situation that has existed at the Company in the past. Notwithstanding the foregoing, the Appointments and Remuneration Committee only established the degree of compliance with the variable remuneration objectives after the audited accounts of the Company have been received, and accordingly the Committee is able to take into account any qualifications that exist therein, if applicable, when determining the degree of compliance of the objectives.

61. A major part of executive directors' variable remuneration should be linked to the award of shares or financial instruments whose value is linked to the share price.

Explain

The variable remuneration of the Managing Director is not structured by way of the award of shares or financial instruments whose value is linked to the share price. The Board considers that it is more effective and simple to structure the objective of the creation of value for the shareholder by means of the establishment of an objective regarding the foregoing and to assign a relevant weighting to said objective. As is explained in the annual remunerations report, the multiannual variable remuneration is designed as set out hereinabove, with a weighting of 25% of the established objectives.

62. Following the award of shares, share options or other rights on shares derived from the remuneration system, directors should not be allowed to transfer a number of shares equivalent to twice their annual fixed remuneration, or to exercise the share options or other rights on shares for at least three years after their award.

The above condition will not apply to any shares that the director must dispose of to defray costs related to their acquisition.

Not applicable

63. Contractual arrangements should include provisions that permit the company to reclaim variable components of remuneration when payment was out of step with the director's actual performance or based on data subsequently found to be misstated.

Explain

The contract executed with the current Managing Director was formalised in 2005 and does not contain said provision.

64. Termination payments should not exceed a fixed amount equivalent to two years of the director's total annual remuneration and should not be paid until the company confirms that he or she has met the predetermined performance criteria.

Explain

The contract executed with the current Managing Director was formalised in 2005 and establishes a compensation entitlement in certain situations of three years of full remuneration. The terms of the modifications thereof, in October 2016, are set out in the annual remunerations report.

H. Other information of interest

1. If there are any significant aspects regarding corporate governance at the company or at entities of the group that is not included in the other sections of this report, but should be included in order to provide more complete and well-reasoned information regarding the corporate governance structure and practices at the entity or its group, briefly describe them.
2. In this section, you may also include any other information, clarification, or comment relating to the prior sections of this report to the extent they are relevant and not repetitive

Specifically, state whether the company is subject to laws other than Spanish laws regarding corporate governance and, if applicable, include such information as the company is required to provide that is different from the information required in this report.

3. The company may also state whether it has voluntarily adhered to other international, industrial, or other codes of ethical principles or good practices. If so, identify the code in question and the date of adherence thereto.

The Board of Directors, at its meeting of September 17, 2010, agreed to the adhesion of Gas Natural Fenosa to the Code of Good Tax Practices. In accordance with the provisions of the aforementioned Code, it is expressly stated that Gas Natural Fenosa has effectively complied with its content and, in particular, that at the meeting held on February 7, 2017, the Gas Natural Audit Committee Fenosa has been informed about the fiscal policies followed by the Group during the 2016 financial year.

Note to C.1.2

Mr. Salvador Gabarró Serra by agreement of the Board of Directors dated September 30, 2016 was named Honorary Chairman of the Company.

Note to C.1.9

Mr. Juan Rosell Lastortras submitted his resignation by letter dated 20 September 2016 without expressing the reasons for his resignation.

Note to C.1.12.- Clarification of the position

Mrs. Cristina Garmendia Mendizábal is President of the Supervisory Board at SYGNIS AG.

Note to C.1.16

Total remuneration of senior management has taken into account that received by Mr. José Javier Fernández Martínez as General Director of Global Power Generation, until his retirement in April 2016.

Note to C.1.45

The Appointments and Remuneration Committee is informed of such contracts. Amendments to the Managing Director's contract or the new contractual schemes of the members of the Management Committee must be approved by the Board of Directors.

The Managing Director's contract has been approved by the Company's Board of Directors.

Nota al G 10

Throughout 2016 this has not occurred. The applicable rules would have given rise to different voting rules for the proposed resolutions formulated by the Board in relation to those proposed by other shareholders. In the first case, votes corresponding to the shares present or represented, minus the votes against, the abstentions and the votes of those shareholders who had left the voting room before the vote, would be considered as votes in favor. With respect to the second case, votes to the shares present or represented shall be considered as votes against and, the votes against, as well as the abstentions and the votes of those shareholders who had left the room before the vote were recorded, have to be considered as votes in favor.

This annual corporate governance report has been approved by the company's board of directors at its meeting on February 7, 2017.

Indicate whether there have been directors who have voted against or abstained in connection with the approval of this Report.

No

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