Naturgy Energy Group, S.A.
Annual Report 2018

Looking forward with energy

Naturgy

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Annual Report 2018

Sumary

Naturgy Energy Group, S.A.
Annual Report 2018

Audit Report, Individual Annual Accounts

Translation of a report originally issued in Spanish. In the event of discrepancy, the Spanish-language version prevails

AUDIT REPORT ON FINANCIAL STATEMENTS ISSUED BY AN INDEPENDENT AUDITOR

To the Shareholders of Naturgy Energy Group, S.A.:

Audit report on the financial statements

Opinion

We have audited the financial statements of Naturgy Energy Group, S.A. (the Company), which comprise the balance sheet at December 31, 2018, the income statement, the statement of changes in equity, the cash flow statement, and the notes thereto for the year then ended.

In our opinion, the accompanying financial statements give a true and fair view, in all material respects, of the equity and financial position of the Company at December 31, 2018 and of its financial performance and its cash flows for the year then ended in accordance with the applicable regulatory framework for financial information in Spain (identified in Note 2 to the accompanying financial statements) and, specifically, the accounting principles and criteria contained therein.

Basis for Opinion

We conducted our audit in accordance with prevailing audit regulations in Spain. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our report.

We are independent of the Company in accordance with the ethical requirements, including those related to independence, that are relevant to our audit of the financial statements in Spain as required by prevailing audit regulations. In this regard, we have not provided non-audit services nor have any situations or circumstances arisen that might have compromised our mandatory independence in a manner prohibited by the aforementioned requirements.

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

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our audit opinion thereon, and we do not provide a separate opinion on these matters.

Assessment of the recovery of the book value of long-term investments in group companies and associates

Description

As detailed in Note 7 to the accompanying financial statements, the Company shows long-term investments in group companies and associates amounting to 15,237 million euros.

The determination of the recoverable amounts of the long-term investments in group companies and associates is based on estimates that require Management to use cash flow projections based on current results. These cash flows are calculated based on the new 2018-2022 Strategic Plan approved by the Board of Directors, whose key assumptions are detailed in Note 4 to the accompanying financial statements. Additionally, Management have made a sensitivity analysis of the most significant assumptions that, based on historical experience, may reasonably experience some variations.

As a result of the aforementioned analyses, Company Management have recorded an impairment loss amounting to 4,565 million euros (Note 7).

Given the significance of the balance of the 'Long-term investments in group companies and associates' heading and the existence of significant estimates regarding the key assumptions used in the calculations made by Management, we consider this area a key audit matter.

Our response

Our audit procedures for this area consisted, among others, in:

- Understanding the processes established by Company Management in the determination of the impairment of long-term investments in group companies and associates, including the assessment of the design and implementation of relevant controls.
- Reviewing whether any indications of impairment exist and, where appropriate, reviewing the model used by Company Management, in collaboration with our valuation specialists, covering, in particular, the mathematical consistency of the model, the reasonableness of projected cash flows, discount rates and long-term growth rates, and the results of the sensitivity analyses made by Company Management. In the performance of our review we held meetings with the people in charge of the businesses and used renowned external sources and other available information to verify the data used by Company Management.
- Reviewing the disclosures included in the notes to the financial statements in accordance with the applicable regulatory framework for financial reporting.

Transfer of 20% ownership interest in Holding Negocios del Gas, S.A.

Description

As detailed in Note 7 to the accompanying financial statements, on August 3, 2017 the Company signed an agreement with the consortium made up of Allianz Capital Partners and Canada Pension Plan Investment Board to sell a 20% ownership interest in the natural gas distribution business in Spain for an amount of 1,500 million euros following an increase in debt through a long-term intra-group financing facility by the Company amounting to 6,000 million euros. The transaction was subject to the necessary regulatory and anti-trust approvals.

For the transaction to be completed, in February 2018, Holding de Negocios de Gas, S.A., wholly-owned by the Company, became the parent of the natural gas distribution and transport and the liquefied petroleum gas (LPG) distribution activities in Spain, by acquiring from the Company its entire ownership interest in Nedgia, S.A. (formerly Holding Negocios Regulados Gas Natural, S.A., which is the holding company of the shares of the Spanish gas distribution companies) for an amount of 11,518 million euros. Said amount was determined as fair value based on the same price per share established in the aforementioned sale agreement with the Consortium, which was ratified by the fairness opinions provided by the investment banks J.P. Morgan and Morgan Stanley, which acted as financial advisors of the transaction and concluded that the value was fair from a financial perspective. Additionally, in accordance with section 1 of Recognition and Measurement Standard 21 of the Spanish General Accounting Plan, the transaction carried out was recorded at fair value and generated profit of 9,537 million euros for the Company.

On March 19, 2018, once the necessary regulatory and anti-trust approvals were obtained, the Company transferred a 20% ownership interest in Holding Negocios de Gas, S.A. to the aforementioned Consortium for an amount of 1,500 million euros in cash. The transaction had no significant impact on profit or loss since the ownership interest was recorded at fair value.

Given the significance of the amounts involved in this transaction, we have consider this area a key audit matter.

Our response

Our audit procedures for this area consisted, among others, in:

- Reviewing the sale agreement reached with the Consortium for the transfer of a 20% ownership interest in the natural gas distribution business in Spain.
- Reviewing the valuation reports by the financial advisors on the fair value of this transaction established in the sale agreement.
- Reviewing the intra-group agreements associated with this transaction.
- Verifying the accounting treatment followed by the Company for recording the transaction.
- Reviewing the information disclosed in the notes to the financial statements for the year regarding this transaction.

Other information: Management Report

Other information refers exclusively to the 2018 management report, the preparation of which is the responsibility of the Company's directors and is not an integral part of the financial statements.

Our audit opinion on the financial statements does not cover the management report. Our responsibility for the information contained in the management report is defined in prevailing audit regulations, which distinguish two levels of responsibility:

a. A specific level applicable to the non-financial information statement, as well as certain information included in the Corporate Governance Report, as defined in article 35.2 b) of Law 22/2015 on auditing, which solely requires that we verify whether said information has been included in the management report or where applicable, that the management report includes the corresponding reference to the separate non-financial report as stipulated by prevailing regulations and if not, disclose this fact.

b. A general level applicable to the remaining information included in the management report, which requires us to evaluate and report on the consistency of said information in the financial statements, based on knowledge of the entity obtained during the audit, excluding information not obtained from evidence. Moreover, we are required to evaluate and report on whether the content and presentation of this part of the management report are in conformity with applicable regulations. If, based on the work carried out, we conclude that there are material misstatements, we are required to disclose them.

Based on the work performed, as described above, we have verified that the information referred to in paragraph a) above is provided in the management report, and that the remaining information contained therein is consistent with that provided in the 2018 financial statements and their content and presentation are in conformity with applicable regulations.

Responsibility of the Directors and the audit committee for the financial statements

The directors are responsible for the preparation of the accompanying financial statements so that they give a true and fair view of the equity, financial position and results of the Company, in accordance with the regulatory framework for financial information applicable to the Company in Spain, identified in Note 2 to the accompanying financial statements, and for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

The audit committee is responsible for overseeing the financial reporting process.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with prevailing audit regulations in Spain will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with prevailing audit regulations in Spain, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the audit committee of the Company regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the audit committee of the Company with a statement that we have complied with relevant ethical requirements, including those related to independence, and communicate to them all matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated to the audit committee of the Company, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters.

We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter.

Report on other legal and regulatory requirements

Additional report for the audit committee

The opinion expressed in this audit report is consistent with the additional report we issued to the audit committee of the Company on January 31, 2019.

Term of engagement

The ordinary general shareholders' meeting held on April 20, 2017 appointed us as auditors for 3 years, commencing on December 31, 2018.

ERNST & YOUNG, S.L.
(Signature on the original in Spanish)

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Alfredo Eguiagaray

January 31, 2019

Balance sheet (million euro)

	31.12.18	31.12.17
Non-current Assets	**31,317**	**29,453**
Intangible assets (Note 5)	32	114
Goodwill	27	109
Other intangible assets	5	5
Property, plant and equipment (Note 6)	141	151
Land and buildings	127	134
Other property, plant and equipment	14	17
Long-term investments in Group companies and associates (Note 7)	30,894	29,015
Equity instruments	15,237	13,400
Loans to companies	15,657	15,615
Long-term investments (Note 8)	17	40
Equity instruments	5	5
Derivatives	–	8
Other financial assets	12	27
Other non-current assets (Note 14)	81	–
Deferred income tax assets (Note 17)	152	133
Current assets	**2,225**	**4,512**
Trade and other receivables (Note 9)	661	650
Trade receivables	101	121
Trade receivables, group companies and associates	366	345
Sundry receivables	129	155
Current tax assets	65	29
Short-term investments in Group companies and associates (Note 7)	797	2,223
Loans to companies	740	1,480
Other financial assets	57	743
Short-term investments (Note 8)	44	85
Derivatives	8	56
Other financial assets	36	29
Short-term prepayments and accrued expenses	1	1
Cash and cash equivalents (Note 10)	722	1,553
Cash at banks and in hand	722	1,453
Other cash equivalents	–	100
Total assets	**33,542**	**33,965**

Notes 1 to 30 form an integral part of these annual accounts.

Balance sheet (million euro)

	31.12.18	31.12.17
Equity (Note 11)	**17,226**	**13,466**
Shareholders' funds	**17,253**	**13,473**
Capital	1,001	1,001
Authorised capital	1,001	1,001
Share premium	3,808	3,808
Reserves	8,009	7,971
Legal and statutory	300	300
Other reserves	7,709	7,671
Treasury shares	(121)	–
Profit for the year	5,282	1,023
Interim dividend	(730)	(330)
Other equity instruments	4	–
Adjustments for changes in value	**(27)**	**(7)**
Hedging operations	(27)	(7)
Non-current liabilities	**13,085**	**16,113**
Long-term provisions (Note 12)	478	465
Long-term post-employment obligations	256	272
Other provisions	222	193
Long-term borrowings (Note 13)	2,040	3,912
Bank borrowings	1,985	3,851
Derivatives	54	47
Other financial liabilities	1	14
Amounts owing to group companies and associates falling due in more than one year (Note 15)	10,273	11,508
Deferred income tax liabilities (Note 17)	212	227
Other liabilities	81	–
Long-term accruals	1	1
Current liabilities	**3,231**	**4,386**
Short-term borrowings (Note 13)	246	328
Bank borrowings	233	270
Derivatives	9	44
Other financial liabilities	4	14
Amounts owing to group companies and associates falling due in less than one year (Note 15)	2,283	3,307
Trade and other payables (Note 16)	701	751
Trade payables	249	194
Trade payables, Group companies and associates	267	289
Sundry payables	129	140
Personnel (outstanding remuneration)	29	45
Other amounts payable to Public Administrations	27	83
Short-term accruals	1	–
Total equity and liabilities	**33,542**	**33,965**

Notes 1 to 30 form an integral part of these annual accounts.

Income statement (million euro)

	2018	2017
Revenue (Note 18)	4,527	5,053
Sales	3,464	3,139
Income from equity instruments of Group companies and associates (Note 7)	547	1,470
Income from marketable securities and other financial instruments of Group companies and associates	516	444
Supplies (Note 19)	(3,470)	(3,148)
Consumption of goods	(3,464)	(3,142)
Raw materials and other consumables	(6)	(6)
Other operating income (Note 22)	380	383
Supplementary income and other operating income	379	383
Operating grants released to the income statement	1	–
Personnel expenses (Note 20)	(262)	(234)
Wages, salaries and related expenses	(215)	(180)
Social Security	(33)	(39)
Provisions	(14)	(15)
Other operating expenses (Note 21)	(315)	(344)
External services	(304)	(342)
Taxes	(2)	(2)
Impairment loss and variation in trade provisions	(9)	–
Fixed asset depreciation/amortisation (Notes 5 and 6)	(98)	(91)
Impairment and results on disposals of fixed assets	5,025	(123)
Gain/(loss) on disposals of tangible fixed assets (Note 6)	1	3
Impairment and losses from equity instruments of Group companies and associates (Note 7)	(4,565)	(133)
Gain/(loss) on disposals of equity interests in Group companies and associates (Note 7)	9,589	7
Operating profit/(loss)	**5,787**	**1,496**
Financial income	30	31
Negotiable securities and other financial instruments	30	31
In third parties	30	31
Financial expenses	(536)	(586)
Borrowings from group companies and associates	(464)	(482)
Borrowings from third parties	(72)	(104)
Variation in fair value of financial instruments	8	1
Investments	8	1
Exchange differences	(8)	(1)
Impairment and gains/(losses) on disposals of financial instruments	1	–
Impairment due to disposals of financial instruments	1	–
Net financial income (Note 23)	**(505)**	**(555)**
Profit/(loss) before taxes	**5,282**	**941**
Income tax (Note 17)	–	82
Profit for the year	**5,282**	**1,023**
Basic and diluted earnings per share in euro	5.29	1.02

Notes 1 to 30 form an integral part of these annual accounts.

Statement of changes in equity (million euro)

A) Statement of recognised income and expenses

Profit for the year	**5,282**	**1,023**
Income and expense recognised directly in equity	**(2)**	**(17)**
Cash flow hedges	(28)	(31)
Actuarial gains and losses and other adjustments (Note 12)	24	8
Tax effect (Note 17)	2	6
Releases to income statement	**1**	**3**
Cash flow hedges	1	4
Tax effect (Note 17)	–	(1)
Total income and expense recognised in equity	**5,281**	**1,009**

B) Total statement of changes in equity

	Share capital	Share premium	Reserves	Treasury shares	Profit or loss brought forward	Profit for the year	Interim dividend	Other instruments	Adjustments for changes in value	Total
Balance at 01.01.2017	**1,001**	**3,808**	**7,898**	**(13)**	**–**	**1,067**	**(330)**	**–**	**13**	**13,444**
Total recognised revenues and expenses	–	–	6	–	–	1,023	–	–	(20)	1,009
Operations with shareholders or owners										
- Dividend distribution (Note 11)	–	–	–	–	(671)	–	(330)	–	–	(1,001)
- Trading in treasury shares (Note 11)	–	–	1	13	–	–	–	–	–	14
Other changes in equity (Note 11)	–	–	66	–	671	(1,067)	330	–	–	–
Balance at 31.12.2017	**1,001**	**3,808**	**7,971**	**–**	**–**	**1,023**	**(330)**	**–**	**(7)**	**13,466**
Total recognised revenues and expenses	–	–	15	–	–	5,282	–	4	(20)	5,281
Operations with shareholders or owners										
- Dividend distribution (Note 11)	–	–	–	–	(670)	–	(730)	–	–	(1,400)
- Trading in treasury shares (Note 11)	–	–	–	(121)	–	–	–	–	–	(121)
Other changes in equity (Note 11)	–	–	23	–	670	(1,023)	330	–	–	–
Balance at 31.12.2018	**1,001**	**3,808**	**8,009**	**(121)**	**–**	**5,282**	**(730)**	**4**	**(27)**	**17,226**

Notes 1 to 30 form an integral part of these annual accounts.

Cash flow statement (million euro)

	2018	2017
Profit for the year before tax	**5,282**	**941**
Adjustments to results	**(5,461)**	**(1,124)**
Fixed asset depreciation/amortisation (Notes 5 and 6)	98	91
Impairment adjustments	4,574	133
Change in provisions	11	8
Profit/(loss) on write-offs and disposals of fixed assets	(2)	(3)
Profit/(loss) on write-offs and disposals of financial instruments	(9,589)	(7)
Financial income	(1,093)	(1,945)
Financial expenses	536	586
Exchange differences	8	1
Variation in fair value of financial instruments	(8)	(1)
Other income and expenses	4	13
Changes in working capital	**(180)**	**160**
Debtors and other receivables	(110)	114
Creditors and other payables	(70)	46
Other cash flows from operating activities	**1,292**	**695**
Interest paid	(523)	(593)
Dividends received	1,172	812
Interest collected	539	478
Income tax collections/(payments)	104	(2)
Cash flows from operating activities	**933**	**672**
Amounts paid on investments	**(14,894)**	**(1,304)**
Group companies and associates	(14,883)	(1,283)
Intangible assets	(1)	–
Property, plant and equipment	(10)	(16)
Other financial assets	–	(5)
Amounts collected from divestments	**17,709**	**1,032**
Group companies and associates	17,675	658
Property, plant and equipment	5	12
Other financial assets	29	362
Cash flows from investing activities	**2,815**	**(272)**
Collections and payments on equity instruments	**(110)**	**14**
Acquisition of own equity instruments	(416)	–
Disposal of own equity instruments	306	14
Collections and payments financial liability instruments	**(3,069)**	**1,638**
Issuance	8,431	8,983
Bank borrowings	178	969
Payables to Group companies and associates	8,252	8,014
Other payables	1	–
Repayment/redemption of	(11,500)	(7,345)
Bank borrowings	(2,083)	(261)
Payables to Group companies and associates	(9,381)	(7,057)
Other payables	(36)	(27)
Dividend payments	**(1,400)**	**(1,001)**
Cash flow from financing activities	**(4,579)**	**651**
NET INCREASE/DECREASE IN CASH OR CASH EQUIVALENTS	**(831)**	**1,051**
Cash and cash equivalents at the beginning of the year	1,553	502
Cash and cash equivalents at the year end	722	1,553

Notes 1 to 30 form an integral part of these annual accounts.

Notes to the annual accounts of Naturgy Energy Group, S.A. for the year ended 31 December 2018

Note 1. General information

Naturgy Energy Group, S.A. ("the Company"), the parent company of the Naturgy group ("Naturgy"), was incorporated as a public limited company in 1843 and its registered office for corporate purposes is in Avda. de San Luis 77, Madrid. On 27 June 2018, the shareholders, in general meeting, agreed to change the company's business name to Naturgy Energy Group, S.A., formerly Gas Natural SDG, S.A.

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 administration and management of its shareholdings in subsidiaries. It also has gas supply contracts for other Naturgy companies and in the electricity area it acts as representative of the Naturgy generation and supply companies before the Electricity Market.

The Company's shares are listed on the four Spanish stock exchanges, the continuous market and form part of the Ibex 35 stock index.

Note 2. Basis of presentation

The Company's annual accounts for 2017 were approved by the annual general meeting of shareholders on 27 June 2018.

The annual accounts for 2018, which were drawn up and signed by the Company's Board of Directors on 29 January 2019, will be submitted to the general shareholders' 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 2018, and the results, changes in equity and cash flows of the Company for then ended.

At 31 December 2018, the Company recorded working capital which was negative by Euros 1,006 million. In this respect, the Company's liquidity statements envisaged for the coming year, with the amounts available under credit lines, will ensure coverage of the working capital.

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

The consolidated Annual accounts of Naturgy for 2018 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	40,631
Equity attributed to the parent company	10,948
Non-controlling interests	3,647
Revenue	24,339
Net income after tax attributed to the parent Company	(2,822)

Note 3. Accounting policies

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

3.1. 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 over ten years using the straight-line method. 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

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 over a period of five years as from the time the assets are prepared to be brought into use.

Research expenditure is recognised in the income statement when incurred.

The Company has no intangible assets with an indefinite useful life.

3.2. Property, plant and equipment

Property, plant and equipment are carried at cost less accumulated depreciation and any impairment provision.

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.

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 3.3).

3.3. Asset impairment

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, 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. The Company considers value in use as the recoverable amount, calculated as 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).

For investments in group companies and associates, barring investments the recoverable amount of which is determined based on the investee's equity (Note 3.4), which have required an analysis of potential impairment losses, the cash flows employed are based on the Strategic Plan approved by the Company, updated where appropriate by the most recently approved budgets and extended to a maximum total of 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 five-year 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 parameters taken into account to determine the growth rates, which represent the long-term growth of each line of business, are in line with the long-term growth of the country, obtained from estimated inflation for the period 2021 to 2045 according to the Economist Intelligence Unit (EIU).

The parameters taken into account for the composition of the discount rates before taxes are as follows:

- Risk free rate: Considering the 10-year Bond reference market for the CGU as well as studies of the European Central Bank, the Bank of Spain and others.
- Market risk premium: Premium based on studies of the European Central Bank, the Bank of Spain and others.
- Deleveraged Beta: According to average of each sector in each case, obtained from Bloomberg.
- Local current interest rate swaps: 10-year swap, obtained from Bloomberg.
- Equity-debt ratio: Sector average.

Impairment adjustments to values recognised in previous periods for investments in Group companies and associates may be reversed if and only if there is a change in the estimates used to determine their recoverable amount since the latest impairment loss was recognised.

3.4. Financial assets and liabilities

The Company classifies its financial assets and liabilities based on their valuation which is determined on the basis of the business model and the characteristics of the contractual cash flow.

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 recognized on trade-date, which is the date on which the Company 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.

The necessary value adjustments due to impairment are made if there is objective evidence that the entire amount owed will not be collected. 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.

The are recognised at fair value. Unrealised gains and losses that arise from changes in fair value are recorded in equity. When these assets are sold or impaired over a lengthy period of time, the accumulated adjustments to the reserves due to valuation adjustments are included in the Income statement as gains and losses.

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 the Company.

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.

3.5. 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 in designated as a hedging instrument, and if so, the nature of the asset being hedged.

Naturgy aligns its accounting with its management of financial risk. Risk management objectives and the hedging strategy are reviewed periodically and a description of the risk management objective pursued is carried out.

In order for each hedging operation to be considered effective, the Company documents that the economic relationship between the hedging instrument and the hedged asset is aligned with their entity's risk management objectives.

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 balance sheet date or, for some non-financial items, on best estimation on forward curves of said non-financial item.

The fair values are adjusted for the expected impact of observable counterparty credit risk in positive valuation scenarios and the impact of observable credit risk in 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 accountings

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 the Company 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 irrespective of whether the buyer 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 the Company in accordance with the energy purchase and sale estimates made periodically, which are monitored systematically and adjusted always may be by physical delivery. Consequently, these are negotiated contracts for “own use”, and, accordingly, lie beyond the standards on valuation of financial instruments.

3.6. Non-current assets held for sale and discontinued operations

The Company 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.

Additionally, the Company considers discontinued activities the components (cash generating units or groups of cash generating units) that make up a business line or geographic area of operations, which are significant and which can be considered separately from the rest, and which have been sold or disposed by other means or which meet the conditions to be classified as held-for-sale. Entities acquired solely for resale are also classed as discontinued operations.

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.

In the event of delays caused by events or circumstances beyond Naturgy’s control and there is sufficient evidence that the commitment to the plan to sell those classified as held for sale is maintained, the classification is maintained even though the period to complete the sale is extended beyond one year.

3.7. 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.

3.8. Share-based payments

Share-based and share-settled payments are measured by reference to the fair value of the equity instruments granted on the grant date.

The resulting cost is recognised under Personnel expenses in the income statement as the services are rendered by the employees during relevant vesting period, with a balancing entry in Other equity instruments in the balance sheet.

The amounts recognised in equity are not subject to a subsequent reassessment due to trends in external market conditions.

3.9. 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 the Company.

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.

3.10. Borrowings and equity instruments

Borrowings and equity instruments issued by Naturgy are classified based on the nature of the issue.

Naturgy treats all contracts that represent a residual share in net assets as equity instruments.

Equity instrument issuance costs are presented as a deduction in equity.

3.11. Provisions for employee obligations

a) Post-employment pension obligations and the like

- Defined contribution plans

  The Company, 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 the Company undertakes to make certain contributions to an insurance policy, guaranteeing 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 of 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, in “Reserves”.

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

b) Other post-employment benefit obligations

The Company provides post-employment benefits to its 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. The Company terminates the employment of current employees according to a detailed formal plan without possibility of withdrawal; or providing termination benefits. In the event that mutual agreement is required, the provision is only recorded in those situations in which the Company has decided to give its consent to voluntary redundancies once they have been requested by the employees.

3.12. Provisions

Provisions are recognized when the Company has a legal or implicit present 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.

3.13. 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 payment obligation arising from the lease, net of the finance charge, is recognised in liabilities in the balance sheet. The interest component of the finance charge is taken to the income statement over the term of the lease so as to produce a constant periodic rate of interest on the debt pending payment 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.

3.14. Corporate 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. No deferred tax liabilities are recognised for profits not distributed from the subsidiaries when Naturgy can control the reversal of the timing differences and it is likely that they will not reverse in the foreseeable future.

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.

3.15. Recognition of income and expenses

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. Revenue 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) 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)”.

3.16. 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.

3.17. 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 Naturgy.

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.

3.18. 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 the Company 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.

3.19. 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 Company revenues, as well as other activities that cannot be qualified as investing or financing.

b) Investing activities: the acquisition and disposal of non-current assets and other investments not included in cash and cash equivalents.

c) Financing activities: activities that result in changes in the size and composition of the equity and borrowings of the Company that are not operating activities.

3.20. 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 3.1 and 3.2)

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 3.3)

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 the Company, which have historically been substantially met.

c) Derivatives or other financial instruments (Note 3.5)

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. The Company 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 the Company for similar financial instruments.

d) Provisions for employee benefits (Note 3.11)

A number of assumptions must be used to calculate pension costs, other costs of post-retirement benefits and other post-retirement liabilities. The Company estimates at each year end the provision necessary to meet its pension liabilities and the like, in accordance with the 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 3.12)

The Company 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 3.14)

The calculation of the income tax expense requires interpretations of tax legislation in the jurisdictions in which the Company operates. The determination of expected outcomes of outstanding disputes and litigation requires the preparation of significant estimates and judgment. The Company evaluates the recoverability of the deferred income tax assets based on estimates of future taxable income. Deferred tax liabilities are recognised based on estimates of the net assets that will not be tax deductible in the future.

Note 4. Asset impairment

Definition of Cash Generating Unit

Following the approval on 27 June 2018 of the new Strategic Plan 2018-2022 which has introduced a new industrial and business unit model, and aligned the new structure with the new vision and management method for the lines of business and cash flows under the new Strategic Plan, a new definition of the Cash Generating Units (CGU) has been introduced, as follows:

- Gas and Electricity:
  - Supply of gas, electricity and services: The commercial management of natural gas, electricity and services is carried out on a comprehensive basis, maximising the value of the portfolio by focusing on customers and with high potential for growth in services and solutions, for which there is a single CGU.
  - International LNG sales: There is considered to be a single CGU, since the supply of liquefied natural gas and the maritime transport activity are managed on a global level.
  - Electricity Generation Europe: It is considered that there is a CGU for conventional electricity generation (hydro, coal, nuclear and combined cycle plants) and another CGU for renewable electricity generation (wind, mini-hydro, solar and cogeneration) taking into account the new strategic vision of the Spanish electricity market, with a greater presence in renewables and greater volatility in hourly prices, which requires specialisation in the management of conventional and renewable generation focused, respectively, on cost adjustment and an increase in the installed capacity, in line with the reorganisation carried out.

    In the past, these activities formed part of single CGU because they were managed and controlled jointly and centralised based on conditions of demand, where all power plants using different technologies played a major, complementary and necessary role in light of different market situations, providing the electricity required by customers at any given time. However, as a result of the auctions carried out during 2017 in which Naturgy was awarded a total capacity of 971 MW for wind and solar energy, the generation of renewable electricity will increase from 8% in 2017 with respect to conventional generation to more than 30% in 2020, increasing the quantitative contribution of income, investments and results, which are increasingly affected by the availability of parks, the volatility of electricity prices and the revisions of supplements remuneration, all of which means that the cash inflows from said renewable generation assets are considered independent of those from conventional generation assets for scale substantial increase.
  - International Electricity Generation: A CGU is understood to exist in each country in which there are operations (Brazil, Costa Rica, Mexico, Panama, Dominican Republic, Puerto Rico, Australia and Chile) since the businesses are subject to different regulatory frameworks and are managed independently.
- EMEA Infrastructures:
  - Gas distribution Spain: Is a single CGU as the development, operation and maintenance of the gas distribution network is managed jointly.
  - Electricity Distribution Spain: This makes up a single CGU since the network comprises a group of interrelated assets the development, operation and maintenance of which is managed jointly.
  - Maghreb Infrastructures: Is a single CGU which manages the Maghreb - Europe gas pipeline.
- Latin America South Infrastructures: A CGU is understood to exist for each business and country in which there are operations since the businesses are subject to different regulatory frameworks. It includes the regulated gas distribution business in Argentina, Brazil, Chile and Peru and the regulated electricity distribution business in Argentina and Chile.

- Latin America North Infrastructures: A CGU is understood to exist for each business and country in which there are operations since the businesses are subject to different regulatory frameworks. It includes the regulated gas distribution business in Mexico and the regulated electricity distribution business in Panama.

- Remainder: Basically includes the Unión Fenosa Gas CGU and the gas storage business.

In summary, and with respect to the previous year, the Electricity Spain CGU has been divided into: i) Supply of electricity; ii) Generation of conventional electricity; and iii) Generation of renewable electricity.

Information on recognised impairments

In 2017 an impairment of Euros 109 million was recognised with respect to the 50% interest in Unión Fenosa Gas, S.A. due to the change in the contribution to the consolidated figures of the interest in said company, and Euros 23 million for the shareholding in Unión Fenosa Minería, S.A.

In 2018, following the approval of the new Strategic Plan 2018-2022, impairments of shareholdings in Group companies and associates amounting to Euros 4,565 million have been recognised under “Impairment of and losses from equity instruments of Group companies and associates” in the income statement, arising from the revaluation of future cash flow estimates based on said Plan or by other factors arising in the period, which are detailed as follows:

- Euros 3,401 million for the shareholding in Naturgy Generación, S.L.U.

  Due to the existence of impairment evidence, following the approval of the new Strategic Plan and taking into account external reports by analysts that regularly cover the Naturgy monitoring that indicate a value for the electricity business in Spain which is lower than the relevant carrying value, an impairment analysis has been carried out on the three CGUs that made up the Electricity CGU in Spain in previous years: conventional electricity generation, renewable electricity generation and electricity supply. Impairment was detected only with respect to the conventional electricity generation CGU in Spain.

  The new assumptions and projections that affect these CGUs are based on the new Strategic Plan 2018-2022, approved by the Board of Directors following the last General Shareholders’ Meeting which update those that had been used to date, and have been determined: i) in the light of the new sector variables for the next five-year period, ii) taking into account the uncertainty regarding the role of certain generation assets in the energy transition policy (coal, nuclear and combined cycles) and consequently the development of the associated risks, iii) considering the greater presence forecast in renewables, iv) considering the increasing volatility of prices in the electricity wholesale market and emission allowances and v) assessing the references provided by very recently announced transactions in conventional electricity generation assets in Spain.

  The assumptions taken into consideration are the following:

	2018	2019	2020	2021	2022
Evolution of Spanish GNP	2.70%	2.20%	1.90%	1.70%	1.70%
Pool price €/MWh	58.5	56.8	54.8	51.3	50.3
Brent (USD/bbl)	75.3	75.5	71.0	67.8	65.6
Gas Henry Hub (USD/MMBtu)	2.9	2.8	2.7	2.7	2.7
Coal (API2 CIF ARA) (USD/t)	89.6	88.0	85.2	82.9	81.9
CO_2 €/t	14.0	16.1	16.3	16.6	17.0

  The most sensitive aspects that are included in the new estimate of the recoverable amount determined according to the value in use and applying the methodology detailed in Note 3.3 are the following:

  – Electricity generated. Market demand evolution has been estimated based on the consensus expressed by several international bodies. The share has been estimated based on Naturgy’s market share in each technology and on the expected evolution of each technology’s share of the total market, assuming an average year for hydro generation purposes. The main variation with respect to past projections is a decrease in conventional production in line with the expected future evolution of the conventional generation mix.

- 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. The main variation with respect to the past projections is that, as a result of this analysis, price paths have been obtained which, as a result of the above-mentioned uncertainty over energy policy in Spain, have been adjusted downwards on average with futures curves and analysts' forecasts. The sources used for analysts' forecasts relate to IHS CERA.

- Fuel costs. Estimated by reference to long-term supply contracts concluded by Naturgy, the forecast evolution of price curves and market experience. The main variation with respect to past projections corresponds to an increase in the cost of emission allowances based on the evolution of futures curves and analysts' forecasts (IHS CERA).

- Operation and maintenance costs. Estimated from historical costs of managed park.

- Taxes established by Law 15/2012.

  In addition, a long-term growth rate of 1.9% and a pre-tax discount rate of 7.0% have been used for the conventional electricity generation CGU. The discount rate has been determined specifically for the new CGU based on the risks associated with it in a manner consistent with those considered in the estimates of future cash flows. In 2017 the long-term growth rate for the Electricity Spain CGU was 2.2%, while the pre-tax discount rate applied for said CGU was 6.3%.

The recoverable amount calculated as the value in use of the conventional electricity generation CGU, which is equivalent to its carrying value, was Euros 3,591 million. A sensitivity analysis was carried out independently for each of the following variations in the key assumptions:

- An increase in the discount rate of 50 basis points would increase impairment by Euros 333 million.

- A decrease in the growth rate of 50 basis points would increase impairment by Euros 258 million.

- A decrease in electricity output of 5% would increase impairment by Euros 203 million.

- An increase in fuel costs of 5% would increase impairment by Euros 364 million.

- A decrease in electricity prices of 5% would increase impairment by Euros 528 million.

Accumulated impairment at 31 December 2018 recognised for the holding in Naturgy Generación, S.L.U. amounted to Euros 3,401 million.

- Euros 729 million relates to the impairment of the 50% interest in Unión Fenosa Gas.

  Since 2014, Egyptian Natural Gas Holding (EGAS), an Egyptian public company, ceased to supply gas to Unión Fenosa Gas and stopped paying the utilisation fee for the Damietta liquefaction plant in Egypt. This led Unión Fenosa Gas to file various arbitration petitions, the progress of which is described in Note 27. As a result of impairment already arising prior to 2017, the recoverable value of Unión Fenosa Gas was approximately equivalent to its carrying value and therefore any negative variation in the assumptions meant that the recoverable value would less than the carrying value.

  The most significant matters included in the impairment test are as follows:

  - Gas volumes to be supplied from each supply source. The main causes of the differences between the past and current cash flow projections are the decrease in the volumes of gas to be supplied from Egypt and to liquefying at the plant during the Strategic Plan 2018-2022 because the agreement with EGAS has still not materialised and due to the delays in coming to an agreement with EGAS that would enable the plant to be reactivated and supplies to recommence. Naturgy continues to be confident that the resolution of the arbitration processes will enable a commercial agreement to be reached, enabling the recommencement of gas supplies to the plant as swiftly as possible.

- Gas supply costs. In accordance with the prices of the long-term contracts entered into by Unión Fenosa Gas and expected price fluctuations in spot markets based on the change in the composition of gas volumes affected by the situation in Egypt.

- 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 operates.

A long-term growth rate of 1.9% (1.8% in 2017) and a pre-tax discount rate of 15.1% (13.4% in 2017) have been used.

The accumulated impairment at 31 December 2018 relating to the 50% interest in Unión Fenosa Gas amounts to Euros 2,100 million (Euros 1,371 million at 31 December 2017). At 31 December 2018, the recoverable amount calculated as the value in use of Unión Fenosa Gas, which is equivalent to its carrying value, was Euros 340 million (Note 7). A sensitivity analysis has been carried out for an increase in the discount rate of 50 basis points which would increase impairment by Euros 16 million.

- Euros 140 million relating to the impairment of the shareholding in Naturgy Informática, S.A. for the impairment of computer software, resulting from the review thereof under the new Strategic Plan 2018-2022 and taking obsolescence into account.

  Accumulated impairment at 31 December 2018 recognised for the holding in Naturgy Informática, S.A. amounted to Euros 140 million.

- Euros 70 million for the impairment of the 32.3% holding in Petroleum Oil & Gas España, S.A. due to the lack of feasibility of this company's projects.

  The accumulated impairment at 31 December 2018 recognised for the holding in Petroleum Oil & Gas España, S.A. amounted to Euros 70 million.

  Impairment has also been recognised with respect to the following assets:

- Euros 207 million impairment of the holding in Unión Fenosa Minería, S.A. due to the difference between the carrying value of the interest in the coalfield in South Africa (Kangra Coal (Propietary) LTD) and the price at which it was sold.

  Accumulated impairment at 31 December 2018 recognised for the holding in Unión Fenosa Minería, S.A. amounting to Euros 242 million.

- Euros 18 million other impairment of holdings in group companies, recognised on the basis of its equity.

Information on other impairment tests performed

As regards the remaining CGUs or groups of CGUs that have been allocated goodwill or intangible assets with an indefinite useful life, in 2018 and 2017 the recoverable amounts, calculated according to the methodology described in Note 3.3., have been higher than the carrying values recorded in these annual accounts. The most sensitive aspects that are included in the projections used and which are based on industry forecasts and historical experience are as follows:

- Supply of gas, electricity and services:

  - Supply margin. Projections have been used on the evolution of the number of customers and unitary margins based on existing contracts and the knowledge of the markets in which it operates.

  - In addition, a long-term growth rate of 1.9% and a pre-tax discount rate of 6.8% have been used for this CGU. The discount rate has been determined specifically for the new CGU based on the risks associated with it in a manner consistent with those considered in the estimates of future cash flows. In 2017 the long-term growth rate for the Electricity Spain CGU was 2.2%, while the pre-tax discount rate applied for said CGU was 6.3%.

- Renewable electricity generation:
  - Electricity generated. Projections of hours of operation of each park consistent with their historical output and predictions based on historical records of similar parks have been used when there were no historical data.
  - 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.
  - Remuneration. For facilities with a right to specific remuneration, this has been estimated based on the remuneration parameters for the established regulated income period.
  - Operation and maintenance costs. Estimated from historical costs of managed park.
  - Taxes established by Law 15/2012.
  - In addition, a long-term growth rate of 1.9% and a pre-tax discount rate of 6.1% have been used for this CGU. The discount rate has been determined specifically for the new CGU based on the risks associated with it in a manner consistent with those considered in the estimates of future cash flows. In 2017 the long-term growth rate for the Electricity Spain CGU was 2.2%, while the pre-tax discount rate applied for said CGU was 6.3%.
- International Electricity Generation:
  - Operation and maintenance costs. Estimated on the basis of historical costs.
  - International electricity generation is managed under energy sale-purchase contracts through stable business models and which are not subject to fluctuation risks on the basis of market variables.
  - In addition, long-term growth rates of 2.1% - 4.0% (2.6% - 4.0 % in 2017) and pre-tax discount rates of 7.9% - 14.8% (6.5% - 12.8%) have been used for these CGUs.
- Electricity distribution Spain:
  - Remuneration. Amount and increase in remuneration approved by the regulator.
  - Operation and maintenance costs. Estimated on the basis of the historical cost of the network managed.
  - Investments. Taking into account the necessary investments to maintain the regular use of the network and quality of supply.
  - In addition, a long-term growth rate of 1.2% (1.2% in 2017) and a pre-tax discount rate of 6.0% (5.2% in 2017) have been used for this CGUs.
- Latin America North and South Infrastructures:
  - Variations in rates. Valuation of rates in each country, based on existing regulatory conditions and rate reviews, taking into account the experience gained from previous rate reviews in each country.
  - Cost of raw materials and consumables. Estimated on the basis of predictive modelling based on an understanding of energy markets in each country.
  - Operation and maintenance costs. Estimated on the basis of the historical cost of the network managed.
  - Investments. Taking into account the necessary investments to maintain the regular use of the network and quality of supply.
  - In addition, long-term growth rates of 1.3% - 3.8% (1.6% - 3.0 % in 2017) and pre-tax discount rates of 9.9% - 17.6% (8.8% - 17.0%) have been used for these CGUs.

The Company has carried out a sensitivity analysis of the unfavourable variations which, drawing on historical experience, may reasonably impact on the aforementioned sensitive parameters on which the recoverable amounts of these remaining CGUs have been determined. Specifically, the most significant sensitivity analyses performed were as follows:

	Increase	Decrease
Discount rate	50 basis points	–
Growth rate	–	50 basis points
Electricity generated	–	5%
Electricity price	–	5%
Fuel supply costs	5%	–
Tariff/remuneration performance	–	5%
Operating and maintenance costs	5%	–
Investments	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 for investments in group companies and associates.

Note 5. Intangible assets

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

	Computer software	Other intangible assets	Subtotal	Goodwill	Total
Cost	6	1	7	815	822
Accumulated amortisation	(2)	–	(2)	(625)	(627)
Carrying value at 1.1.2017	**4**	**1**	**5**	**190**	**195**
Amortisation charge	–	–	–	(81)	(81)
Carrying value at 31.12.2017	**4**	**1**	**5**	**109**	**114**
Cost	6	1	7	815	822
Accumulated amortisation	(2)	–	(2)	(706)	(708)
Carrying value at 1.1.2018	**4**	**1**	**5**	**109**	**114**
Investment	1	–	1	–	1
Amortisation charge	(1)	(1)	(2)	(82)	(84)
Other	1	–	1	–	1
Carrying value at 31.12.2018	**5**	**–**	**5**	**27**	**32**
Cost	6	–	6	815	821
Accumulated amortisation	(1)	–	(1)	(788)	(789)
Carrying value at 31.12.2018	**5**	**–**	**5**	**27**	**32**

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 Naturgy Group.

At 31 December 2018 intangible assets do not include fully amortised assets still in use (Euros 2 million at 31 December 2017).

In 2018 there have been disposals of fully-amortised assets totalling Euros 2 million (Euros 4 million at 31 December 2017).

Note 6. Property, plant and equipment

Set out below is an analysis showing movements in Property, plant and equipment during 2018 and 2017:

	Land and buildings	**Other property, plant and equipment**	**Total**
Cost	201	33	234
Accumulated depreciation	(61)	(20)	(81)
Carrying value at 1.1.2017	**140**	**13**	**153**
Investment	12	4	16
Divestment	(8)	–	(8)
Depreciation charge	(7)	(3)	(10)
Reclassifications and transfers	(3)	3	–
Carrying value at 31.12.2017	**134**	**17**	**151**
Cost	197	40	237
Accumulated depreciation	(63)	(23)	(86)
Carrying value at 1.1.2018	**134**	**17**	**151**
Investment	7	1	8
Divestment	(4)	–	(4)
Depreciation charge	(11)	(3)	(14)
Other	1	(1)	–
Carrying value at 31.12.2018	**127**	**14**	**141**
Cost	197	37	234
Accumulated depreciation	(70)	(23)	(93)
Carrying value at 31.12.2018	**127**	**14**	**141**

In May 2018 the Company sold the building located in la avenida Balears, Valencia, for Euros 5 million, generating a capital gain before income tax of Euros 1 million.

In November 2017 the Company sold the building located in calle Lérida, Madrid, for Euros 12 million, generating a capital gain before income tax of Euros 3 million. In addition, an operating lease without a purchase option was concluded with the acquiring company for a period of ten years which may be extended for a further five-year period. At the date of the transaction, the remaining useful life of the property transferred was considerably greater than the maximum lease period.

In 2018 there have been disposals of fully-amortised assets totalling Euros 4 million (Euros 4 million at 31 December 2017).

Property, plant and equipment include fully-depreciated assets still in use totalling Euros 13 million at 31 December 2018 (Euros 15 million in 2017).

It is the Company's policy to take out insurance where deemed necessary to cover risks that could affect its property, plant and equipment.

At 31 December 2018 and 31 December 2017, the Company had no investment commitments.

Note 7. Investments in group companies and associates

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

	At 31.12.18	At 31.12.17
Equity instruments	15,237	13,400
Loans	15,657	15,615
Non-current	**30,894**	**29,015**
Loans	740	1,480
Other financial assets	57	743
Current	**797**	**2,223**
TOTAL	**31,691**	**31,238**

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 1.1.2017	**13,677**	**15,755**	**11**	**29,443**
Additions	26	2	–	28
Divestments	(180)	(12)	(1)	(193)
Reclassification	–	(124)	–	(124)
Charge/reversal provisions	(133)	–	–	(133)
Exchange differences	–	(6)	–	(6)
Balance at 31.12.2017	**13,390**	**15,615**	**10**	**29,015**
Additions	11,437	6,743	–	18,180
Divestments	(5,035)	(1,475)	–	(6,510)
Reclassification	–	(5,218)	–	(5,218)
Charge/reversal provisions	(4,565)	–	–	(4,565)
Exchange differences	–	(8)	–	(8)
Balance at 31.12.2018	**15,227**	**15,657**	**10**	**30,894**

2018

- On 3 August 2017 the Company entered into an agreement with a consortium formed by Allianz Capital Partners and Canada Pension Plan Investment Board to sell a 20% interest in the natural gas distribution business in Spain for an amount of Euros 1,500 million, after increasing the level of debt through long-term intra-group financing on Naturgy's part amounting to Euros 6,000 million. The completion of the operation was subject to the obtainment of the relevant regulatory and competition authorisations.

  To carry out the operation, Holding de Negocios de Gas, S.A., a company wholly owned by the Company, has become the head of the natural gas distribution and transport activity and the liquefied petroleum natural gas distribution activity in Spain, carrying out the following operations:

  - On 7 February 2018, Holding de Negocios de Gas, S.A. increased capital through the issue of 15,000 new shares with a par value of Euro 1 each and a share premium of Euros 499,999 per share. These new shares have been fully subscribed and paid by the Company for a total amount of Euros 7,500 million.

  - On 7 February 2018 the Company granted an intragroup loan of Euros 6,000 million to Holding de Negocios de Gas, S.A. This loan matures between 7 and 12 years and bears interest at a market rate.

- On 7 February 2018, using the funds received, Holding de Negocios de Gas, S.A. acquired 100% of the shares in Nedgia ,S.A. (formerly called Holding Negocios Regulados Gas Natural, S.A. and which is the holding company of the Spanish gas distribution companies) from the Company for Euros 11,518 million, an amount that has been determined as the fair value based on the same price per share set in said sale agreement with the Consortium and which has been confirmed by the fairness opinion of the investment banks J.P. Morgan and Morgan Stanley which have acted as financial advisors in this operation and which have concluded that the value is reasonable from a financial viewpoint. In accordance with the provisions of paragraph 1 of Recognition and Valuation Standard 21 of the Spanish Chart of Accounts, the transaction has been accounted for at fair value and has generated a profit of Euros 9,537 million. The Company has also cancelled the loans it had granted to the Spanish gas distribution companies amounting to Euros 1,981 million, while the company Holding de Negocios de Gas, S.A. has granted said financing for the same amount to the Spanish gas distribution companies.

- On 14 February 2018 Holding Negocios de Gas, S.A. acquired from Nedgia, S.A. 100% of the shares in Gas Natural Transporte SDG, S.L. and in Gas Natural Redes GLP, S.A. for Euros 165 million. This figure was determined as the fair value based on the price set in the above-mentioned sale agreement with the Consortium, following the payment by Nedgia, S.A. of dividends amounting to Euros 165 million by charge to the share premium.

On March 19, the Company, after obtaining the necessary regulatory and competition approvals, transferred 20% of the interest in Holding de Negocios de Gas, S.A. to said Consortium for an amount of Euros 1,500 million in cash, without any significant impact on the income statement as the shareholding was recorded at fair value.

- Capital reduction through the reimbursement of contributions in Clover Financial and Treasury Services, D.A.C. in the amount of USD 667 million (Euros 609 million). The reduction in the shareholding has generated a Euros 73 million profit due to the exchange rate effect.

- Subscription of a capital increase through a monetary contribution in Naturgy Participaciones, S.A.U. for Euros 100 million.

- Creation and subscription of a capital increase in Naturgy Infraestructuras EMEA, S.L. in the amount of Euros 88 million.

- The distributions of reserves by Global Power Generation, S.A. and Holding de Negocios de Gas, S.A. amounting to Euros 110 million and Euros 885 million, respectively, have been recorded as a decrease in the carrying value of the shareholdings.

- Sale of 98.48% of the holding in Compañía Española de Industrias Electroquímicas, S.A. for Euros 8 million, generating a capital gain before tax of Euros 3 million.

- Sale of the holding in La Propagadora del Gas, S.A. to the group company Naturgy Generación, S.L.U. for Euros 11 million, generating a capital gain before tax of Euros 1 million.

- Euros 14 million monetary contribution to offset losses to Comercializadora Regulada Gas & Power, S.A.

- Euros 136 million monetary contribution to offset losses to Naturgy Informática, S.A.

- Euros 67 million monetary contribution to offset losses to Naturgy Aprovisionamientos, S.A.

- Euros 32 million monetary contribution to offset losses to Petroleum Oil & Gas España, S.A.

- Subscription of a capital increase by Naturgy Generación, S.L.U. of Euros 3,500 million through the capitalisation of a loan.

2017

The most significant movements in the item "Shareholdings in Group companies and associates" in 2017 relate to:

- Capital contribution to offset losses in Comercializadora Regulada Gas and Power, S.A. in the amount of Euros 26 million.
- Capital reduction through the reimbursement of contributions in Clover Financial and Treasury Services, D.A.C. in the amount of USD 75 million (Euros 69 million). The reduction in the shareholding has generated a Euros 7 million profit due to the effect of the exchange rate.
- Decrease in the carrying amount of the holding due to the distribution of reserves by Global Power Generation, S.A. in the amount of Euros 17 million.

The cumulative provision for the impairment of shareholdings in Group companies and associates totals Euros 6,185 million at 31 December 2018 (Euros 1,620 million at 31 December 2017), relating basically to the following companies (Note 4):

	2018	2017	Change
Naturgy Generación, S.L.U.	3,401	–	3,401
Unión Fenosa Gas, S.A.	2,100	1,371	729
Unión Fenosa Minería, S.A.	242	35	207
Petroleum Oil & Gas España, S.A.	70	–	70
Gas Natural Exploración, S.L.	213	213	–
Naturgy Informática, S.A.	140	–	140
Other	19	1	18
Total	**6,185**	**1,620**	**4,565**

Financial income for dividends received from investments in equity instruments of group companies and associates during the years 2018 and 2017, correspond to the following companies:

	2018	2017
UFD Distribución Electricidad, S.A.	238	133
Holding Negocios Gas, S.A.	173	–
Clover Financial and Treasury Services, D.A.C.	32	40
Global Power Generation, S.A.	30	41
Naturgy Aprovisionamientos, S.A	24	155
Naturgy Distribución Latinoamérica, S.A.	23	178
General de Edificios y Solares, S.L.	11	19
Naturgy Capital Markets, S.A.	6	8
Naturgy Finance, B.V.	3	–
Sagane, S.A.	2	335
Unión Fenosa Minería, S.A.	2	–
Gas Natural Almacenamientos Andalucía, S.A.	1	1
Compañía Española de Industrias Electroquímicas, S.A.	1	1
Naturgy Iberia, S.A.	–	179
Nedgia, S.A.	–	156
Gas Natural Comercializadora, S.A.	–	134
Naturgy Inversiones Internacionales, S.A.	–	88
Naturgy Engineering, S.L.	–	1
Other	1	1
Total	**547**	**1,470**

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

Figures at 31 December 2018

					% interest			Equity				
Company	**Registered Office**	**Activity**	**Carrying value 2018**	**Carrying value 2017**	**Direct**	**Indi-rect**	**Total**	**Capital**	**Reserves (1)**	**Profit/ (loss)**	**Interim dividend**	**Other (2)**
Naturgy Aprovisionamientos, S.A.	Spain	Gas marketing	85	18	100.0	–	100.0	1	86	(71)	–	(3)
Naturgy LNG, S.L.	Spain	Gas marketing	2	2	100.0	–	100.0	2	–	–	–	–
Sagane, S.A.	Spain	Gas marketing	42	42	100.0	–	100.0	95	22	240	–	2
Unión Fenosa Gas, S.A.	Spain	Gas marketing	340	1,065	50.0	–	50.0	33	459	(20)	–	–
Gas Natural Comercializadora, S.A.	Spain	Gas and electricity marketing	121	121	100.0	–	100.0	3	85	(2)	–	(28)
Comercializadora Regulada Gas & Power, S.A.	Spain	Gas and electricity marketing	84	70	100.0	–	100.0	2	19	(13)	–	–
La Energía, S.A.	Spain	Gas and electricity marketing	11	11	100.0	–	100.0	11	5	–	–	–
Naturgy Iberia, S.A.	Spain	Gas and electricity marketing	106	106	100.0	–	100.0	3	51	59	–	1
UFD Distribución Electricidad, S.A.	Spain	Electricity distribution	1,630	1,630	100.0	–	100.0	833	233	152	–	359
Holding de Negocios de Gas, S.A.	Spain	Gas distribution	5,115	–	80.0	–	80.0	–	6,177	728	–	–
Nedgia S.A.	Spain	Gas distribution	–	1,981	–	80.0	80.0	–	–	–	–	–
Naturgy Generación, S.L.U.	Spain	Electricity generation	3,996	3,897	100.0	–	100.0	1,052	3,824	(2,075)	–	4
Naturgy Renovables, S.L.U.	Spain	Electricity generation	397	397	100.0	–	100.0	90	131	39	–	–
Global Power Generation, S.A.	Spain	Electricity generation	1,401	1,514	75.0	–	75.0	20	1,667	40	–	13
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	–	–
Naturgy Almacenamientos Andalucía S.A.	Spain	Gas infrastructures	8	8	100.0	–	100.0	–	8	–	–	–
Gas Natural Exploración, S.L.	Spain	Gas infrastructures	9	9	100.0	–	100.0	8	11	–	–	(11)
Petroleum Oil & Gas España, S.A.	Spain	Gas infrastructures	4	41	32.3	67.7	100.0	4	117	(109)	–	–
Natural Re, S.A.	Luxembourg	Insurance	9	9	100.0	–	100.0	5	52	1	–	–
Compañía Española de Industrias Electroquímicas, S.A.	Spain	Services	–	4	–	–	–	–	–	–	–	–
General de Edificios y Solares, S.L.	Spain	Services	63	63	100.0	–	100.0	34	35	(5)	–	–
Clover Financial and Treasury Services, D.A.C.	Ireland	Financial services	–	542	100.0	–	100.0	–	(24)	24	–	–
Naturgy Capital Markets, S.A.	Spain	Financial services	–	–	100.0	–	100.0	–	–	4	–	–
Naturgy Finance, B.V.	Netherlands	Financial services	7	7	100.0	–	100.0	–	9	(40)	–	57
Naturgy Participaciones, S.A.	Spain	Financial services	96	11	100.0	–	100.0	–	100	(4)	–	–
Unión Fenosa Preferentes, S.A.U.	Spain	Financial services	–	–	100.0	–	100.0	–	1	1	–	110
Naturgy Informática, S.A.	Spain	IT services	16	20	100.0	–	100.0	20	143	(149)	–	–
Naturgy Engineering, S.L.	Spain	Engineering services	20	24	100.0	–	100.0	–	18	1	–	–
Naturgy Distribución Latinoamérica, S.A.	Spain	Holding company	558	558	100.0	–	100.0	402	237	166	–	–
La Propagadora del Gas, S.A.	Spain	Holding company	–	10	100.0	–	100.0	–	–	–	–	–
Naturgy Gas and Power, S.L.U.	Spain	Holding company	–	–	100.0	–	100.0	–	–	–	–	–
Naturgy Infraestructuras EMEA, S.L.	Spain	Holding company	88	–	100.0	–	100.0	–	88	2	–	–
Naturgy Inversiones Internacionales, S.A.	Spain	Holding company	944	944	100.0	–	100.0	250	336	118	–	(117)
Unión Fenosa Minería, S.A.	Spain	Holding company	75	286	100.0	–	100.0	11	169	(105)	–	–
TOTAL			**15,227**	**13,390**								

Appendix I to Naturgy's consolidated annual accounts provides a breakdown of other indirect shareholdings.
1. Includes the share premium, reserves, prior-year losses, contributions 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 2018 total Euros 15,657 million mature in 2019 (at 31 December 2017, Euros 15,615 million maturing in 2018).

Set out below are movements during 2018 and 2017 in loans and other current financial assets:

	Loans to group companies	Other financial assets	Total
Balance at 1.1.2017	**816**	**67**	**883**
Additions	882	740	1,622
Divestments	(594)	(64)	(658)
Reclassifications	376	–	376
Balance at 31.12.2017	**1,480**	**743**	**2,223**
Additions	261	53	314
Divestments	(5,031)	(739)	(5,770)
Reclassifications and transfers	4,024	–	4,024
Exchange differences	6	–	6
Balance at 31.12.2018	**740**	**57**	**797**

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

The heading “Loans to group companies” includes loans to Group companies amounting to Euros 313 million (Euros 962 million in 2017) and cash pooling balances with investee companies, as manager of the Group’s centralised cash system amounting to Euros 371 million (Euros 481 million in 2017). It also includes accrued unmatured interest of Euros 56 million (Euros 37 million in 2017).

At 31 December 2018, loans to Group companies and associates have borne interest at a rate of 2.81% (2.66% in 2017) in the case of non-current amounts, and 1.00% (1.00% in 2017) in the case of current amounts.

Dividends pending collection at 31 December 2018 amounted to Euros 53 million, recorded under “Other current financial assets” (Euros 739 million at 31 December 2017).

Note 8. Investments

The breakdown of investments by category is as follows:

At 31 December 2018	Available-for-sale financial assets	Loans and receivables	Assets at fair value through profit or loss	Hedging derivatives	Total
Equity instruments	5	–	–	–	5
Other financial assets	–	12	–	–	12
Non-current investments	**5**	**12**	**–**	**–**	**17**
Derivatives (Note 14)	–	–	6	2	8
Other financial assets	–	36	–	–	36
Current investments	**–**	**36**	**6**	**2**	**44**
Total	**5**	**48**	**6**	**2**	**61**

At 31 December 2017	Available-for-sale financial assets	Loans and receivables	Assets at fair value through profit or loss	Hedging derivatives	Total
Equity instruments	5	–	–	–	5
Derivatives (Note 14)	–	–	–	8	8
Other financial assets	–	27	–	–	27
Non-current investments	**5**	**27**	**–**	**8**	**40**
Derivatives (Note 14)	–	–	43	13	56
Other financial assets	–	29	–	–	29
Current investments	**–**	**29**	**43**	**13**	**85**
Total	**5**	**56**	**43**	**21**	**125**

Available-for-sale financial assets

All available-for-sale financial assets relate to unlisted shareholdings at 31 December 2018 and 31 December 2017.

Loans and receivables

The breakdown of Loans and other receivables is as follows:

	At 31.12.18	At 31.12.17
Loans to companies	–	2
Gas system income deficit financing	7	19
Deposits and guarantee deposits	5	6
Non-current	**12**	**27**
Gas system income deficit financing	2	–
Deposits and guarantee deposits	34	29
Current	**36**	**29**
Total	**48**	**56**

Other financial assets

The heading “Gas system revenue deficit financing” includes temporary mismatches between gas system revenues and costs accumulated in 2017, funded by Naturgy pursuant to Law 18/2014 of 17 October. This amount was acquired by the Company in 2017 from the distribution companies of Naturgy and will be recovered through gas system settlements as the right to the recovery of this amount is generated in the following five years, recognising a market interest rate. The amount of this financing has been recognised based on the estimated recovery period. In December 2017 the irrevocable assignment without recourse of the 2014 deficit and the mismatches for 2015 and 2016 to various financial institutions took place, transferring all associated risks and rewards. All the balances at the date of the assignment were therefore derecognised.

Following successive settlements in 2017, the final settlement for 2017 was received on 28 November 2018. The deficit in the gas sector has evolved favourably and the amount of the acquisition made from the distribution companies corresponding to the mismatch in 2017 has been adjusted by Euros 9 million.

Note 9. Trade and other receivables

The breakdown of this account is as follows:

	At 31.12.18	At 31.12.17
Trade receivables	130	145
Trade receivables, group companies and associates	366	345
Sundry receivables	23	38
Provision	(29)	(24)
Derivatives (Note 14)	106	117
Current income tax asset	65	29
Total	**661**	**650**

In general, amounts billed pending collection do not bear interest, being the average maturity period less than 21 days.

Movements in the bad debt provision are as follows:

	2018	2017
At 1 January	**(24)**	**(24)**
Net charge for the year (Note 21)	(5)	–
At 31 December	**(29)**	**(24)**

Note 10. Cash and cash equivalents

Cash and cash equivalents include:

	At 31.12.18	At 31.12.17
Cash at banks and in hand	722	1,453
Other cash equivalents	–	100
Total	**722**	**1,553**

At 31 December 2017, investments in Cash equivalents matured in less than three months at a weighted effective interest rate of 0.073%.

Note 11. Equity

The main items of Equity are as follows:

Share capital and share premium

The variations during the years 2018 and 2017 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 2017	**1,000,689,341**	**1,001**	**3,808**	**4,809**
Changes:	–	–	–	–
At 31 December 2017	**1,000,689,341**	**1,001**	**3,808**	**4,809**
Changes:	–	–	–	–
At 31 December 2018	**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 Company's Board of Directors, which for these purposes may be substituted by the Executive Committee, for a maximum term of five years as from 20 April 2017, is empowered to increase share capital by Euros 500,344,670 through one or more cash payments at the time and in the amount that it deems fit, issuing ordinary, privileged or redeemable shares with or without voting rights, with or without a share premium, without requiring any further authorisation from the shareholders, with the possibility of agreeing, as appropriate, the full or partial exclusion of preferential subscription rights up to a limit of 20% of share capital at the date of this authorisation, and to alter the By-laws as required due to the capital increase or increases performed by virtue of said authorisation, with provision for an incomplete subscription, in accordance with the provisions of Article 297.1.b) of the Spanish Capital Companies Act.

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

The most relevant holdings in the Company's share capital at 31 December 2018 and 2017, in accordance with publicly information available or the communication issued by the Company itself, are as follows:

	% interest in share capital	
	2018	**2017**
- Fundación Bancaria Caixa d'Estalvis i Pensions de Barcelona, "la Caixa" [1]	25.6	24.4
- Repsol, S.A.	–	20.1
- Global Infrastructure Partners III [2]	20.0	20.0
- Rioja Bidco Shareholdings, S.L.U. [3]	20.1	–
- Sonatrach	3.9	4.0

1. 20.4% direct holding through Criteria Caixa S.A.U. and 5.2% indirect (holding 5.0% through Energía Boreal 2018, S.A. and 0.2% through other).
2. Global Infrastructure Partners III, whose investment manager is Global Infrastructure Management LLC, holds its interest indirectly through GIP III Canary 1, S.à.r.l.
3. Company controlled by funds advised by CVC.

On 22 February 2018 Repsol, S.A. concluded an agreement with Rioja Bidco Shareholdings, S.L.U., a company controlled by funds advised by CVC, for the sale of 20.072% of the capital of Naturgy Energy Group, S.A. On 18 May 2018 the transaction was completed and Repsol, S.A. ceased to be the owner of said company.

All the Company's shares are traded on the four official Spanish Stock Exchanges and the "Mercado continuo" and form part of Spain's Ibex 35 stock index.

The Company's share price at 31 December 2018 was Euros 22.26 (Euros 19.25 at 31 December 2017).

Reserves

Reserves includes the following:

	2018	**2017**
Legal reserve	200	200
Statutory reserve	100	100
Goodwill reserve	109	191
Voluntary reserves	7,305	7,200
Other reserves	295	280
Total	**8,009**	**7,971**

At the annual general meeting held on 27 June 2018, the shareholders agreed to the transfer to Voluntary Reserves of Euros 82 million from the Goodwill Reserve.

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 Company's Articles of Association, 2% of net profit for the year must be allocated to the statutory reserves until it reaches at least 10% of share capital.

Goodwill reserve

Law 22/2015 on Auditing 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 commencing 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.

Voluntary and other reserves

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 Naturgy's Consolidated annual accounts.

Share-based payments

Within the framework of the new Strategic Plan 2018-2022 the Board of Directors, at meeting held on 31 July 2018, approved a long term variable incentive plan involving the Executive Chairman and 25 other executives. The main characteristics of the plan are as follows:

- The incentive covers the duration of the Strategic Plan 2018-2022, and the incentive plan is scheduled to expire in July 2023. It is directly related to the total yield obtained by the shareholders of Naturgy Energy Group S.A. in the period concerned.
- It is arranged through the acquisition of 8,639,595 shares in Naturgy Energy Group S.A. at a average price of Euros 23.15 (see Treasury Shares section) through a 100% company owned by the Company. It has been endowed with resources through a Naturgy Energy Group, S.A. contribution and external bank financing with which it has acquired the aforementioned shares.
- At the finalisation of the plan this vehicle will obtain income derived from the receipt of the dividends attributed to its shares and the payment of financial costs incurred in their acquisition. At that time it will sell the shares required to return all the resources received for the acquisition of the shares and after settling all its obligations it will distribute any surplus among its members in the form of shares.
- The surplus will be received only if a minimum profitability threshold has been surpassed, considering a price of Euros 19.15 and assuming that all the dividends foreseen in the Strategic Plan 2018-2022 are distributed.
- If they leave the Company, the beneficiaries will only be entitled, in certain cases, to receive a part of the final incentive calculated in proportion to their length of service in the Company with respect to the duration of the plan.

The fair value of the equity instruments granted has been determined at the grant date using a Monte Carlo simulation valuation model with the following assumptions:

Share price on the grant date (euro/share)	23.15
Forecast share price volatility [1]	17.73%
Plan duration (years)	5
Expected dividends	6.26%
Risk-free interest rate	0.34%

1. Forecast volatility has been determined based on the historical volatility of the daily share price in the last year.

As a result of the time apportionment of the fair value estimate of the equity instruments granted over the term of the plan, an amount of Euros 4 million has been recorded in the income statement for 2018 under Personnel expenses, credited to "Other equity instruments" in the balance sheet at 31 December 2018.

Treasury shares

Movements during 2018 and 2017 involving the Company's treasury shares are as follows:

	Number of shares	In million euro	% Capital
At 31 December 2016	**750,545**	**13**	**0.1**
Acquisitions	7,623,586	147	0.8
Share Acquisition Plan	(336,625)	(7)	(0.1)
Disposals	(8,037,506)	(153)	(0.8)
At 31 December 2017	**–**	**–**	**–**
Acquisitions	19,421,635	427	1.9
Share Acquisition Plan	(354,422)	(7)	–
Disposals	(13,669,476)	(299)	(1.4)
At 31 December 2018	**5,397,737**	**121**	**0.5**

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 accordance with the resolutions adopted by the Naturgy Energy Group, S.A. shareholders at the General Meeting held on 20 April 2017, the resolutions relating to FY 2017 and 2018 within the Share Acquisition Plan 2017-2018-2019, aimed at Naturgy employees in Spain who decide voluntarily to take part in the Plan, was set in motion. The Plan enables participants to receive part of their remuneration in the form of shares of Naturgy Energy Group, S.A. subject to an annual limit of Euros 12,000. During 2018, 354,422 of the Company's own shares were acquired for Euros 7 million to be handed over to the employees taking part in the Plan (336,625 own shares amounting to Euros 7 million during 2017).

In 2018 the profit on transactions involving Naturgy treasury shares amounted to a loss of Euros 0.4 million, recognised under "Other reserves" (Euros 0.5 million profit in 2017).

During 2018 the Company acquired 8,639,595 treasury shares at an average price of Euros 23.15 per share for a total of Euros 200 million, the objective of which is to cover the potential delivery of shares derived from the increase in the value of the shares involved in the long-term variable incentive plan.

Within the Strategic Plan 2018-2022, The Board of Directors of Naturgy Energy Group, S.A. approved a treasury shares buy-back programme, which was published on 6 December 2018, with a maximum investment of Euros 400 million to 30 June 2019, representing approximately 1.8% of share capital, which may be redeemed if such is decided by the shareholders at the annual general meeting to be held in the first half of 2019. At 31 December 2018, a total of 5,397,737 treasury shares had been acquired under this programme at an average price of Euros 22.42 per share, representing a total cost of Euros 121 million.

At a meeting held on 29 January 2019, the Board of Directors of Naturgy Energy Group, S.A. agreed to propose to the general shareholders' meeting a capital reduction in Naturgy Energy Group, S.A. in the amount resulting from the sum of:

a) Euros 3 million through the redemption of 2,998,622 treasury shares with a par value of Euro 1 each which had been acquired at the close of trading on 6 December 2018.

b) the aggregate par valued, up to a maximum of Euros 16 million, of the 16,000,000 additional shares with a par value of one euro each which, where applicable, are acquired for redemption by the Company under the treasury share buyback programme approved by the Company under Regulation (EU) No. 596/2014 on market abuse and disclosed as price-sensitive information on 6 December 2018.

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 31.12.18	At 31.12.17
Profit for the year	5,282	1,023
Weighted average number of ordinary shares in issue	997,663,816	1,000,478,210
Earnings per share (in Euros):		
– Basic	5.29	1.02
– Diluted	5.29	1.02

The average weighted number of ordinary shares used in the calculation of earnings per share in 2018 and 2017 is as follows:

	2018	2017
Weighted average number of ordinary shares	1,000,689,341	1,000,689,341
Weighted average number of treasury shares	(3,025,525)	(211,131)
Weighted average number of shares in issue	997,663,816	1,000,478,210

The basic earnings per share coincide with the diluted ones, since there were no instruments that could be converted into ordinary shares during those years and at the end of the year 2018 the conditions to consider the actions corresponding to the incentive described in the section "Share-based payments" in the calculation of diluted earnings were not met.

Dividends

Set out below is a breakdown of the payments of dividends made in 2018 and 2017:

	2018			2017		
	% of Nominal	Euros per share	Amount	% of Nominal	Euros per share	Amount
Ordinary shares	100%	1.40	1,400	100%	1.00	1,001
Other shares (without voting rights, redeemable, etc.)	–	–	–	–	–	–
Total dividends paid	**100%**	**1.40**	**1,400**	**100%**	**1.00**	**1,001**
a) Dividends charged to income statement	100%	1.40	1,400	100%	1.00	1,001
b) Dividends charged to reserves or share premium account	–	–	–	–	–	–
c) Dividends in kind	–	–	–	–	–	–

2018

The Annual General Meeting held on 27 June 2018 approved the payment of a supplementary dividend of Euros 0.670 per share for a total amount of Euros 670 million, which was paid in full in cash on 05 July 2018.

On 24 July 2018, the Company's Board of Directors resolved to pay an interim dividend of Euros 0.28 per share out of 2018 results, for a total of Euros 280 million, which was paid on 31 July 2018.

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 30 June 2018 is as follows:

Profit after tax	5,597
Reserves to be replenished	–
Maximum amount distributable	5,597
Forecast interim dividend payment	280
Cash resources	2,564
Undrawn credit facilities	6,555
Total liquidity	9,119

On 31 October 2018, the Company's Board of Directors resolved to pay an interim dividend of Euros 0.45 per share out of 2018 results for a total of Euros 450 million, which was paid on 27 November 2018 with respect to the outstanding shares at that date.

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 30 September 2018 is as follows:

Profit after tax	5,542
Reserves to be replenished	–
Maximum amount distributable	5,542
Interim dividend 2018 profits	280
Forecast interim dividend payment	450
Cash resources	757
Undrawn credit facilities	6,551
Total liquidity	7,308

On 29 January 2019, the Board of Directors approved the following proposal for the distribution of the Company's net profit for 2018, for submission to the Annual General Meeting:

AVAILABLE FOR DISTRIBUTION

Available for distribution 5,282

***DISTRIBUTION*:**

TO DIVIDENDS: the gross aggregate amount shall be equal to the sum of the following quantities:

(i) Euros 730 million relating to the two interim dividends for 2018 paid by Naturgy Energy Group, S.A., equivalent jointly to Euros 0.73 per share by the number of shares that were not direct treasury shares on the relevant dates; and

(ii) the amount obtained by multiplying Euros 0.57 per share by the number of shares that are not direct treasury shares on the date on which the registered shareholders entitled to receive the complementary dividend are determined.

The supplementary dividend will be paid through entities participating in Sociedad de Gestión de los Sistemas de Registro, Compensación y Liquidación de Valores, S.A.U. (Iberclear), and the Board of Directors is expressly empowered to delegate its powers to the director(s) it deems so that they may perform all the actions required to carry out the distribution and, in particular, without limitation, so that they may (i) set the date on which the shareholders entitled to receive the dividend are determined and the date of payment; (ii) determine the definitive amount of the supplementary dividend, and (ii) designate the entity that is to act as payment agent.

TO VOLUNTARY RESERVES: Determinable amount obtained by subtracting the dividend amount from the distribution base.

Total distributed 5,282

This proposal for the distribution of profits prepared by the Board for approval by the Annual General Meeting includes as supplementary payment of Euros 0.57 per share for each qualifying share outstanding at the proposed date of payment, 20 March 2019. In this respect, in the event that at the time of distribution of the third and last payment of the proposed 2018 dividend (Euros 0.57 per share) the same number of treasury shares is maintained as at the 2018 year end (5,397,737 shares excluding shares covering the LTI, see section on Treasury shares), the amount applied to voluntary reserves would be Euros 3,985 million.

2017

The General Shareholders Meeting held on 20 April 2017 approved payment of a complementary dividend of Euros 0.670 per share for a total of Euros 671 million, paid on 27 June 2017.

The Company's Board of Directors approved on 25 July 2017 payment of a interim dividend for 2017 of Euros 0.330 per share, for a total of Euros 330 million, which was paid on 27 September 2017.

Note 12. Provisions

The breakdown of provisions at 31 December 2018 and 2017 is as follows:

	At 31.12.18	At 31.12.17
Provisions for employee obligations	256	272
Other provisions	222	193
Non-current provisions	**478**	**465**

Provisions for employee obligations

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

	2018			2017		
	Pensions and other similar obligations	Other obligations with personnel	Total	Pensions and other similar obligations	Other obligations with personnel	Total
At 1 January	**262**	**10**	**272**	**275**	**10**	**285**
Appropriations/reversals charged to income statement	7	(1)	6	6	6	12
Payments during the year	(16)	–	(16)	(18)	–	(18)
Changes recognised directly in equity	(21)	–	(21)	(8)	–	(8)
Transfers and other applications	18	(3)	15	7	(6)	1
At 31 December	**250**	**6**	**256**	**262**	**10**	**272**

Pensions and other similar liabilities

Most of the Company's post-employment obligations consist of the contribution of defined amounts to occupational pension plan systems. Nevertheless, at 31 December 2018 and 31 December 2017, the Company held the following defined benefit obligations for certain groups of workers:

- Pensions to retired workers, the disabled, widows and 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	**2018**	**2017**
At 1 January	995	1,080
Service cost for the year	2	2
Interest cost	16	13
Changes recognised directly in equity	(42)	(36)
Benefits paid	(66)	(71)
Transfers and other	22	7
At 31 December	**927**	**995**
Fair value of plan assets		
At 1 January	733	805
Expected yield	11	9
Contributions	4	7
Changes recognised directly in equity	(21)	(28)
Benefits paid	(54)	(60)
Transfers and other	4	–
At 31 December	**677**	**733**
Provisions for pensions and similar obligations	**250**	**262**

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

	2018	**2017**
Service cost for the year	2	2
Interest cost	5	13
Expected return on plan assets	–	(9)
Total charge to the income statement	**7**	**6**

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

	2018	**2017**
1 to 5 years	1	1
5 to 10 years	16	22
More than 10 years	233	239
Provisions for pensions and similar obligations	**250**	**262**

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

% of total	2018	2017
Bonds	100%	100 %

Cumulative actuarial gains and losses, net of the tax effect, recognised directly in equity are positive in the amount of Euros 18 million in 2018 (positive in the amount of Euros 3 million in 2017).

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

	2018	2017
Financial assumptions	3	(13)
Experience	(24)	5
At 31 December	**(21)**	**(8)**

Actuarial assumptions applied are as follows:

	At 31.12.18	At 31.12.17
Discount rate (p.a.)	0.3 to 2.39%	0.0 to 2.25%
Expected return on plan assets (p.a.)	0.3 to 2.39%	0.0 to 2.25%
Future salary increases (p.a.)	2.0%	2.0%
Future pension increases (p.a.)	2.0%	2.0%
Inflation rate (annual)	2.0%	2.0%
Mortality table	PERMF 2000	PERMF 2000
Life expectancy:		
Men		
Retired during the year	22.9	22.9
Retiring within 20 years	42.9	42.7
Women		
Retired during the year	27.4	27.4
Retiring within 20 years	48.8	48.6

These assumptions are equally applicable to all the obligations, 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 2018 and 31 December 2017, nor would it cause a relevant variation in the normal, financial costs for future years in relation to that booked in 2018 and 2017.

Other obligations with personnel

Within the framework of the new Strategic Plan 2018-2022, a new long-term incentives plan has been implemented for the executives of Naturgy no included in the plan mentioned in the Note 11, the aim of which is to align the shareholders' interests, the materialization of the Strategic Plan and the executives' multi-year variable remuneration. This programme replaces the previous scheme, called PREMP, and is linked to the total return earned by the shareholders over the duration of the Strategic Plan, generating a collection right once the annual accounts for 2022 have been approved by the General Meeting, which will be collected in cash. At 31 December 2018 the provision for this commitment amounted to Euros 3 million.

At 31 December 2018 a provision has been recorded corresponding to the remuneration programmes 2016-2018 and 2017-2019 in the amount of Euros 6 million (Euros 19 million at 31 December 2017 in relation to the remuneration programmes 2015-2017, 2016-2018 and 2017-2019), of which Euros 3 million is classified as non-current in 2018 (Euros 10 million 2017).

Other non-current provisions

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

	2018	2017
At 1 January	**193**	**182**
– Appropriations [1]	16	2
– Reversals	–	–
Payments	–	(4)
Transfers and other	13	13
At 31 December	**222**	**193**

1. Includes Euros 3 million and Euros 2 million in 2018 and 2017, respectively, relating to the financial update of provisions.

“Non-current provisions” mainly includes provisions posted to cover obligations deriving mainly from tax claims (Note 17), litigation and arbitration, and other liabilities.

No provision for onerous contracts was deemed necessary at 31 December 2018 or 2017.

At 31 December 2018, the estimated payment dates for these obligations are Euros 21 million between one and five years, Euros 45 million between five and ten years and Euros 156 million more than ten years (2017: Euros 3 million at between one and five years, Euros 49 million at between five and ten years and Euros 141 million at more than 10 years).

Note 13. Borrowings

The breakdown of borrowings at 31 December 2018 and 2017 is as follows:

	At 31.12.18	At 31.12.17
Borrowings from financial institutions	1,985	3,851
Derivatives (Note 14)	54	47
Other financial liabilities	1	14
Non-current borrowings	**2,040**	**3,912**
Borrowings from financial institutions	233	270
Derivatives (Note 14)	9	44
Other financial liabilities	4	14
Current borrowings	**246**	**328**
Total	**2,286**	**4,240**

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

	Carrying amount		Fair value	
	At 31.12.18	At 31.12.17	At 31.12.18	At 31.12.17
Bank borrowings, derivatives and other financial liabilities	2,040	3,912	2,040	3,912

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 2018 and 31 December 2017 on borrowings with similar credit and maturity characteristics.

The movement in borrowings is as follows:

	2018	2017
At 1 January	**4,240**	**3,597**
Increase	135	913
Decrease	(2,089)	(270)
At 31 December	**2,286**	**4,240**

The following tables describe borrowings and maturities at 31 December 2018 and 2017, taking into account the impact of derivative hedges.

	2019	2020	2021	2022	2023	2024 and beyond	Total
At 31 December 2018:							
Fixed	95	115	158	125	91	1,143	1,727
Floating	151	184	90	69	36	29	559
Total	**246**	**299**	**248**	**194**	**127**	**1,172**	**2,286**

	2018	2019	2020	2021	2022	2023 and beyond	Total
At 31 December 2017:							
Fixed	200	261	287	170	137	1,263	2,318
Floating	128	250	722	278	527	17	1,922
Total	**328**	**511**	**1,009**	**448**	**664**	**1,280**	**4,240**

Setting aside the impact of derivatives on borrowings, fixed-rate debt would amount to Euros 95 million of total borrowings at 31 December 2018 (Euros 337 million at 31 December 2017); variable-rate debt would amount to Euros 2,128 million at 31 December 2018 (Euros 3,812 million at 31 December 2017).

The following tables describe the gross borrowings denominated in foreign currencies at 31 December 2018 and at 31 December 2017 and their maturities, taking into account the impact of the derivative hedges:

	2019	2020	2021	2022	2023	2024 and beyond	Total
At 31 December 2018:							
Euro debt	246	299	248	194	127	1,172	2,286
Total	**246**	**299**	**248**	**194**	**127**	**1,172**	**2,286**

	2018	2019	2020	2021	2022	2023 and beyond	Total
At 31 December 2017:							
Euro debt	315	400	746	448	664	1,280	3,853
USD debt	13	111	263	–	–	–	387
Total	**328**	**511**	**1,009**	**448**	**664**	**1,280**	**4,240**

Borrowings bore an average effective interest rate in 2018 of 0.87% (1.31% in 2017) including the derivatives assigned to each transaction.

At 31 December 2018, this includes in bank borrowings Euros 7 million in interest pending payment (Euros 9 million at 31 December 2017).

Most of the drawn-down borrowings include a clause relating to a change in control, the activation of which depends on the simultaneity of some of the following events: the non-permanence of any of the current reference shareholders in a significant percentage; the loss of investment grade status from the Rating Agencies, or the incapacity to meet the financial obligations under the contract.

At the preparation date of these annual accounts, the Company 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.

We set out below the most relevant financial instruments:

Other bank borrowings

At 31 December 2018 there are no bilateral bank loans (Euros 1,645 million at 31 December 2017) and there are no drawn-down credit facilities.

Institutional financing

The Company records balances payable to the Official Credit Institute (ICO) relating to instruments for a total amount of Euros 200 million (Euros 235 million in 2017).

Additionally, financing granted by the European Investment Bank to the Company has been drawn down in the amount of Euros 2,011 million (2017: Euros 2,240 million). These loans could be subject to early repayment in the event of a change of control. This amount is linked to infrastructural financing that requires, in addition to the event of the change of control, a reduction in the rating and have special repayment terms for the debt that are longer than those for early termination cases, amounting to Euros 1,555 million (Euros 1,656 million at 31 December 2017).

Note 14. Risk management and derivative financial instruments

Risk management

Naturgy 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 its risk exposure for Naturgy in its business is in line with the objective risk profile.
- 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 UK voters supported the departure of their country from the European Union (“Brexit”). The referendum has caused significant uncertainty about the future of relations between the United Kingdom and the European Union, including the laws and regulations that will apply since the United Kingdom will determine which European laws it will replicated or replace in the event of its departure. The development of the negotiations has had and may continue to have adverse effects on global economic conditions and the stability of global financial markets.

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.

The Company employs financial swaps to manage exposure to interest rate fluctuations, swapping floating rates for fixed rates.

The financial debt structure at 31 December 2018 and 2017 (Note 13), after taking into account the hedges arranged through derivatives, is as follows:

	At 31.12.18	At 31.12.17
Fixed interest rate	1,727	2,318
Floating interest rate	559	1,922
Total	**2,286**	**4,240**

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

The sensitivity of results and equity (Adjustments for changes in value) to interest rate fluctuations is as follows:

	Increase/decrease in interest rates (basis points)	Effect on profit before tax	Effect on equity before tax
2018	+50	(3)	51
	-50	3	(51)
2017	+50	(10)	131
	-50	10	(131)

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 the Company 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 the Company operates most is the US Dollar. The sensitivity of the Company's profits and consolidated equity ("Adjustments for changes in value") to a 5% variation (increase or decrease) in the US dollar/euro exchange rate is as follows:

		2018	2017
Effect on profit before tax	+5%	–	–
	- 5%	–	–
Effect on equity before tax	+5%	–	–
	- 5%	–	–

Commodity price risk

The Company purchases gas to be supplied to other Group companies.

A large portion of Naturgy's operating expenses are linked to gas purchased to supply customers or generate electricity at combined cycle plants. Therefore, Naturgy is exposed to the variation in commodity prices whose determination is basically subject to crude oil prices and those of its by-products and the prices of natural gas hubs.

The exposure to these risks is managed and mitigated for natural hedge through the monitoring of its position regarding these commodities, seeking to balance purchase and supply obligations, and the 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 CO_2 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 (value change adjustments) to changes in the fair value of derivatives contracted to hedge commodity prices and derivatives used for trading purposes is analysed below:

	Increase / decrease in the electricity sale price	**Effect on profit before tax**	**Effect on equity before tax**
2018	+10%	–	–
	-10%	–	–
2017	+10%	–	–
	-10%	–	–

Naturgy has no relevant investments in upstream businesses or commodities production, therefore a low price scenario in commodities would have no significant impact on asset values.

Business segment 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 are 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 Naturgy's results.

- Gas and electricity. Profit margins on gas and electricity supply activities are directly affected by commodity prices. In this regard, Naturgy 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 formulae, and specific hedging so as to maximise the risk-profit relationship.

Credit risk

Credit risk is defined as the potential loss resulting from the possible nonfulfillment of the contractual obligations of counterparties with which the Group does business.

Naturgy performs solvency analyses on the basis of which credit limits are assigned and any necessary provisions are determined. Based on these models, the probability of customer default can be measured and the expected commercial loss can be kept under control. In addition, credit quality and portfolio exposure are monitored on a recurring basis to ensure that potential losses are within the limits provided for by internal regulations. This allows a certain capacity to anticipate events in credit risk management.

Credit risk relating to trade receivables is reflected in the balance sheet net of provisions for bad debts (Note 9), estimated by the Company on the basis of the ageing of the debt and past experience in accordance with the prior segregation of customer portfolios and the current economic environment.

Credit risk relating to trade accounts receivable is historically limited given the short collection periods of customers that do not individually accumulate significant amounts before supply can be suspended due to non-payment, in accordance with applicable regulations.

With respect to other exposures to counterparties in transactions involving financial derivatives and the investment of cash surpluses, credit risk is mitigated by carrying out such operations with reputable financial institutions whose rating is equal or over “BB”. No significant defaults or losses arose in 2018 or 2017.

The ageing analysis of financial assets concluded that there were no unimpaired, past due financial assets at 31 December 2018 and 2017.

The impaired financial assets are broken down in Note 9.

Concerning supplier credit risk, the solvency of each supplier of products and services is guaranteed through the recurring analysis of their financial information, particularly prior to new engagements. To this end, the relevant assessment criteria are applied depending on the supplier’s criticality in terms of service or concentration. This procedure is supported by control mechanisms and systems and supplier management.

At 31 December 2018 and 2017 the Company did not have significant concentrations of credit risk.

Liquidity risk

The Company 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 2018, available cash totalled Euros 5,756 million (Euros 8,400 million in 2017), including cash and cash equivalents of Euros 722 million (Euros 1,553 million in 2017), undrawn bank financing and credit lines to the amount of Euros 5,034 million (Euros 6,847 million in 2017).

Capital management

The main purpose of the Company’s capital management is to ensure a financial structure that can optimise capital cost and maintain a solid financial position, in order to combine value creation for the shareholder with the access to the financial markets at a competitive cost to cover financing needs.

Naturgy considers the following to be indicators of the objectives set for capital management maintaining a long-term leverage ratio of approximately 50%.

The Company’s long-term credit rating is as follows:

	2018	2017
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 31.12.18		At 31.12.17	
	Assets	**Liabilities**	**Assets**	**Liabilities**
Hedging derivative financial instruments	**–**	**54**	**8**	**47**
Fair value hedge				
– Interest rate and foreign exchange rate	–	–	–	6
Cash flow hedge				
– Interest rate	–	26	8	41
– Interest rate and foreign exchange rate	–	28	–	–
Other financial instruments	**81**	**81**	**–**	**–**
– Interest rate and foreign exchange rate	81	81	–	–
Derivative financial instruments – non current	**81**	**135**	**8**	**47**
Hedging derivative financial instruments	**2**	**10**	**13**	**–**
Fair value hedge				
– Exchange rate	–	–	3	–
Cash flow hedge				
– Interest rate	2	10	1	–
– Exchange rate	–	–	9	–
Other financial instruments	**112**	**117**	**161**	**166**
– Price of commodities	106	117	117	122
– Interest rate and foreign exchange rate	–	–	43	43
– Exchange rate	6	–	1	1
Derivative financial instruments current	**114**	**127**	**174**	**166**
Total	**195**	**262**	**182**	**213**

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

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

	2018		2017	
	Operating profit	**Net financial income/ (expense)**	**Operating profit**	**Net financial income/ (expense)**
Cash flow hedge	–	(6)	–	(4)
Other financial instruments	(1)	(2)	(1)	(2)
Total	**(1)**	**(8)**	**(1)**	**(6)**

The breakdown of derivatives at 31 December 2018 and 2017, their fair value and maturities of their notional values is as follows:

	31.12.18							
	Fair value	Notional value						
		2019	2020	2021	2022	2023	Subsequent years	Total
Interest rate hedges:								
Cash flow hedges:								
Financial swaps (EUR)	(34)	95	844	63	91	91	1,392	2,576
Financial swaps (NOK)	(28)	–	–	–	–	101	–	101
Other:								
Foreign exchange insurance (USD)	6	439	–	–	–	–	–	439
Commodities price derivatives (EUR)	(11)	7	–	–	–	–	–	7
Commodities price derivatives (USD)	–	1	–	–	–	–	–	1
	(67)	**542**	**844**	**63**	**91**	**192**	**1,392**	**3,124**

	31.12.17							
	Fair value	Notional value						
		2018	2019	2020	2021	2022	Subsequent years	Total
Interest rate hedges:								
Cash flow hedges:								
Financial swaps (EUR)	(8)	95	95	844	63	91	2,484	3,672
Financial swaps (USD)	1	228	–	–	–	–	–	228
Financial swaps (NOK)	(25)	–	–	–	–	–	101	101
Exchange rate hedges:								
Cash flow hedges:								
Financial swaps (USD)	9	489	–	–	–	–	–	489
Fair value hedges:								
Financial swaps (USD)	(6)	–	–	–	160	–	–	160
Foreign exchange insurance (USD)	3	193	–	–	–	–	–	193
Other:								
Commodities price derivatives (EUR)	(3)	4	–	–	–	–	–	4
Commodities price derivatives (USD)	(2)	–	–	–	–	–	–	–
	(31)	**1,009**	**95**	**844**	**223**	**91**	**2,585**	**4,847**

Note 15. Payables to Group companies and associates

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

Maturity	At 31.12.18	At 31.12.17
2018	–	3,307
2019	2,283	1,311
2020	932	1,116
2021	1,181	1,417
2022	1,486	1,743
2023	736	872
2024	1,897	1,879
Subsequent years	4,041	3,170
Total	**12,556**	**14,815**

Payables to Group companies correspond, mainly, to the issues made by Naturgy Capital Markets, S.A. and Naturgy Finance, B.V of the medium-term Euro Medium Term Notes program (EMTN). It also includes payables with Naturgy Finance, B.V. for subordinated perpetual debentures amounting to Euros 1,500 million (Euros 1,500 million in 2017) and the payables with Unión Fenosa Preferentes, S.A. for the debt of the preference shares for an amount of Euros 110 million (Euros 110 million in 2017).

It also includes accrued unmatured interest of Euros 217 million (Euros 288 million in 2017) and cash-pooling balances with Group companies amounting to Euros 962 million are also included (Euros 1,642 million in 2017).

A breakdown of amounts owed to Group companies due to bond issues of Naturgy Finance, B.V. and Naturgy Capital Markets, S.A. is as follows:

At 31 December 2018							
Programme/Company	**Country**	**Year formalised**	**Currency**	**Programme limit**	**Drawn-down nominal amount**	**Available**	**Issuances per year**
Euro Commercial Paper (ECP) programme							
Naturgy Finance B.V.	Netherlands	2010	Euros	1,000	-	1,000	6,478
European Medium Term Notes (EMTN) programme							
Gas Natural Capital Markets, S.A. and Naturgy Finance B.V.	Netherlands/ Spain	1999	Euros	15,000	9,707	5,293	850

At 31 December 2017							
Programme/Company	**Country**	**Year formalised**	**Currency**	**Programme limit**	**Drawn-down nominal amount**	**Available**	**Issuances per year**
Euro Commercial Paper (ECP) programme							
Naturgy Finance B.V.	Netherlands	2010	Euros	1,000	-	1,000	4,594
European Medium Term Notes (EMTN) programme							
Gas Natural Capital Markets, S.A. and Naturgy Finance B.V.	Netherlands/ Spain	1999	Euros	15,000	11,205	3,795	2,100

The main movements for the year are:

2018

In January 2018 Naturgy issued bonds under its Euro Medium Term Notes (EMTN) programme for an amount of Euros 850 million maturing in 10 years and with a 1.5% coupon, the proceeds of which were used in a bond buy-back offer for Euros 916 million of debentures maturing between 2019 and 2023, which entailed a net disbursement of Euros 66 million. In the first half of 2018 two bonds have matured for a total amount of Euros 1,099 million and an average coupon of 4.59%.

On 22 October 2018, the company successfully repurchased bonds under its Euro Medium Term Notes (EMTN) programme amounting to Euros 314 million with maturities between 2019 and 2021. Additionally, on 18 December 2018 the repurchase of Euros 19 million of the bond maturing in January 2020 with a coupon of 4.50% was completed.

2017

In April 2017 bonds were issued by Naturgy Capital Markets, S.A. under the EMTN programme for a value of Euros 1,000 million which was used to repurchase debentures amounting to Euros 1,000 million maturing in 2018, 2020 and 2021,therefore not leading to any cash movements.

Most of the drawn-down borrowings include a clause relating to a change in control, the activation of which depends on the simultaneity of some of the following events: the non-permanence of any of the current reference shareholders in a significant percentage; the loss of investment grade status from the Rating Agencies, or the incapacity to meet the financial obligations under the contract.

Specifically, the bonds issued, in a volume of Euros 9,708 million, could be redeemed in advance provided that such a change in control triggers a downgrade of more than two full notches in at least two of the three ratings that it had obtained, and all the ratings fall below investment grade, and provided that the rating agency states that the rating downgrade results from the change in control.

Borrowings from group companies and associates accrued an average interest rate of 2.81% in 2018 (3.51% in 2017).

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

Note 16. Trade and other payables

The breakdown at December 2018 and 2017 is as follows:

	At 31.12.18	At 31.12.17
Trade payables	249	194
Trade payables, Group companies and associates	267	289
Derivatives (Note 14)	117	122
Other payables	12	18
Personnel (outstanding remuneration)	29	45
Public Administrations	27	83
Total	**701**	**751**

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.

At 31 December 2018, Accrued wages and salaries includes Euros 7 million in relation to termination benefits resulting from agreements with employees to terminate their employment contracts, to be paid in the first quarter of 2019. At 31 December 2017, Euros 25 million was recognised for this item, which was paid in the first quarter of 2018.

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:

	2018	2017
	Amount	**Amount**
Total payments (thousand euro)	4,663,208	4,452,183
Total outstanding payments (thousand euro)	52,844	79,532
Average supplier payment period (days) [1]	17	20
Transactions paid ratio (days) [2]	17	20
Transactions pending payment ratio (days) [3]	34	23

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.

The accompanying ratios do not include situations that could distort calculations, such as trade payables, group companies and associates.

Note 17. Tax situation

The Company is the parent of tax consolidated group 59/93, which includes all the companies resident in Spain that are at least 75% directly or indirectly owned by the parent company and that fulfil certain requirements, entailing the overall calculation of the group's taxable income, deductions and tax credits. The tax consolidated group for 2018 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 2018 and 2017 to taxable income is as follows:

	At 31.12.18	At 31.12.17
Accounting profit before tax	**5,282**	**941**
Permanent differences	**(5,544)**	**(1,264)**
Temporary differences:		
Arising during current year	150	43
Arising in prior years	(70)	(23)
Taxable income	**(182)**	**(303)**

Permanent differences mainly relate to the application of the tax consolidation system and the double taxation exemption for dividends and income derived from the transfer of shares under Article 21 of Law 27/2014 on Corporate Income Tax, which has led to negative permanent differences of Euros 547 million resulting mainly from negative adjustments for dividends accruing during the year (Euros 1,264 million in 2017), the impairment of shareholdings in Group companies and associates amounting to Euros 4,565 million (Euros 133 million in 2017) and intragroup sales of shareholdings in Group companies and associates for an negative amount of Euros 9,590 million.

In 2018 the Company posted a tax loss of Euros 182 million (Euros 303 million in 2017), which is recovered from the Tax Group companies due to the taxable income generated by them during the year.

Law 27/2014 maintained the non-tax deductibility of impairment losses on equity interests, which had been introduced under Law 16/2013 with effect from 1 January 2013. In 2018 and 2017 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 2017 are the following:

Company	Amounts pending inclusion in tax base in 2016	Amounts included in 2017	Amounts pending inclusion in tax base in 2017
Other	1	(1)	–
	1	(1)	–

Income tax expense is as follows:

	2018	2017
Current-year tax	(53)	(77)
Deferred tax	53	(5)
Total	**–**	**(82)**

Current corporate income tax is the result of applying a 25% tax rate to taxable income. In the tax consolidated group, tax credits applied in 2018 amounted to Euros 8 million (Euros 9 million in 2017) and no tax losses were offset. Adjustments are also included for prior-year taxable differences, entailing a decrease in the expense of Euros 2 million (decrease of Euros 13 million in 2017).

On 3 December 2016 Royal Decree-Law 3/2016 was published, adopting tax measures for the consolidation of public finances, which introduced relevant changes in the corporate income tax area. Among other matters, with effect from 1 January 2016 the obligation is laid down to reverse provisions for the impairment of shareholdings that would have been deductible before 2013 in a maximum term of five years, the offsetting of tax losses for large companies is limited to 25% of the preliminary tax base and the application of the tax credit for domestic or international double taxation generated or pending application is restricted to 50% of preliminary gross tax payable Additionally, effective from 1 January 2017, losses on the transfer of shares will not be deductible. In 2018 and 2017 these measures did not have a significant impact on the Company's financial statements.

Incomes that qualify to 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 relevant 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 was made in fixed assets related to economic activities carried out by the Company itself or any other company included in the Consolidated Tax Group by virtue of the provisions of 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	19	443
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**	**29**	**2,220**

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 31.12.18			At 31.12.17		
	Gross	**Tax effect**	**Net**	**Gross**	**Tax effect**	**Net**
Cash flow hedges	27	(7)	20	(27)	7	(20)
Actuarial gains and losses and other adjustments	(24)	5	(19)	8	(2)	6
	3	**(2)**	**1**	**(19)**	**5**	**(14)**

A breakdown of deferred taxes is as follows:

	At 31.12.18	At 31.12.17
Deferred tax assets:	152	133
– Non-current	140	126
– Current	12	7
Deferred tax liabilities:	(212)	(227)
– Non-current	(212)	(227)
Net deferred tax	**(60)**	**(94)**

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 1.1.2017	**105**	**6**	**3**	**11**	**3**	**128**
Creation (reversal)	4	–	–	1	–	5
Movements linked to equity adjustments	(2)	–	3	–	–	1
Transfers and other	4	(4)	–	(1)	–	(1)
At 31.12.2017	**111**	**2**	**6**	**11**	**3**	**133**
Creation (reversal)	3	–	–	1	16	20
Movements linked to equity adjustments	(5)	–	4	–	–	(1)
Transfers and other	–	–	–	–	–	–
At 31.12.2018	**109**	**2**	**10**	**12**	**19**	**152**

Deferred tax liabilities	Differences Depreciation	Deferred gains	Other	Total
At 1.1.2017	**3**	**210**	**18**	**231**
Creation (reversal)	–	–	–	–
Movements linked to equity adjustments	–	–	(4)	(4)
Transfers and other	–	(13)	13	–
At 31.12.2017	**3**	**197**	**27**	**227**
Creation (reversal)	(1)	–	(32)	(33)
Movements linked to equity adjustments	–	–	(2)	(2)
Transfers and other	–	10	10	20
At 31.12.2018	**2**	**207**	**3**	**212**

In 2015, the demerger of the thermal and hydraulic power generation business from the Company to Naturgy Generación, S.L.U. was completed. 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. The information requirements stipulated in the special tax scheme are fulfilled in the notes to the Company's 2015 annual accounts.

In 2014, the demerger of the thermal and hydraulic power generation business from the Company to Naturgy 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. The information requirements stipulated in the special tax scheme are fulfilled in the notes to the Company's 2014 annual accounts.

In 2009, the companies Unión Fenosa, S.A. and Unión Fenosa Generación S.A. were merged into the Company 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 the Company's 2009 annual accounts.

In July 2018 tax inspection proceedings were instigated against Naturgy Energy Group, S.A. as the parent company of Group 59/93 in relation to corporate income tax and as the parent company of Group 273/08 with respect to VAT. The periods under inspection for corporate income tax (tax consolidation regime) are from 2011 to 2015 and for VAT purposes (corporate group regime) from June 2014 to December 2015.

This notification interrupts the limitation period for assessing the taxes for the periods mentioned above with respect to the entire tax group for corporate income tax purposes and the VAT Group for VAT purposes.

The inspection proceedings are not expected to significantly impact the Group companies.

In accordance with Spanish tax legislation, at the date of preparation of these annual accounts, the Company's returns for the last four year for the principal taxes to which it is subject and which are not involved in the above-mentioned tax inspection are open to inspection.

On 3 November 2017 an unfavourable judgment was received from the Supreme Court in relation to the tax inspection assessments resulting from inspections on corporate income tax for 2003-2005, due to the application of the deduction for export activities. These assessments had been fully provided for (Note 12) and amounted to Euros 4 million, which has been fully offset by balances to be refunded by the Spanish tax authorities.

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.

Naturgy has recorded provisions for obligations deriving from a number of tax claims. There are no lawsuits or uncertain tax treatments which are individually significant (Note 12).

Note 18. Revenue

Sales break down as follows:

	2018	2017
Electricity sales	1,845	1,714
Natural gas sales	1,614	1,420
Other sales	5	5
Income from equity instruments of Group companies and associates (Note 7)	547	1,470
Income from marketable securities and other financial instruments of Group companies and associates	516	444
Total	**4,527**	**5,053**

	2018	2017
Domestic market	4,130	4,569
Export market	397	484
– European Union	385	445
– OECD countries	–	8
– Other countries	12	31
Total	**4,527**	**5,053**

Electricity and gas sales are made basically in the domestic market and relate to gas and electricity sales to other Naturgy companies.

The Company also has gas supply contracts for other Naturgy companies and in the electricity area it acts as representative of the Naturgy generation and supply companies before the Electricity Market.

Note 19. Raw materials and consumables

Includes purchases of gas and electricity related to the activity of selling gas and electricity to other Naturgy companies.

Note 20. Personnel expenses

The breakdown of this account in the income statement for 2018 and 2017 is as follows:

	2018	2017
Wages and salaries	150	151
Termination benefits	65	29
Social security costs	24	26
Defined contribution plans	12	13
Defined benefit plans (Note 12)	2	2
Share-based payments (Note 11)	4	–
Other	5	13
Total	**262**	**234**

The average number of Company employees in 2018 and 2017 is as follows:

	2018	2017
Executives	488	494
Middle management	202	204
Specialists	723	738
Workers	293	348
Total	**1,706**	**1,784**

The average number of Company employees during 2018 and 2017 with a disability equal to or greater than 33% is as follows:

	2018		2017	
	Men	Women	Men	Women
Executives	3	1	3	–
Middle management	2	1	1	1
Specialists	11	12	12	13
Workers	5	7	7	10
Total	**21**	**21**	**23**	**24**

The number of Company employees at the end of 2018 and 2017 broken down by category and gender is as follows:

	2018		2017	
	Men	Women	Men	Women
Executives	276	167	332	172
Middle management	93	93	112	102
Specialists	260	384	345	412
Workers	53	190	92	252
Total	**682**	**834**	**881**	**938**

Note 21. Other operating expenses

A breakdown of this heading on the income statement account for 2018 and 2017 is as follows:

	2018	2017
Taxes	2	2
Leases, royalties, operation and maintenance	71	80
Professional services and insurance	35	58
Advertising and other commercial services	22	26
Contribution Naturgy Foundation	7	7
Impairment losses and changes in trade provisions (Note 9)	9	–
Other	169	171
Total	**315**	**344**

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

In the community area, the Naturgy Foundation has broadened its activities to place greater emphasis on its community initiatives, defining new strategic lines for actions aimed at palliating energy vulnerability.

Note 22. Other operating income

This account includes Euros 353 million in transactions with group companies and associates in 2018 (Euros 380 million in 2017).

Note 23.Net financial income/(expense)

The breakdown of this account in the Income statement for 2018 and 2017 is as follows:

	2018	2017
Income from marketable securities and other financial instruments	30	31
Total financial income	**30**	**31**
Cost of borrowings	(451)	(545)
Interest expense on pensions (Note 12)	(5)	(4)
Other financial expense	(80)	(37)
Total financial expense	**(536)**	**(586)**
Variation in fair value of financial instruments	8	1
Trading portfolio and other available-for-sale assets	8	1
Net exchange differences	(8)	(1)
Impairment and gains/(losses) on disposals of financial instruments	1	–
Net financial income/(expense)	**(505)**	**(555)**

Note 24. Foreign currency transactions

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

	2018	2017
Sales	1.009	713
Income from equity instruments of Group companies and associates	–	40
Income from marketable securities and other financial instruments of Group companies and associates	12	9
Purchases	(1.006)	(772)
Services received	(9)	(23)
Total	**6**	**(33)**

Note 25. Information on transactions with related parties

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

- Significant Company shareholders, i.e. those directly or indirectly owning an interest of 5% or more, and those who, though not significant, have exercised the power to propose the appointment of a member of the Board of Directors.
- Based on this definition, the significant shareholders of Naturgy are Fundación Bancaria Caixa d'Estalvis i Pensions de Barcelona ("la Caixa"), Repsol, S.A. (Repsol) until 17 May 2018, Rioja Bidco Shareholdings, S.L.U. (controlled by the funds advised by CVC) since 18 May 2018, Global Infrastructure Partners III (GIP) and related companies.
- Directors and executives of the Company and their immediate families. The term "director" means a member of the Board of Directors; "executive" means direct dependency of Executive Chairman and the Internal Audit Director. Operations with directors and executives are disclosed in Note 26.

- Transactions between Group companies form part of ordinary activities and are effected at arm's length. Group companies includes the amount that reflects the Company's share of the balances and transactions with companies consolidated under the equity method.

  At 1 January 2018 Naturgy ceased to regard CaixaBank and the companies that make up its consolidated group as a related entity. However, CriteriaCaixa and its consolidated group continue to be regarded as a related party as the criteria laid down by international and commercial legislation have been maintained.

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

	2018				2017		
Income and expense (in thousand Euros)	**"la Caixa" group ***	**Repsol group ****	**Rioja Bidco/CVC Capital Partners *****	**GIP group**	**"la Caixa" group**	**Repsol group**	**GIP group**
Financial expenses	–	–	–	–	1,007	–	–
Receipt of services	1	801	–	–	7,315	1	–
Purchases of goods	–	–	–	–	–	2,408	–
Other expenses [1]	–	–	–	–	20,796	–	–
Total expenses	**1**	**801**	**–**	**–**	**29,118**	**2,409**	**–**
Financial income	–	–	–	–	5	–	–
Provision of services	–	38	–	–	–	–	–
Sale of goods	–	293	–	–	–	–	–
Total income	**–**	**331**	**–**	**–**	**5**	**–**	**–**

	2018				2017		
Other transactions (thousand euro)	**"la Caixa" group ***	**Repsol group ****	**Rioja Bidco/CVC Capital Partners *****	**GIP group**	**"la Caixa" group**	**Repsol group**	**GIP group**
Financing agreements, loans and capital contributions(lender) [2]	–	–	–	–	1,152,621	–	–
Financing agreements, loans and capital contributions(borrower) [3]	–	–	–	–	100,000	–	–
Warranties and guarantees received	–	–	–	–	160,000	–	–
Dividends and other profits distributed ****	346,808	–	281,202	280,193	244,558	200,859	200,138
Other operations [4]	–	–	–	–	666,476	–	–

* Since 1 January 2018 only transactions with Fundación la Caixa and Criteria Caixa are reported.

** Until 17 May 2018.

*** Since 18 May 2018.

**** The "la Caixa" dividend includes 22,516 thousand paid to Energía Boreal 2018, S.A.

1. Includes contributions to pension plans, group insurance policies, life insurance and other expenditure.
2. Includes cash and cash equivalents.
3. At 31 December 2018, credit lines contracted with "la Caixa" amounted to Euros 569,000 thousand (Euros 569,000 thousand at 31 December 2017), of which no amounts having been utilised. "La Caixa" is not involved in other loans (Euros 100,000 thousand at 31 December 2017).
4. In 2017, the heading "Other transactions" with "La Caixa" included Euros 565,568 thousand in respect of foreign exchange hedges and Euros 100,908 thousand in respect of interest rate hedges.

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

	2018		2017	
Expenses, income and other transactions	**Group companies**	**Jointly-controlled entities and associates**	**Group companies**	**Jointly-controlled entities and associates**
Financial expenses	(464)	–	(496)	–
Lease expenses	(33)	(6)	(39)	(6)
Receipt of services	(28)	–	(28)	–
Purchases of goods	(171)	–	(2,329)	–
Total expenses	**(696)**	**(6)**	**(2,892)**	**(6)**
Financial income	516	–	444	–
Dividends received	546	1	1,486	1
Sale of goods	1,839	–	3,533	–
Other income	351	2	375	5
Total income	**3,252**	**3**	**5,838**	**6**

The item “Purchases of goods” relates basically to electricity purchased from the other Group companies, since the Company 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 7).

“Sales of goods” includes sales of natural gas derived from supply and electricity contracts, as it acts as the representative of the Group companies vis-à-vis the market.

The heading “Other income” includes income from services rendered in accordance with the nature and extent thereof (Note 22).

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 26. Information on members of the Board of Directors and senior management personnel

Remuneration of the members of the Board of Directors

The remuneration policy for the members of the Board of Directors was approved at the General Shareholders’ Meeting held on 27 June 2018 and is periodically reviewed and revised by the Board of Directors following a report from the Appointments and Remuneration Committee, in order to keep it aligned with the best practices in the reference market and with the objectives indicated in the Bylaws.

The amount accrued by the members the Board of Directors of Naturgy Energy Group, S.A., for belonging to the Board of Directors, Executive Committee (EC), Audit Committee (CA) and Appointments and Remuneration Committee (ARM), totalled Euros 4,412 thousand (Euros 4,668 thousand in 2017), broken down in euros as follows:

	Office	Board	EC	AC	ARC	Total
Mr. Francisco Reynés Massanet [1]	Executive Chairman	789,286	239,285	–	–	1,028,571
Mr. Isidro Fainé Casas [2]	Chairman	60,714	60,714	–	–	121,428
Mr. Rafael Villaseca Marco [2]	Chief Executive Officer	13,964	13,964	–	–	27,928
Mr. Ramón Adell Ramón	Coordinating Director	185,136	69,000	51,818	48,226	354,180
Mr. Enrique Alcántara-García Irazoqui	Director	156,500	–	51,818	–	208,318
Mr. Iñigo Alonso de Noriega [4]	Director	27,823	–	–	5,498	33,321
Mr. Xabier Añoveros Trías de Bes [8]	Director	69,000	–	21,818	–	90,818
Mr. Marcelino Armenter Vidal	Director	156,500	69,000	–	30,000	255,500
Mr. Mario Armero Montes [8]	Director	69,000	–	–	–	69,000
Mr. Francisco Belil Creixell	Director	156,500	69,000	50,162	43,636	319,298
Ms. Benita María Ferrero-Waldner [8]	Director	69,000	69,000	–	–	138,000
Mr. Alejandro García-Bragado Dalmau [7]	Director	53,790	28,935	–	10,411	93,136
Ms. Cristina Garmendia Mendizábal [8]	Director	69,000	–	16,657	10,411	96,068
Ms. Helena Herrero Starkie	Director	156,500	–	51,818	–	208,318
Mr. Josu Jon Imaz San Miguel [3]	First Deputy Chairman	23,000	23,000	–	–	46,000
Mr. Guillermo Llopis García [4]	Director	27,823	6,677	8,798	–	43,298
Mr. Miguel Martínez San Martín [3]	Director	23,000	23,000	–	4,546	50,546
Mr. Rajaram Rao	Director	156,500	69,000	51,818	–	277,318
Rioja Bidco Shareholdings, S.L.U., Mr. Javier de Jaime Guijarro [6]	Director	103,823	16,322	–	33,226	153,371
Mr. Pedro Sainz de Baranda [9]	Director	87,500	–	30,000	30,000	147,500
Mr. Claudio Santiago Ponsa [9]	Director	87,500	–	–	30,000	117,500
Mr. Luis Suárez de Lezo Mantilla [5]	Director	52,677	27,823	11,496	–	91,996
Theatre Directorship Services Beta, S.à.r.l., Mr. José Antonio Torre de Silva López de Letona [6]	Director	103,823	16,322	35,161	–	155,306
Theatre Directorship Services Beta, S.à.r.l., Mr. Juan Arbide Estensoro [6 and 8]	Director	16,323	–	–	–	16,323
Mr. William Alan Woodburn	Director	156,500	69,000	–	43,636	269,136
		2,871,182	**870,042**	**381,364**	**289,590**	**4,412,178**

1. Since 6 February 2018.
2. Until 6 February 2018.
3. Until 06 March 2018.
4. From 6 March 2018 to 18 May 2018.
5. Until 18 May 2018.
6. Since 18 May 2018.
7. Until 21 May 2018.
8. Until 27 June 2018.
9. Since 27 June 2018.

In 2018, as in 2017, no amounts were received for other items.

At 31 December 2017, the Board of Directors consisted of 17 members. On 6 February 2018, the Board of Directors agreed to appoint a new Executive Chairman due to the departure of the former CEO and Chairman. As a result, the number of Board members was reduced to 16 persons.

Finally, on 27 June 2018, the General Shareholders' Meeting approved the reduction in the number of members of the Board of Directors 12 members. In addition, the Executive Committee was eliminated and the number of members of the Audit Committee was set at 7 persons and the number of Appointments and Remuneration Committee members was set at 7 persons.

Until 6 February 2018, 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 130 thousand, Euros 115 thousand, Euros 898 thousand and Euros 4 thousand, respectively, in 2018 (Euros 1,285 thousand, Euros 1,131 thousand, Euros 757 thousand and Euros 16 thousand in 2017). He also received the agreed termination benefit of three years' total remuneration and compensation for the no-competition agreement of one year's total salary amounting to Euros 4,248 thousand. Contributions to pension plans and group insurance policies, together with life insurance premiums paid, totalled Euros 34 thousand in 2018 (Euros 321 thousand in 2017).

As from 6 February 2018, the amounts accruing to the Executive Chairman for executive functions carried out in respect of fixed remuneration, annual variable remuneration and other items amounted to Euros 809 thousand, Euros 1,803 thousand and Euros 11 thousand, respectively, in 2018.

Contributions to pension plans and group insurance policies, together with life insurance premiums paid, totalled Euros 490 thousand in 2018. Funds accumulated due to these contributions amount to Euros 360 thousand at 31 December 2018.

The Chairman's contract was approved by the Board of Directors on 6 February 2018 and provides for a fixed remuneration component, an annual variable component and a long-term incentive plan, as well as other welfare benefits.

At a meeting held on 31 July 2018 the Board of Directors approved a long-term variable incentive plan (LTI) in which the Executive Chairman and 25 other executives take part. It is arranged through the acquisitions of shares the main characteristics of which are described in Note 14. The new incentive requires the adaptation of the Remuneration Policy and the Executive Chairman's contract, which are subject to the suspensive condition of being approved by the shareholders in general meeting.

In the central scenario, the Executive Chairman would receive an amount of 125% of the total annual fixed remuneration, multiplied by the expected duration in years of the LTI. This central scenario envisages the distribution of all the dividends foreseen in the Strategic Plan 2018-2022. Also to ensure this scenario it is required that the share price in July 2023 will be above to the purchase price of Euros 23.15.

The Chairman's contract provides for an indemnity for termination or non-renewal as a director of two annual payments of the combined amount of total fixed remuneration, annual variable remuneration and 1.25 times total fixed remuneration (as long-term variable remuneration subject to having achieved the minimum profitability target under the LTI). The indemnity will not be payable in the event of the serious and culpable nonfulfillment of his professional obligations causing significant harm to Naturgy's interests. 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 fixed remuneration is provided for.

Except as mentioned for the CEO, 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 Naturgy. The premium paid in 2018 by Naturgy, S.A. for the entire policy amounted to Euros 121 thousand (Euros 109 thousand in 2017).

Transactions with Directors

The Directors have the obligation to avoid conflicts of interest as established by the Board Regulations of Naturgy Energy Group, S.A. and Articles 228 and 229 of the Spanish Companies Law. Additionally, these articles require that conflicts of interest incurred by the board shall be reported in the annual accounts.

The Directors of Naturgy have not reported any conflict of interest to the Board of Directors that has to be notified.

In transactions with related parties (significant shareholders) that have been submitted for approval by the Board, subject to a favourable report of the Audit Committee, any directors linked to the related party involved have abstained.

During the years 2018 and 2017, 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.

Senior management remuneration

For the sole purposes of the information contained in this section, "senior management personnel" refers to executives reporting directly to the Executive Chairman, excluding the Executive Chairman, whose remuneration has been included in the previous section, and to the Internal Audit Director.

At 31 December 2018, 13 people make up this group, without taking into account the Internal Audit Director (11 people at 31 December 2017), one of whom is a woman. During 2018 there were two new members in July and two departures in December.

The amounts accrued by senior management personnel in respect of fixed remuneration, annual variable remuneration, multi-year variable remuneration and other items totalled Euros 6,769 thousand, Euros 3,853 thousand, Euros 595 thousand and Euros 230 thousand, respectively, in 2018 (Euros 5,507 thousand, Euros 2,595 thousand, Euros 1,641 thousand and Euros 108 thousand in 2017).

Contributions to pension plans and group insurance policies, together with life insurance premiums paid, totalled Euros 1,599 thousand in 2018 (Euros 2,564 thousand in 2017). Funds accumulated due to these contributions amount to Euros 23,309 thousand at 31 December 2018 (Euros 26,367 thousand at 31 December 2017).

At a meeting held on 31 July 2018 the Board of Directors approved a long-term variable incentive plan (LTI) in which the Executive Chairman and 25 other executives take part. It is arranged through the acquisitions of shares the main characteristics of which are described in Note 11.

Advances amounting to Euros 30 thousand had been granted to management personnel at 31 December 2018 (zero at 31 December 2017). At 31 December 2018, Naturgy had not granted any new guarantees on loans to management personnel (Euros 754 thousand at 31 December 2017). Severance benefits received by senior management personnel leaving Naturgy amounted to Euros 6,493 thousand in 2018 (zero in 2017).

The contracts signed with the 11 directors contain a clause that establishes compensation between a fixed annual remuneration in some cases and three and a half annual remuneration in others, in certain cases of extinction of the relationship, which include certain situations of change in control, unfair dismissal or the cases contemplated in articles 40, 41 or 50 of the Statute of Workers. Likewise, 10 of these contracts contain a clause that establishes compensation equivalent to an annuity of fixed remuneration for post-contractual non-competition for a period of two years.

Note 27. Contingent liabilities and commitments

Guarantees

Guarantees furnished by Naturgy Energy Group, S.A. at 31 December 2018 and 2017 are as follows:

- Guarantees provided to third parties, basically for investment commitments of Group companies, amounting to Euros 55 million (Euros 138 million at 31 December 2017).

- Guarantees relating to the economic obligations resulting from its participation in the Spanish electricity system (MEFF and OMIE) for Euros 160 million (Euros 200 million at 31 December 2017).

- Guarantee exist for compliance with obligations under loans received by Group companies amounting to Euros 7 million and USD 75 million.

- Guarantees to group companies Naturgy Capital Markets, S.A., Naturgy Finance, B.V., Unión Fenosa Preferentes, S.A.U. and Gas Natural México S.A. de C.V. for debt issuances carried out by them totalling Euros 11,531 million (Euros 12,879 million at 31 December 2017).

- Guarantees to group companies Naturgy Aprovisionamientos, S.A. and Gas Natural Europe, S.A.S for obligations under the gas purchase and transport contracts and gas tanker chartering agreements.

- Irrevocable guarantee for all the liabilities and commitments of Naturgy Energy (UK), Ltd. and its subsidiaries in Ireland at 31 December 2018 and 31 December 2017, in accordance with Article 357 of the 2014 Companies Act of Ireland, in order to file the consolidated financial statements of Naturgy instead of its separate financial statements on the basis of the exemption allowed under Section 1 (b) of said Act.

As the above guarantees are basically granted in order to guarantee the fulfilment of contractual obligations or investment commitments, the events that would lead to their execution, and therefore a cash disbursement, would be the nonfulfillment by Naturgy of its obligations in the ordinary course of its business, the probability of which is considered remote. Naturgy estimates that the liabilities not foreseen at 31 December 2018, if any, that could arise from guarantees furnished, would not be significant.

Contractual commitments

At 31 December 2018, the Company is party to several gas supply contracts with "take or pay" clauses negotiated for "own use" (Note 3.5), by virtue of which it has gas purchase rights for the period 2019-2040 in the amount of Euros 3,489 million, calculated on the basis of natural gas prices at 31 December 2018 (2017: Euros 8,056 million based on natural gas prices at 31 December 2017).

Operating lease obligations breakdown as follows:

	2018	**2017**
Up to one year	17	20
Between 1 and 5 years	76	73
Between 5 and 10 years	32	43
	125	**136**

Includes the rent of the "Torre del Gas" building owned by Torre Marenostrum, S.L., for which the Company has an operating lease without a purchase option until 2019 extendible at market value for successive periods of three years, on a discretionary basis for the Company and an obligatory basis for Torre Marenostrum S.L.

It also includes operating leases without a purchase option for five properties in Madrid (Avenida San Luis 77, Antonio López 193, Acanto 11-13, Avenida América 38 and calle Lérida) for a nine-year term which may be extended for five years except in the case of Avenida América 38 (Note 6).

Litigation, arbitration, guarantees and commitments

The Company is involved in certain judicial and extrajudicial disputes within the ordinary course of their activities. At the date of preparation of these annual accounts, the main litigation or arbitration in which the Company is involved are the following:

Qatar Gas arbitration

In May 2015, Naturgy commenced an arbitration procedure against Qatar Liquefied Gas Company Limited in order, among other matters, to set the prices for gas supplies that it receives from said company. Naturgy has requested a price reduction and the supplier has requested an increase. The award was delivered on 3 February 2018 and contains various provisions that require negotiations between the parties, which have given rise to a second arbitration process.

Unión Fenosa Gas

In 2014, Egyptian Natural Gas Holding (EGAS), an Egyptian public company, ceased to supply gas to Unión Fenosa Gas, a company 50% owned by Naturgy, and stopped paying the utilisation fee for the Damietta liquefaction plant. This led to Unión Fenosa Gas instigating arbitration proceedings at various locations (Madrid, El Cairo and the CIADI) against this supplier, which requested the nullity of the contract, and against the Arab Republic of Egypt. In December 2017 the arbitration proceedings against EGAS conducted in Cairo concluded with a decision that confirmed the position of Unión Fenosa Gas concerning the nonfulfillment of the relevant obligations. The decisions on the arbitration under way in Madrid have yet to be delivered. In August 2018 a decision was made in the investment protection arbitration proceedings (ICSID) against the Arab Republic of Egypt, ordering it to pay USD 2,013 million after taxes and before interest. On 19 December 2018 Unión Fenosa Gas obtained confirmation of the award in the United Kingdom and expects to obtain confirmation in the United States. On 21 December 2018, the Arab Republic of Egypt submitted an appeal to the ICSID against the award and requested its suspension while the appeal proceedings last, as has been done.

Social Bond

The Supreme Court has ordered to reimbursement of the amounts contributed by Naturgy Energy Group, S.A. to the social bond for 2014 to 2016 (Euros 74 million) in accordance with Royal Decree-Law 9/2013. However, this decision has been appealed against by the government before the Constitutional Court. Though unlikely, said Court could revoke the Supreme Court ruling.

The Company's balance sheet at 31 December 2018 includes provisions for litigation, based on the best estimate made using the information available at the date of preparation of these annual accounts on their progress and ongoing negotiations, which cover the estimated risks. The Company therefore considers that no significant liabilities will be derived from the risks described in the relevant section of this Note.

Note 28. Auditors' fees

The fees accrued in thousand euro by the different companies trading under the Ernst & Young brand in 2018 (PwC in 2017) are as follows:

						Thousand Euros
	2018			2017		
	Ernst & Young, S.L.	Rest E&Y network	Total	PwC Auditores, S.L.	Rest PwC network	Total
Auditing services	681	–	681	912	–	912
Assurance services and services related to the audit [1]	42	–	42	383	–	383
Other services [1]	181	–	181	146	881	1,027
Total fees	**904**	**–**	**904**	**1,441**	**881**	**2,322**

1. These headings include verification reports on non-financial information, comfort letters and advice on sustainability

Note 29. Environment

Environmental actions

Naturgy is aware of its activities' environmental impacts and therefore the company pays particular attention to the protection of the environment and the efficient use of natural resources to meet energy demand.

Responsible environment management is a strategic pillar for Naturgy and is structured around three strategic axes:

- Climate and air: contributing to the mitigation of climate change, the energy transition and the improvement of air quality.

- Circular economy: enhancing eco-efficiency in the use of resources to reduce negative environmental impacts.
- Natural capital and biodiversity: promoting the conservation of natural and cultural heritage in the areas of action.

To achieve this, environmental management is based on the ISO 14001 model, the correct functioning of which is audited externally each year, providing the tools required to optimise environmental management.

In climate and air, the main lines of action carried out in 2018 to reduce emissions are the replacement of carbon-intensive fuels by more sustainable fuels, renewable generation and the reduction of leak emissions in gas distribution networks.

In 2018 direct CO_2 emissions fell compared with 2017 as two factors. First, the meteorological conditions have led to an increase in renewable generation (hydroelectric and, to a lesser extent, wind power) and a reduction in coal generation, resulting in a reduction in CO_2 emissions. Secondly, the disinvestments in Kenya, in CO_2-intensive generation technologies and in Colombia (gas distribution) have also contributed to the reduction in greenhouse gas emissions.

In the circular economy, the lines of work are different. Firstly, energy efficiency improvement projects were carried out, both at our own facilities and at our customers', and initiatives were developed to reduce the consumption of various materials and consumables. Actions have also been taken to enhance waste recovery and reduce waste generation. With regard to water, measures have been taken to optimise water consumption, such as the actions taken at the Aceca CC plant to reduce consumption of clarified water. On a global level there was a decrease in 2018 compared to 2017, mainly due to lower demand for coal-fired power plants. It should finally be noted that innovation projects have been carried out in new energy models that are fully aligned with the circular economy. An example of this is the pilot plants to generate renewable gas from urban wastewater at the Arazuri (Navarra) or Bens treatment plants and the Metamorphosis project to convert waste treatment plants into bioenergy plants.

In 2018, Naturgy has conducted multiple actions in the natural capital and biodiversity area, all of which are aligned with the prevention, reduction and compensation for its impacts and the enhancement of the value of the natural surroundings.

The environmental activities undertaken in 2018 by the Company amounted to Euros 11 million, Euros 1 million relating to environmental investment and Euros 10 million relating to the costs of environmental management at facilities (Euros 1 million for environmental investments and Euros 9 million related to expenses incurred in environmental management at facilities in 2017).

Finally, referring to possible contingencies, indemnities and other environmental risks that may be incurred by the company, third-party liability insurance policies are in place to cover any damage that might arise.

Note 30. Events after the reporting date

There were no significant events between 31 December 2018 and the date of preparation of these financial statements.

Appendix I. Naturgy Tax Group Companies

The companies in the Naturgy tax group are as follows:

Naturgy Energy Group, S.A.	Naturgy Iberia, S.A.
Boreas Eólica 2, S.A.	Naturgy Informática, S.A.
Comercializadora Regulada Gas & Power, S.A.	Naturgy Infraestructuras EMEA, S.L.
Energías Ambientales de Somozas, S.A.	Naturgy Inversiones Internacionales, S.A.
Energías Especiales Alcoholeras, S.A.	Naturgy LNG, S.L.
Europe Maghreb Pipeline, Ltd.	Naturgy Participaciones, S.A.U.
Explotaciones Eólicas Sierra de Utrera, S.L.	Naturgy Renovables, S.L.U.
Fenosa, S.L.U.	Naturgy Wind 4, S.L.U.
Gas Natural Comercializadora, S.A.	Naturgy Wind, S.L.U.
Gas Natural Exploración, S.L.	Nedgia Andalucía, S.A.
Gas Natural Fenosa Renovables Ruralia, S.L.U.	Nedgia Aragón, S.A.
Gas Natural Redes GLP, S.A.	Nedgia Balears, S.A.
Gas Natural Transporte SDG, S.L.	Nedgia Castilla La-Mancha, S.A.
General de Edificios y Solares, S.L.	Nedgia Catalunya, S.A.
Global Power Generation, S.A.	Nedgia Cegas, S.A.
GPG Ingeniería y Desarrollo de Generación, S.L.U.	Nedgia Madrid, S.A.
GPG México Wind, S.L.U.	Nedgia Navarra, S.A.
GPG México, S.L.U.	Nedgia, S.A.
Holding de Negocios de Gas, S.A.	Operación y Mantenimiento Energy, S.A.
J.G.C. Cogeneración Daimiel, S.L.	P.E. El Hierro, S.L.
La Energía, S.A.	P.E. Montamarta, S.L.
La Propagadora del Gas, S.A.	P.E. Nerea, S.L.
Lignitos de Meirama, S.A.	P.E. Peñarroldana, S.L.
Naturgy Acciones, S.L.	Petroleum Oil & Gas España, S.A.
Naturgy Alfa Investments, S.A.U	Sagane, S.A.
Naturgy Almacenamientos Andalucía, S.A.	Sociedad de Tratamiento Hornillos, S.L.
Naturgy Aprovisionamientos, S.A.	Sociedad Parque Eólico Mouriños, S.L.U.
Naturgy Capital Markets, S.A.	Societat Eòlica de l´Enderrocada, S.A.
Naturgy Distribución Latinoamérica, S.A.	Tratamiento Cinca Medio, S.L.
Naturgy Electricidad Colombia, S.L.	Tratamiento Almazán, S.L.
Naturgy Engineering, S.L.	UFD Distribución Electricidad, S.A.
Naturgy Gas and Power, S.L.U.	Unión Fenosa Minería, S.A.
Naturgy Generación, S.L.U.	Unión Fenosa Preferentes, S.A.U.

Naturgy Energy Group, S.A.
Annual Report 2018

Directors' Report

1. Business performance and results

The main financial aggregates of Naturgy Energy Group, S.A. and their performance are as follows:

	2018	2017	%
Net turnover	4,527	5,053	(10.4)
Operating profit	5,787	1,496	286.8
Profit for the year	5,282	1,023	416.3
Shareholders' equity	17,253	13,473	28.1
Net equity	17,226	13,466	27.9
Current liabilities	2,286	4,240	(46.1)

Naturgy Energy Group, S.A., is a company that develops its activity basically through the tendency of other group and associated companies shares, so information bellow refers to de Consolidated group of Naturgy.

1.1. Main milestones and key figures

1.1.1. Main milestones in 2018

January to March

- Naturgy issued Euros 850 million in 10-year bonds paying 1.5%, the proceeds from which were used to tender for Euros 916 million in bonds maturing between 2019 and 2023.
- Publication of the first report in compliance with Decree-Act 18/2017 on non-financial and diversity disclosures, which transposed into Spanish law European Directive 2014/95 as regards disclosure of non-financial and diversity information and requires companies to report on environmental, social and governance issues.
- On 1 and 22 February 2018, following approval by the competition authorities, the sale of the gas distribution and supply companies in Italy for Euros 766 million was completed, resulting in a capital gain of Euros 188 million after taxes.
- On 6 February 2018, following the resignation of Mr. Rafael Villaseca Marco as Managing Director of the company, the Board of Directors of Naturgy appointed Mr. Francisco Reynés Massanet as Executive Chairman. Additionally, Mr. Isidro Fainé Casas resigned as a director and was appointed Honorary Chairman of Naturgy.
- On 22 February 2018, Repsol reached an agreement to sell its 20.072% stake in the capital of Naturgy Energy Group, S.A. to Rioja Bidco Shareholdings, S.L.U., a company controlled by funds advised by CVC; the deal was completed in May 2018.
- Top Employers 2018 recognition due to having some of the highest standards in work conditions.
- Naturgy, through subsidiary Global Power Generation (GPG), acquired two solar photovoltaic projects in Brazil in March 2018. The development of these projects, located in the state of Minas Gerais and with a total capacity of 83 MW, represented an investment of over Euros 95 million; they entered commercial operation on 12 December 2018.
- On 19 March 2018, following approval by the competition authorities, a minority 20% stake in the company Holding de Negocios de Gas, S.A., which owns gas network assets in Spain, was sold to a consortium of long-term infrastructure investors comprising Allianz Capital Partners and Canada Pension Plan Investment Board for Euros 1.5 billion, resulting in a capital gain of Euros 1 billion.

April to June

- The volunteer programme with the Red Cross that commenced in 2017 concluded in June 2018, having attained a total of 481 Naturgy volunteers; 437 families were assisted in person, 108 express refurbishments were performed, and another 1,080 households received energy efficiency kits and energy advice workshops.
- The sale of the remaining 41.9% of the gas distribution business in Colombia for Euros 334 million, i.e. its net carrying amount net of dividends received, was completed on 1 June 2018.
- On 27 June 2018, the Shareholders' Meeting approved the distribution of income consisting of allocating Euros 1,001 million out of 2017 income to dividends. That is a dividend of Euro 1 per share, of which Euros 0.33 per share was paid as an interim dividend in cash on 27 September 2017 and the remaining Euros 0.67 per share, also in cash, on 5 July 2018.

- The Shareholders' Meeting also approved the Business Plan 2018-2022, which establishes a new industrial and business unit model, providing for the continuity of the businesses and markets in the future, and updating the main premises and business projections.
- On 27 June 2018, Naturgy reached an outline agreement to sell its 70% stake in Kangra Coal (a mine in South Africa) to Menar Holding. The sale was completed in December 2018.
- Additionally, on 27 June 2018, Naturgy reached an agreement to sell its 100% stake in Iberafrica Power, in Kenya, to AEP Energy Africa Limited; the sale is expected to be completed the first quarter of 2019.
- In June, Naturgy was awarded the "Empresa más igual" seal by the Madrid regional government.

July to September

- In July 2018, the company obtained the Bequal plus certificate, which recognises companies with excellent management of people in terms of diversity of ability.
- In September 2018, Naturgy concluded the agreement to renew and extend the gas supply contract with Sonatrach to 2030 under better terms.
- On 3 September 2018, Unión Fenosa Gas (UFG), the company that owns the Damietta plant in Egypt and is owned 50% by Naturgy, received an arbitration award in its favour from the International Centre for Settlement of Investment Disputes (ICSID), an agency of the World Bank, resolving the dispute presented in 2014; the arbitrators ruled against the Arab Republic of Egypt for failure to supply to UFG's liquefaction facilities in Damietta.
- On 11 September 2018, the Government of Victoria in Australia announced the award to GPG of a total of 180 MW of power generating capacity in a wind project located approximately 150 km from the city of Melbourne.
- In September 2018, the Dow Jones Sustainability Index (DJSI) ranked Naturgy as the world leader in the Gas Utilities sector for the second consecutive year; the company was also certified as world leader in the multiutilities segment by FTSE4GOOD.
- In September 2018, the women's leadership programmes "Take The Lead" and "Hazte Visible" granted Naturgy the Talent Mobility 2018 award.

October to December

- In October 2018, the company was awarded the "Equality in employment" seal by Spain's Ministry of the Presidency, Relations with Parliament and Equality in recognition of the implementation of equal opportunity policies through comprehensive, measurable equality plans that produced concrete results.
- The Solidarity Fund for Energy Rehabilitation was launched in October 2018; the funds were allocated to energy refurbishment of dwellings selected by NGOs with which the company has cooperation agreements.
- On 19 October 2018, Naturgy completed a Euros 314 million bond tender.
- On 6 December 2018, Compañía General de Electricidad, S.A., a subsidiary of Naturgy Energy Group, S.A. in Chile, completed a bond issue for a total of 5 million Unidades de Fomento (UF), equivalent to approximately Euros 176 million.
- On 6 December 2018, Naturgy Energy Group S.A. resolved to conduct a share buyback programme in accordance with the announcement made in the Business Plan 2018-2022 that was presented on 28 June 2018; the shares may be retired if the Shareholders' Meeting to be held in the first half of 2019 so decides.
- On December 2018 Naturgy was awarded the EFR "Family-friendly enterprise" seal by Fundación Más Familia for its contribution to its employees' work-life balance.

Financial performance (Euros million)

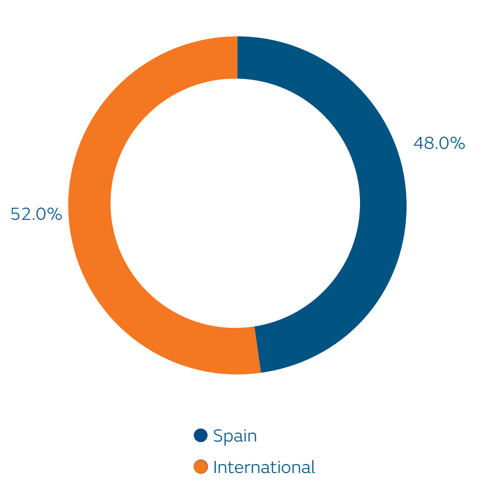
Notes to financial information

- Naturgy's financial disclosures contain magnitudes and metrics drafted in accordance with International Financial Reporting Standards (IFRS) and others that are based on the Group's disclosure model, referred to as Alternative Performance Metrics (APM), which are viewed as adjusted figures with respect to those presented in accordance with IFRS. The attached annex includes a glossary of terms with the definition of the APMs.
- The consolidated income statement and operating figures for 2017 have been re-stated due to the discontinuation of the mining business in South Africa in application of IFRS 5.

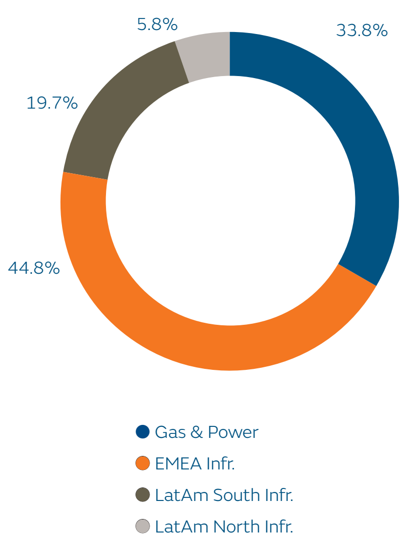
Main financial aggregates

	2018	2017	%
Revenue	24,339	23,207	4.9
Ebitda	4,019	3,903	3.0
Income attributable to equity holders of the parent	(2,822)	1,360	–
Capex	2,321	1,782	30.2
Net financial debt (at 31/12)	13,667	15,154	(9.8)
Free Cash Flow after minorities	3,054	746	–

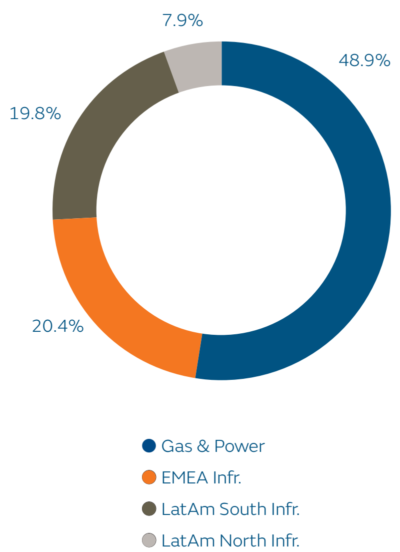
Ebitda by geography 2018 (%)



Ebitda by business 2018 (%)



Capital expenditure by business in 2018 (%)



Main financial ratios

	2018	2017
Leverage	48.4%	45.3%
Ebitda / Net debt Cost	7.5x	6.4x
Net financial debt / Ebitda	3.4x	3.9x
Net financial debt / Ebitda (IFRS 16)	3.8x	4.2x

Main stock market ratios and shareholder remuneration

	2018	2017
Total nº of shares ('000)	1,000,689	1,000,689
Average no. of shares ('000) [1]	998,966	1,000,478
Share price at 31/12 (Euros)	22,26	19,25
Market capitalisation at 31/12 (Euros million)	22,275	19,263
Earnings per share (Euros)[1]	(2,82)	1,36
Dividend paied	1,400	1,001

1. Calculated considering the weighted average number of shares during the year.

1.2. Operational performance

Distribution	2018	2017
Gas distribution (GWh)	449,259	460,014
Electricity distribution (GWh)	54,920	53,670
Gas distribution connections ('000)	10,605	10,491
Electricity connection points ('000)	7,569	7,447
Gas distribution network (km)	119,998	116,181
Length of electricity transmission and distribution network (km)	215,532	214,399

Gas	2018	2017
Gas supply (GWh)	237,379	237,945
LNG International (GWh)	140,669	122,086
Total gas supply (GWh)	**378,048**	**360,031**

Electricity	2018	2017
Installed capacity in Spain (MW)	12,479	12,716
Installed capacity in rest of world (MW)	3,093	2,732
Total installed capacity (MW)	**15,572**	**15,448**
Net production in Spain (GWh)	28,307	27,953
Net production in rest of world (GWh)	18,351	18,436
Total net production (GWh)	**46,658**	**46,389**

1.3. Environmental and social performance

Main aggregates

Environment	2018	2017
Emission factor (t CO2/GWh)	342	388
GHG emissions (M tCO_2 e)[1]	18.3	20.5
Emissions-free installed capacity (%)	27.5	26.4
Emissions-free net production (%)	24.9	19.6

Interest in people	2018	2017
No. of employees [2]	12,700	14,718
Training hours per employee	49.9	38.4
Men/women (%)	69/31	71/29

Health and safety	2018	2017
No. of accidents leading to days lost	28	45
Frequency	1.0	1.3

Commitment to society and integrity	2018	2017
Economic value distributed (Euros million)	23,413	22,402
No. of notifications received by the Ethics Committee	199	141

1. GHG: greenhouse gases, measured as tCO2 equivalent (scope 1).
2. Does not include the number of employees at discontinued operations (786 persons in 2018 and 2,053 persons in 2017).

2. Main risks and opportunities

2.1. Risks

2.1.1. Risk management model

Naturgy's risk management model seeks to ensure that the company's performance is predictable in all aspects that are of relevance to its stakeholders. This requires establishing the risk tolerance by setting limits for the main risk categories. In this way, the company can anticipate the consequences of certain risks and be perceived in the market as a sound, stable company, with all the benefits that entails.

Naturgy has a framework integrating the vision of governance, risks and compliance so as to provide a 360º view of the group's processes, existing controls and the associated risks.

Risk management bodies

Guaranteeing the predictability and sustainability of the company's operational and financial performance is a key aspects of risk management at Naturgy, and is supported by a number of bodies with clearly identified areas of responsibility.

Audit Committee

Supervises the company's internal control and risk management systems. Its function is to identify the various types of risk and the measures implemented to mitigate them, and to address them in the event that they materialise in the form of actual damage.

Risk Committee

Entrusted with determining and reviewing the company's target risk profile. It ensures that the risk profile is aligned with the company's strategic position and it also safeguards stakeholders' interests. It also exercises oversight to ensure that the entire organisation understands and accepts its responsibility for identifying, assessing and managing the main risks.

Risk Control Units

In charge of monitoring and reporting risks and ensuring that they fall within the limits defined in the target risk profile by the Risks Committee. Three units in particular stand out:

- Risks and Insurance:Identifies, monitors and tracks the Group's overall risk profile based on a definition of policies and metrics in coordination with the business units. Supports the Risk Committee in determining and monitoring the overall risk profile.

- Gas & Power Risks: Oversees and proposes measures to mitigate risks on the basis of Group policy, reducing volatility to achieve the target rate of return.

- Internal audit: Reviews and tracks the internal control system established by Senior Management and evaluates the operational risks linked to the processes. Supports the Audit Committee in its supervisory functions.

Businesses

In charge of managing risk in all their areas of action. They identify trends and positions that may entail risk and report them to the Risk Units. They also apply the guidelines and criteria established by the Risk Units.

Business, Corporate and Project units

Responsible for applying the general principles established in the Risk Control and Management Policy and for risk management in their areas of responsibility, observing, reporting, managing and mitigating risks.

Risk categories

Each business unit has specific information on the main types of risk that may affect it. The goal is to facilitate decision-making, which is positive for the company since it enhances profitability, predictability and efficiency.

The system addresses basically three categories of risk:

- **Market risk**, understood as the uncertainty related to commodity prices, exchange rates and interest rates, which may impact the company's balance sheet, its procurement costs or its ability to raise funding in the capital markets. It is measured using two yardsticks: in the short term, focused on the income statement, and in the long term, focused on enterprise value, including the capacity to generate cash flow and its stability, variations in the funding structure, and volatility in the applicable discount rates.

- **Credit risk**, i.e. the risk to the financial solvency of the company's receivables. It also incorporates the short-term measurement of returns on placing cash surpluses with financial institutions, the aim being to select the most efficient portfolios.

- **Operating risk**, i.e. the possibility of financial losses as a result of failures in processes, internal systems or other factors. It enables risk to be measured objectively, which is decisive for raising awareness within the company and for improving management of exposure, all of which have an essential impact on the reinsurance market's perception of Naturgy's operational excellence.

2.1.2. Main risks

Risk type		Description	Management approach	Metric		Trend
Market risks						
Commodity prices	Gas	Volatility in the international markets that set gas prices.	Physical and financial hedges. Portfolio management.	Stochastic	▲	Decoupling of long-term contracts from hub prices.
	Electricity	Volatility in the Spanish and Portuguese electricity markets	Physical and financial hedges. Optimisation of the power generating fleet.	Stochastic	▲	Penetration by renewables with zero marginal cost and intermittent production.
Volume	Gas	Mismatch between gas supply and demand.	Optimisation of contracts and assets worldwide.	Deterministic/ Stochastic	◀▶	Aggregate demand pressure in Spain in a context of energy efficiency.
	Electricity	Reduction of the available thermal gap. Uncertainty about volume of hydroelectric output.	Optimisation of the balance between supply and generation.	Stochastic	▲	Aggregate demand pressure in Spain in a context of energy efficiency.

Risk type	Description	Management approach	Metric		Trend
Regulatory	Exposure to regulatory review of the criteria and returns recognised for regulated activities.	Step up communications with regulators. Adjust efficiency and capital expenditure to recognised rates.	Scenarios	▲	Different business units at different stages of maturity.
Exchange rate	Volatility in international currency markets.	Geographic diversification. Hedging via local-currency funding and derivatives. Monitoring the net position.	Stochastic	◀▶	Uncertainty about growth prospects in Latin America.
Interest rate and credit spread.	Volatility in funding rates.	Financial hedges. Diversification of funding sources.	Stochastic	◀▶	Uncertainty about the interest rate scenario. .
Tax	Ambiguity or subjectivity in the interpretation of current tax regulations, or due to a material amendment of same.	Queries to independent expert bodies. Engagement of top-level advisory firms. Adoption of the Code of Best Tax Practices. Recognition of provisions on a prudential basis.	Scenarios	◀▶	Different business units at different stages of maturity.
Credit risk					
Credit	Uncertainty about performance of bad debt ratios as a result of the economic cycle.	Analysis of customer solvency to define specific contractual conditions. Debt collection process.	Stochastic	◀▶	Pursues efficiency in debt collection.
Operational risk					
Operational: insurable risks	Accidents, damage and non-availability of Naturgy assets.	Continuous improvement plans. Optimisation of total cost of risk and of hedges.	Stochastic	▲	Growing tension in the insurance market in the face of natural catastrophes.
Operational: image and reputation	Impaired perception of Naturgy by stakeholders.	Identification and tracking of potential reputational events. Transparency.	Scenarios.	◀▶	Stabilisation of MERCO index score.
Operational: environment	Harm to the natural and/or social environment. Trend in environmental regulations.	Emergency plans at facilities with risk of environmental accident. Specific insurance policies. End-to-end environmental management.	Scenarios.	▼	Implementation of an Integrated Management System that is audited and certified each year by AENOR.
Operational: climate change	Changes in environmental factors as a result of climate change. Regulation aimed at combating it.	Corporate positioning vis-à-vis climate change.	Stochastic/ Scenarios	▲	Uncertainty about policy developments to encourage energy efficiency.

Metrics used:

- **Stochastic:** production of trend lines for the main magnitudes, taking the maximum deviation from the benchmark scenario to be the risk, within a pre-set confidence interval. Those magnitudes are generally EBITDA, earnings after taxes, cash flow and value.

- **Scenarios:** analysis of the impact with respect to the benchmark scenario of a limited number of possible incidents.

Financial risks (interest rate, exchange rate, commodity prices, credit risk, liquidity risk) are discussed in Note 14 to the Naturgy Energy Group, S.A. Financial Statements.

2.2. Opportunities

Naturgy's main opportunities are as follows:

- **Renewable generation:** Increase renewable capacity internationally, given that renewable energies are cost-competitive and considering Naturgy's presence in growth markets.

- **Generation mix:** Naturgy's generating fleet, which is dominated by CCGTs, has the necessary flexibility to adapt to different market situations and is a valuable asset for seizing opportunities related to volatility in prices and demand volume in the gas and electricity markets.

- **Portfolio of natural gas and LNG procurements:** Management of gas pipelines, stakes in plants and the fleet of LNG carriers make it possible to meet the needs of the Group's various businesses in a flexible, diversified way by optimising for different energy scenarios. Naturgy is one of the world's leading LNG operators and a key player in the Atlantic and Mediterranean.

- **A balanced structural position** in businesses and regions, many of them with stable flows that are independent of commodity prices, making it possible to optimise the capture of energy demand growth and maximise new business opportunities in new markets.

- **Technological development and innovation:** Naturgy focuses on research, development and innovation as a means of generating a reliable, sustainable energy supply.

3. Corporate governance

3.1. Corporate Governance Model

Naturgy is governed in accordance with the principles of efficiency and transparency in line with the main recommendations and standards in this area, and it adopts advanced corporate governance practices for this purpose.

The corporate governance terms of reference comprise basically:

- Articles of Association (updated in 2018).
- Regulations of the Board of Directors and its committees (updated in 2018).
- Regulations of the General Meeting of Shareholders (updated in 2018).
- Human Rights Policy.
- Code of Ethics (updated in 2015).

On 6 February 2018, following the resignation of Mr. Rafael Villaseca Marco as Managing Director of the company, the Board of Directors of Naturgy appointed Mr. Francisco Reynés Massanet as Executive Chairman. Additionally, Mr. Isidro Fainé Casas resigned as a director and was appointed Honorary Chairman of Naturgy.

On 22 February 2018, Repsol, S.A. reached an agreement to sell its 20.072% stake in the capital of Naturgy Energy Group, S.A. to Rioja Bidco Shareholdings, S.L.U., a company controlled by funds advised by CVC. The transaction was completed on 18 May 2018, with the result that Repsol, S.A. ceased to be a shareholder of the company.

Following that transactions, the main shareholders of Naturgy as of 31 December 2018 are as follows:

	Stake %	
	2018	**2017**
- Fundación Bancaria Caixa d'Estalvis i Pensions de Barcelona,"la Caixa" [1]	25.6	24.4
- Repsol, S.A.	–	20.1
- Global Infrastructure Partners III [2]	20.0	20.0
- Rioja Bidco Shareholdings, S.L.U. [3]	20.1	–
- Sonatrach	3.9	4.0

1. A 20.4% direct holding through Criteria Caixa S.A.U. and 5.2% indirect (holding 5.0% through Energía Boreal 2018, S.A. and 0.2% through other).
2. Global Infrastructure Partners III, which is managed by Global Infrastructure Management LLC, holds its stake indirectly via GIP III Canary 1, S.à.r.l.
3. Controlled by funds advised by CVC.

Following the changes in ownership structure, on 27 June 2018 the Shareholders' Meeting approved the reduction in the number of members of the Board of Directors to 12. Additionally, the Executive Committee was eliminated and the number of members of the Audit Committee and of the Appointments and Remuneration Committee was set at 7 in both cases.

As a result of those changes, the following directors stepped down:

- Mr. Isidro Fainé Casas (Chairman), on 6 February 2018.
- Mr. Rafael Villaseca Marco (Managing Director), on 6 February 2018.
- Mr. Alejandro García-Bragado (proprietary director, representing Criteria), on 21 May 2018.
- Mr. Josu Jon Imaz San Miguel (proprietary director, representing Repsol), on 6 March 2018.
- Mr. Luis Suárez de Lezo Mantilla (proprietary director, representing Repsol), on 18 May 2018.
- Mr. Iñigo Alonso de Noriega (proprietary director, representing Repsol), appointed on 6 March 2018 until 18 May 2018.
- Mr. Guillermo Llopis Garcia (proprietary director, representing Repsol), appointed on 6 March 2018 until 18 May 2018.
- Mr. Mario Armero Montes (proprietary director, representing GIP), on 27 June 2018.
- Theatre Directorship Services Beta, S.à.r.l., Mr. Juan Arbide Estensoro (proprietary director, representing CVC), appointed on 18 May 2018 until 27 June 2018.
- Ms. Cristina Garmendia Mendizabal (independent), until 27 June 2018.
- Ms. Benita María Ferrero-Waldner (independent), until 27 June 2018.
- Mr. Xavier Añoveros Trias de Bes (independent), until 27 June 2018.

And the following new directors were appointed:

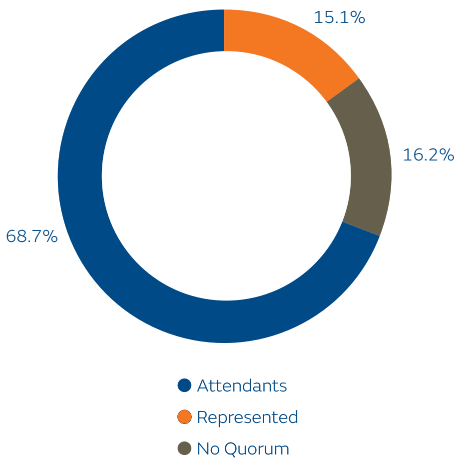
- Rioja Bidco Shareholdings, S.L.U., Mr. Javier de Jaime Guijarro (proprietary director, representing CVC), appointed on 18 May 2018.
- Theatre Directorship Services Beta, S.à.r.l., Mr. José Antonio Torre de Silva López de Letona (proprietary director, representing CVC), appointed on 18 May 2018.
- Mr. Pedro Sainz de Baranda (independent), appointed on 27 June 2018.
- Mr. Claudio Santiago Ponsa, appointed on 27 June 2018.

3.2. Shareholders' Meeting

Any person who is a shareholder of record five days before the Shareholders' Meeting is entitled to attend the Meeting.

Attendance at the 2018 Shareholders' Meeting (%): 83.8%

Attendance at the Shareholders' Meeting %



3.3. Board of Directors

The Board of Directors of Naturgy operates via plenary meetings and committees, in accordance with the requirements of the Capital Companies Act. Accordingly, the Board of Directors of Naturgy has an Audit Committee and an Appointments and Remuneration Committee, whose functions are as set out in the Act.

Until 27 June 2018, the Board had an Executive Committee, which was responsible for deciding on the issues most closely related to operations over which the Board has competence. In the framework of the Action Plan implemented by the Board of Directors as a result of the self-assessment performed in 2017, the size of the Board of Directors and the existence of the Executive Committee were reconsidered in 2018. After the reduction of the number of members of the Board of Directors to 12, it was no longer considered necessary to maintain that Committee since the aforementioned number guarantees agility in the decision-making process.

In 2018, the Board of Directors undertook an in-depth debate on strategy which crystallised in the approval of the Business Plan 2018-2020.

The other main issues that were considered are as follows:

- Monthly, six-monthly and annual oversight and review of business performance.
- Approval of the accounts, and other actions required by accounting and/or securities market regulations.
- Budgets, finance plan, capital expenditure plan and other actions related to activities planning and to financial discipline.
- Efficiency plan.
- Examination of the Company's main risks and its control systems.

- Actions in connection with corporate governance: in addition to the normal reports (annual corporate governance report, annual report on remuneration, etc.), as a result of a performance assessment of the Board of Directors and its committees this year a Corporate Governance Action Plan was drawn up and approved, in line with best practices in the area of corporate governance. This resulted in material changes in this area, such as a review to simplify all corporate regulations, reduce the number of directors, and eliminate the Executive Committee.

- Notice of the Shareholders' Meeting, including the proposal to appoint new directors and a dividend proposal.

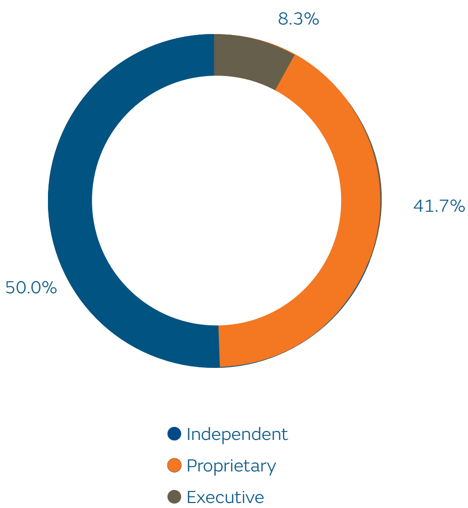
- Corporate Social Responsibility and health and safety issues.

Composition of the Board of Directors and its committees (at 31 December 2018)

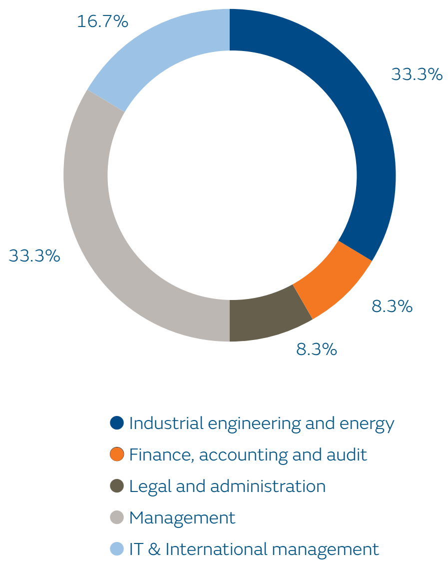
Board of Directors		Audit Committee	Appointments and Remuneration Committee	Category of director	Seniority on Board
Executive Chairman	Mr. Francisco Reynés Massanet			Executive	6/02/2018
Lead director	Mr. Ramón Adell Ramón	Director	Chairman	Independent	18/06/2010
Director	Mr. Enrique Alcántara-García Irazoqui	Director		Independent	18/06/2010
Director	Mr. Marcelino Armenter Vidal		Director	Proprietary	21/09/2016
Director	Mr. Francisco Belil Creixell	Chairman	Director	Independent	14/05/2015
Director	Ms. Helena Herrero Starkie	Director		Independent	04/05/2016
Director	Mr. Rajaram Rao	Director		Proprietary	21/09/2016
Director	Rioja Bidco Shareholdings, S.L.U., Mr. Javier de Jaime Guijarro		Director	Proprietary	18/05/2018
Director	Mr. Pedro Sainz de Baranda	Director	Director	Independent	27/06/2018
Director	Mr. Claudio Santiago Ponsa		Director	Independent	27/06/2018
Director	Theatre Directorship Services Beta, S.à.r.l., Mr. José Antonio Torre de Silva López de Letona	Director		Proprietary	18/05/2018
Director	Mr. William Alan Woodburn		Director	Proprietary	30/09/2016
Secretary (not a director)	Mr. Manuel García Cobaleda	Secretary (not a director)	Secretary (not a director)	N/A	29/10/2010

Board of Directors profile (%)

Type of Director



Skills



Board of Directors activities and performance

Number of meetings of the Board of Directors and its committees

	Board of Directors	Executive Committee	Audit Committee	Appointments and Remuneration Committee
2018	14	2	7	11
2017	15	3	10	5

3.4. Management structure

Following the appointment of Mr. Francisco Reynés Massanet as Executive Chairman on 6 February, the group's organisation structure was redesigned, including the elimination of the Executive Committee.

A new and simplified organisational structure was defined comprising four business units (Gas and Power, Infrastructure EMEA, Infrastructure South Latin America (LatAm) and Infrastructure North LatAm) and a leaner corporate structure was adopted, the goal being for the businesses to operate autonomously with full responsibility for their bottom line, leaving corporate functions to focus on value-added processes and on ensuring centralised control.

Senior Management is defined as meaning the executives who report directly to the Executive Chairman, Mr. Francisco Reynés Massanet. As of 31 December 2018, it comprised the following executives:

Business Units

Mr. Manuel Fernández Álvarez: Gas and Power.

Ms. Rosa María Sanz García: Infrastructure EMEA.

Mr. Antonio Gallart Gabás: Infrastructure South LatAm.

Mr. José García Sanleandro: Infrastructure North LatAm.

Corporate Units

Mr. Carlos J. Álvarez Fernández: CFO.

Mr. Antonio Basolas Tena: Strategy & Development.

Mr. Manuel García Cobaleda: Company Secretary and Secretary of the Board of Directors.

Mr. Jordi García Tabernero: Communication and Institutional Relations.

Mr. Antoni Peris Mingot: Resources.

Mr. Jon Ganuza Fernández de Arroyabe: Control.

Mr. Steven Fernández Fernández: Capital Markets.

Projects

Mr. José Mª Egea Krauel: PIPE project.

Mr. Miguel Aller: LEAN project.

3.5. Remuneration policy

Board of Directors

The annual report on director remuneration was presented as a separate item for a consultative vote at the Shareholders' Meeting in 2018.

Directors' remuneration for their membership of the Board and its committees consists solely of fixed amounts determined on the basis of the positions they hold.

The remuneration system was amended in 2018:

- On 6 February 2018, the Board of Directors adopted a material change in the Company's management and administration structure by approving the appointment of a new Executive Chairman and the resignation of the former Chairman and CEO, with the result that the contractual relationship with the previous CEO was terminated on 6 February.

- As part of the process of simplifying corporate governance, the Shareholders' Meeting on 27 June 2018 decided to reduce the size of the Board to 12 members and to abolish the Executive Committee, which resulted in a redistribution and overall reduction of the directors' remuneration for performing non-executive functions.

- In accordance with the provisions of article 9 of the Bylaws and in the framework of the approval of the Business Plan by the Board of Directors on 27 June 2018, the Board resolved, at a meeting on 31 July, to replace the pre-existing multi-year variable remuneration system with a long-term incentive which, since it requires the approval of the Shareholders' Meeting, is subject to the condition precedent that it be authorised by the 2019 Shareholders' Meeting.

These decisions were adopted by the Board of Directors following recommendations in this connection by the Appointments and Remuneration Committee; external legal advice was obtained for the implementation of the new long-term incentive plan and its submission to the Shareholders' Meeting.

Remuneration for membership of the Board of Directors and its committees (€/year):

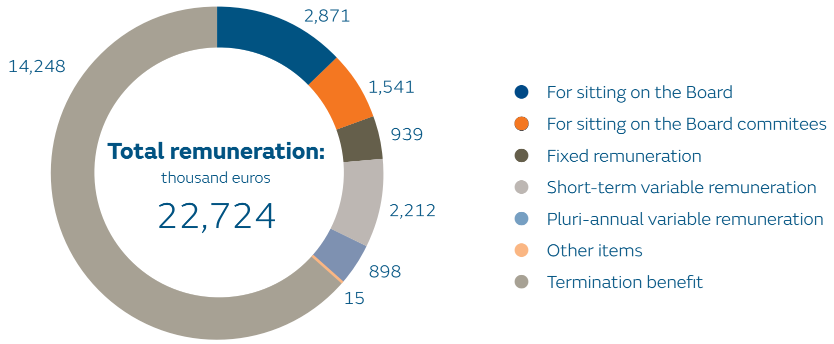
	From 27 June 2018	Up to 27 June 2018
Chairman of the Board of Directors	1,100,000	550,000
Director	175,000	126,500
Lead director	30,000	30,000
Committee chairman	90,000	-
Committee member	60,000	-
Chairman of the Executive Committee	Not applicable	550,000
Member of the Executive Committee	-	126,500
Member of the Appointments and Remuneration Committee	-	25,000
Member of the Audit Committee	-	40,000

Following those changes, the remuneration policy for the Executive Chairman, in respect of his executive functions, is based on the following:

Item	Objective	Criteria
Fixed remuneration annual basis	Remunerate the level of responsibility attached to these functions.	Ensure that the remuneration is competitive vis-à-vis comparable companies.
Annual variable remuneration	Link remuneration with the company's performance in the short term.	Based on 100% of the total fixed annual remuneration, multiplied by the degree to which the goals were actually achieved in the year. Achievement is capped at 150%. No remuneration is payable if goal achievement is less than 80%. The goals and weightings are expected to be established by the Board of Directors at a meeting on 5 March 2019.
Long-term incentive plan	Strengthen the commitment to achieving the goals set out in the strategic plans.	Related to the return obtained by shareholders in the period of reference, which coincides substantially with that of the Business Plan 2018-2022.
Other items	Safeguard the company's benefits.	Health, life insurance and disability. Energy rebate, company vehicle.

The remuneration is supplemented by pension plans and a group health insurance policy.

Total remuneration earned by the Board of Directors in 2018, by type (Euros '000)**:**

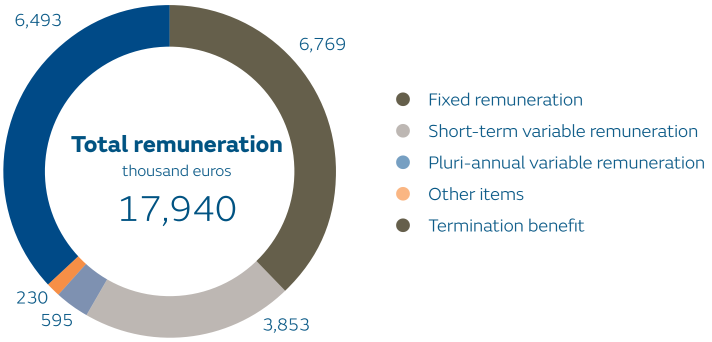


Senior Management

The general remuneration policy for Senior Management is determinated by the Board of Directors on the basis of a proposal by the Appointments and Remuneration Committee.

The remuneration model contains the same components as above for the Executive Chairman's executive functions.

Total remuneration earned by the Management Committee and head of Internal Audit[1] in 2018, by type (Euros '000)



1. In accordance with CNMV Circular 5/2013, for the purposes of remuneration, senior management includes executives who report directly to the company's chief executive and also the head of internal audit.

4. Forecast Group performance

4.1. Foundations of strategy

The new Business Plan 2018-2022, unveiled in London on 28 June 2018, establishes the group's business model, which is focused on value creation.

Naturgy is focused on responding to its own industrial model, based on:

- Treating the energy transition as an opportunity.
- Being a flexible, competitive company.
- Transforming via digitalisation.
- Placing the customer at the centre of the model.

Treating the energy transition as an opportunity

Naturgy believes that natural gas and renewable energies will play a very important role in the transition to energies that produce lower CO_2 emissions, as needed to meet the targets set in the 2015 Paris Agreement on climate change.

As a result, the following lines of action have been established:

- Triple renewable installed capacity by 2022
- Leverage Naturgy's lead in combined cycle plants and in the global LNG market

- Develop the use of natural gas in transportation
- Develop renewable gas

Moreover, Naturgy's infrastructure assets will play a vital role over the next few years in the process of electrification and improvement of energy efficiency, supporting greater electrification and greater penetration by gas in countries where the company already operates.

Being a flexible, competitive company

Solid, tangible levers have been defined for achieving the efficiency goals set out in the Business Plan:

- Organisation: the businesses will be autonomous units with full responsibility for their results, while seeking to optimise company personnel. To this end, a number of changes have been implemented at the organisational level in both corporate governance and the organisational structure in order to facilitate decision-making and the business units' autonomy and responsibility, while always guaranteeing control by the parent company.
- Process re-engineering: reviewing service contracts with suppliers, establishing new cooperation relations with suppliers where necessary to achieve automation or outsource non-core tasks.
- Asset management: search for best practices to optimise asset maintenance based on predictive models and centres of excellence.

Naturgy presented an efficiency plan and undertook to cut annual operating expenses by Euros 500 million by 2022.

Transforming via digitalisation

The following key levers for digitalisation have been defined for 2022:

- Customer relations: 75% of services to be provided via digital channels and 20% penetration via Internet of Things (IoT).
- Processes and operations: Over 80% automation of internal processes and operations.
- Remote control of assets: Achieve 80% coverage of assets with sensors and remote control by 2022, from 56% in 2017.
- Advanced analysis techniques: Data-driven management to be implemented in over 90% of processes Group-wide. The main projects to be undertaken in this connection will be in the following areas: develop predictive models for asset maintenance; use models to pursue customer segmentation, predict churn and apply advanced pricing approaches.

These projects will drive the Group's transformation via digitalisation.

Placing the customer at the centre of the model

Enhance our commitment to the customer by placing them at the centre of Naturgy's strategy based on:

- A single customer experience model
- Defining services and solutions that provide added value to the customer
- Improve customer segmentation
- Innovation and digitalisation

Key factors in this connection are technological innovation such as smart apps, smart meters, remote control, autoproduction of electricity, energy storage, etc.

4.2. Value creation

The main objective of the new Business Plan 2018-2022 is to guide the company towards value creation and lay the foundations for the Group's new industrial model. Naturgy's commitment to value creation is underpinned by four basic pillars: simplicity and accountability, optimisation, discipline in investment, and shareholder remuneration.

Simplicity and Accountability

1. Corporate governance and organisation structure

In terms of corporate governance, a major change was the reduction in the number of members in the Board of Directors from 17 to 12 (the executive chairman, six proprietary directors and five independents). Internal governance rules will also be simplified to achieve a more efficient structure and to make decision-making more agile.

The organisation structure has been simplified into four business units (Gas and Power, Infrastructure EMEA, Infrastructure South LatAm and Infrastructure North LatAm), with leaner corporate functions in order to ensure that the businesses operate autonomously and with full responsibility for their results, enabling the parent company to focus on value-added processes and on ensuring centralised oversight.

A new Opex & Capex Committee was created with the task of ensuring the execution of the company's efficiency plan and for fulfilling the discipline in capital expenditure envisaged in the Business Plan.

With these changes, Naturgy has simplified its corporate governance to streamline decision-making and redesigned its organisational structure to attribute greater autonomy and responsibility to the individual businesses.

2. Strategic positioning

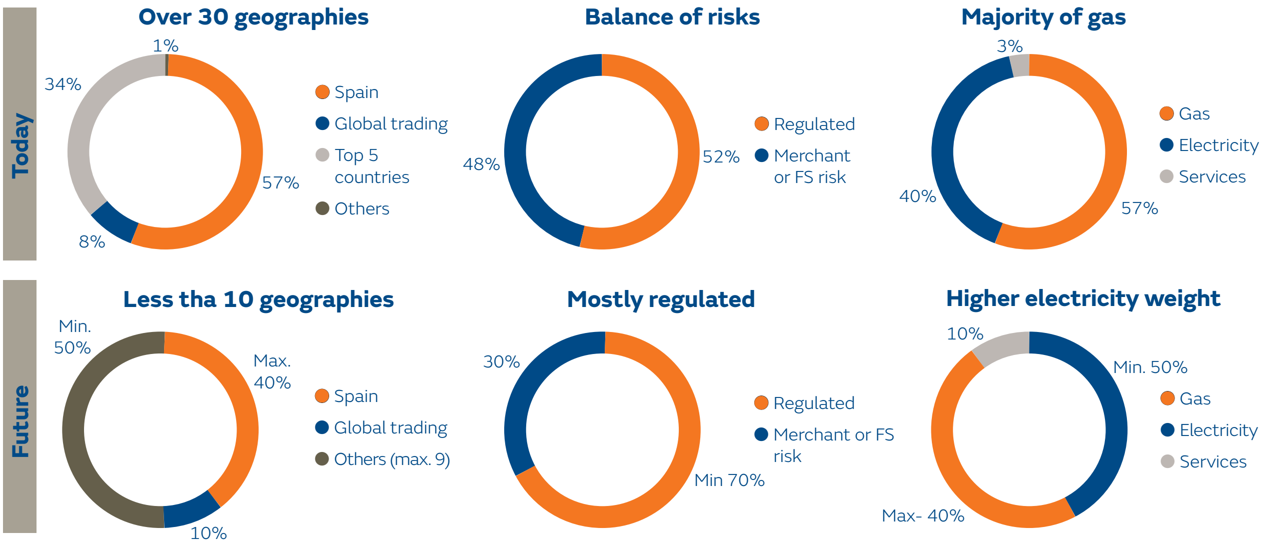
Naturgy defines its strategic positioning on the basis of the following criteria:

	Where to invest	Where to divest
Markets	• Big markets with strong growth potential. • Where Naturgy has a significant market share or critical mass. • That offer legal certainty. • Stable macroeconomic environments (e.g. the EU, North America, OECD).	• Markets that are small and/or offer little growth potential. • High regulatory risk. • Highly concentrated. • Volatile macroeconomic environments.
Businesses	• Electricity or gas grids. • Sale of electricity under contract. • Customer services. • Controlling stakes.	• Low level of integration or synergy with the rest of the Group. • Unhedged volatility. • Non-controlling stakes.
Profitability	• Above hurdle rate.	• Out of hurdle rate.

A total of Euros 5.3 billion of expenditure in growth capex have been identified, and Euros 300 million are expected to be realised through divestments in addition to those already performed.

Naturgy will also work to balance the weight of its businesses in its mix of activities and will be more ambitious to increase the contribution by regulated activities and by electricity. In the future, the company expects that at least 70% of its business will be linked to regulated activities (currently 52%), with half related to electricity (currently 40%). It also expects to increase exposure to services to about 10%, reinforcing its commitment to the customer.

Simplicity and Accountability



Rebalancing of portfolio: more cash flow visibility and lower volatility

Additionally, on the basis of developments in the markets where it operates and in line with the assumptions and foundations of the new Business Plan, Naturgy reviewed the value of its assets, which resulted in a one-time impairment in the amount of Euros 4,851 million before taxes, booked in 2018. This impairment had no impact on shareholder remuneration and it will be accretive from 2019 because of the lower depreciation charge.

Optimisation

Financial strategy will focus on reducing Opex, optimising Capex and applying strict discipline in investments, pursuing organic development.

Under the Business Plan 2018-2022, the company will continue to optimise the businesses with additional efficiency measures, with the commitment to cut annual operating expenses by Euros 500 million in 2022. These efficiencies will be focused on an analysis of the company's non-core activities and on the assignment of the operational functions within each of the business units, all supported by the ongoing digitalisation processes.

Naturgy plans to cut group-level capex by Euros 200 million per year with respect to the average in 2015-2017, while increasing the percentage of investment allocated to organic growth in comparison with previous years. In average terms, the goal is for 63% of capital expenditure to be allocated to growth in 2018-2022 vs. an average of 54% in 2015-2017.

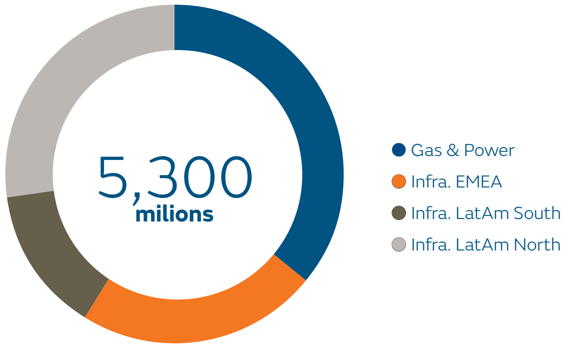
Disciplined investment

Four golden rules were defined to ensure value creation and profitable growth in both organic and inorganic investments:

1. Establishment of a hurdle rate of return, setting minimum profitability targets for businesses, activities and countries so as to ensure value creation.
2. A clear positioning focused on target markets and businesses.
3. Industrial leadership via controlled subsidiaries.
4. Risk management, minimising the volatility of commodity prices and exchange rates.

Applying these rules, Naturgy plans to invest Euros 8.4 billion over the next five years, of which Euros 5.3 billion will be allocated to growth, increasing the proportion of growth capex to 63% of the total in the period:

Growth capex by business (€M)



Fully identified growth capex

Financial discipline will enhance free cash flow so as to sustain attractive shareholder remuneration.

Shareholder remuneration

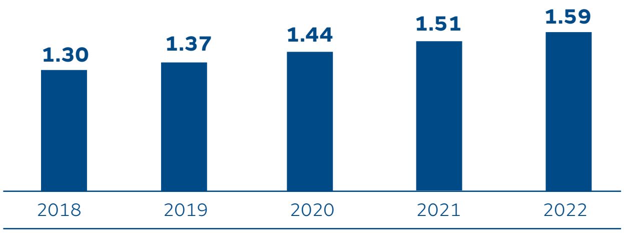
The company will increase the dividend charged to 2018 earnings by 30% to Euros 1.30 per share.

Under the Business Plan 2018-2022, Naturgy made a commitment to its shareholders to increase the cash dividend by at least 5% per year until the end of the period and to pay dividends in three instalments:

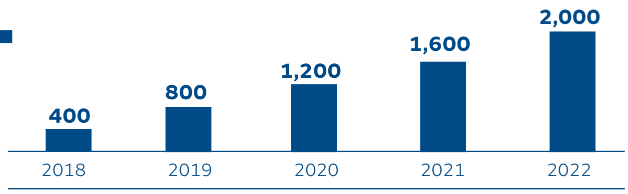
1. at the end of the first half of the year (20% of the total dividend)
2. at the end of the third quarter (35%)
3. after the Shareholders' Meeting (the remaining 45%)

To reinforce the new shareholder remuneration policy, in the event that the company cannot find inorganic investments that meet the hurdle rate, it can allocate a maximum of Euros 2 billion to buying back own shares, capped at Euros 400 million per year.

Dividends (€/share)



Share buy-back (Up to €2,000M)



4.3. Individual business prospects

Naturgy's key financial targets for 2022 are as follows:

Key financial targets for 2022 (milons of euros)

Ebitda
~5,000
2017: **3,915**

Net income
~1,800
2017: **1,360**

Annual avg. FCF
~1,800
2017: **1,300**

Net debt
~16,400
2017: **16,400**

The business goals set in the Business Plan are summarised below:

	Gas & Power	Infr. EMEA	Infr. LatAm South	Infr. LatAm North
Asset base 2018	~9,200	~9,800	~7,300	~1,500
EBITDA 2022	~1,700	~1,600	~1,200	~400
Total capex 18-22	~2,700	~2,300	~2,300	~1,000

The growth prospects for the individual businesses, as defined in the Business Plan 2018-2022, are as follows:

Gas & Power

The Business Plan 2018-2022 targets EBITDA of Euros 1.7 billion per year, with capex amounting to Euros 2.7 billion in the period 2018-2022. This will be driven by organic growth and higher efficiency in exploiting assets. The goals and opportunities defined for each of the units in this business are as follows:

	Opportunities	Goals (EurosM)
Gas, power and services sales	• Define a new integrated commercial model • Maximise value by focusing on customers. • Exploit the strong growth potential of the services and solutions business.	EBITDA 2022 = 549 Capex 18-22 = 452 74% growth capex
International LNG	• Diversified, flexible portfolio of procurement contracts. • Sales secured under contract with end customers. • Entry into attractive new markets, such as the Floating Storage Regasification Unit (FSRU), small-scale solutions and bunkering.	EBITDA 2022 = 422 Capex 18-22 = 392 100% growth capex
European Power Generation	• Double the volume of renewable energy while cutting total costs. • Increase CCGT load factor. • Adjust cost of conventional generating fleet.	EBITDA 2022 = 507 Capex 18-22 = 1.296 64% Growth capex
International generation	• Expand in renewables. • Generate recurring cash flow.	EBITDA 2022 = 270 Capex 18-22 = 568 68% growth capex

Infrastructure EMEA

The EBITDA target for this business is around Euros 1,645 billion, with capex in the period 2018-2022 totalling about Euros 2,310 billion. The goals and opportunities defined for each of the units in this business are as follows:

	Opportunities
Spain gas networks	• Pursue organic growth by exploiting the scope for expanding gas penetration. • Limit the business's regulatory risk. • Increase efficiency via digital transformation.
Spain electricity networks	• Work towards a more flexible, digitalised distribution system. • Future capex to offset regulatory risks. • Pursue efficiency via digitalisation.
EMPL	• Revenues guaranteed until the concession expires (2021). • Negotiations advancing to renew Maghreb-Europe gas pipeline concession.

Infrastructure South LatAm

The EBITDA target for this business is around 1.2 billion, with total capex of about Euros 2.3 billion in the period 2018-2022. The goals and opportunities defined for each of the units in this business are as follows:

	Opportunities	Goals (EurosM)
Chile Electricity	• Distribution: the regulatory model is expected to improve in 2020 to capture updates in technology and service quality. • Transmission: improvements expected due to grid upgrades and new regulations to address the bottleneck produced by the growth of renewable energy.	EBITDA 2022 = 436 Capex 18-22 = 1,105 60% growth capex
Chile Gas	• Organic growth via greater penetration and higher demand for heating. • Drive gas exchanges between Argentina and Chile via existing pipelines.	EBITDA 2022 = 245 Capex 18-22 = 497 85% growth capex
Brazil Gas	• Organic growth through increasing penetration in the gas market as well as seeking new concessions. • Leverage the huge growth potential of the services business.	EBITDA 2022 = 322 Capex 18-22 = 399 57% growth capex
Argentina Gas	• Organic growth underpinned by grid upgrades and implementation of new networks, expanding the grid in the territory. • Leverage the huge growth potential of the services business.	EBITDA 2022 = 159 Capex 18-22 = 323 41% growth capex

Infrastructure LatAm North

The EBITDA target for this business is around Euros 400 million, with capex totalling about Euros 1 billion in the period 2018-2022. The goals and opportunities defined for each of the units in this business are as follows:

	Opportunities	Goals (EurosM)
Mexico Gas	• Organic growth through greater penetration in the gas market and new concessions. • Strong growth potential in services via new customers and the existing customer base.	EBITDA 2022 = 247 Capex 18-22 = 616 22% growth capex
Panama Electricity	• Strong growth is projected against a backdrop of moderate risk to the country's economy, with remuneration stable in USD. • The tariff review for 2019-2022 is expected to be positive. • Significant improvement in operational efficiency and lower power losses. • Capture competitive advantages in services and solutions.	EBITDA 2022 = 146 Capex 18-22 = 341 30% growth capex

4.4. Financial strategy

To support the business strategy, the finance strategy targets net debt at end-2022 at the same level as end-2017 (Euros 16.4 billion, per IFRS 16) as strong cash flow will make it possible to distribute dividends (Euros 6.9 billion) and allocate Euros 2 billion to share buybacks or inorganic growth opportunities.

Finance policy will focus on maintaining the rating and leverage while managing the debt structure to make it more effective. The debt structure will be diversified, prioritising access to capital markets and institutional funds, with at least 70% of debt at fixed cost while seeking "natural" hedges by ensuring that subsidiaries are funded in the currency in which they generate cash flows.

Each business unit will be provided with the necessary liquidity and the necessary level of indebtedness to operate autonomously.

5. Sustainable innovation

Naturgy views innovation as the function that enables it to guide and drive the necessary developments, access them and apply them effectively in pursuit of its objectives. It recognises that properly orienting, implementing and applying strategic innovation are vital to obtaining competitive advantages in the markets and achieving sustainable development of its activity.

Consequently, the company applies an innovation model that is aligned with the businesses and contributes to the objectives of the Strategic Plan, it monitors developments outside the plan and anticipates disruptions in the energy model that may change the rules of the game. It does this through a solid culture of innovation, with open collaboration initiatives, intrapreneurship programmes and other tools to promote innovation.

Innovation vision

The company's innovation function continues to be based on 5 major building blocks:

- Social Innovation, working to mitigate situations of energy vulnerability since 2014 through preventative measures, agreements with local and regional governments, and awareness-raising activities, including participation in forums and round tables on poverty. As part of the Vulnerability Plan, a number of measures were stepped up in 2018: the Solidarity Fund for Energy Rehabilitation and the Social Employment Program.

- Innovation in Marketing. This area includes all the company's efforts to get to know its customers' actual specific needs, and to ensure that they have access to cutting-edge products that make their everyday lives easier. A major ongoing initiative is the CeX (Customer Experience) project, under which the company is applying a new methodology that is primarily customer-centric. The principal project in 2018 was the Clear Communication Project, the goal being to convey relevant information to customers in a clear and simple form.

- Innovation in Organisation. This area refers to actions aimed at meeting emerging needs with respect to new business models, resulting in a new work organisation and steps to minimise risks and increase quality and safety within the organisation's practices.

- Product Innovation. The FutureSisens Project provides smart flow monitoring in renewable gas plants. In particular, the project aims to develop flow sensors that are energy-autonomous or use very little energy and are capable of measuring flows in natural gas distribution networks (medium and low pressure).

- Process Innovation. A notable project in this area was the optimisation of the hydroelectric generating fleet by applying machine learning in combination with traditional optimisation approaches, as well as cloud computing solutions, in models for operating the hydroelectric generation fleet in the electricity market. The goal is to achieve more advanced analytical models in an AWS environment that allow for growth in revenues by detecting and seizing new market opportunities within a process of continuous improvement.

In 2018, a total of Euros 63 million were spent on innovation (Euros 99 million in 2017), as indicated below:

(million euro)	2018	2017
Investment in innovation	63	99

Innovation Plan

The innovation plan is structured through four strategic innovation areas: Energy Transition, Digitalisation, Customer-Centric and New business models, within which the following priorities were defined:

Sustainable mobility

Naturgy identifies sustainable mobility as a key component of strategic innovation within its positioning in environmentally friendly energies. As a leading energy company, it will play a fundamental role in the process of transforming mobility models, where renewable natural gas and electricity are the main vectors.

In 2018, we have developed the COFAST project, which consists of a new standardised integrated solution for fast charging stations for electric vehicles. The electricity for the charging stations will be supplied by small-scale natural gas-fired cogeneration plants.

Smart Client

In the Smart Client area, Naturgy is committed to the digital transformation of its customers as the key to achieving the objective of evolving our energy model towards a more efficient, decarbonised and decentralised one in which the concept of consumer will evolve towards a more active role in which their participation makes it possible to achieve those goals. The new active consumer will focus on three axes: distributed generation and autoproducer solutions, digital solutions and IoT products, and data analytics, making it possible to enhance customer segmentation and get to know customers better in order to offer them personalised recommendations, products and services, and also to optimise asset efficiency and operations. One of the most notable projects in 2018 was GrowSmarter, an IoT solution for residential customers, and a pilot test of a number of photovoltaic and energy storage solutions for residential and tertiary customers has begun.

In the area of Energy Efficiency Solutions, activities focused on the development of new integrated energy solutions, based on high-efficiency renewable technologies, that can be designed and operated optimally (in both energy and monetary terms) for the development of Near-Zero Energy Buildings. One of the projects in 2018 was ReUseHeat, which aims to demonstrate heat recovery technologies in urban environments; Naturgy implemented a pilot project at a hospital in Madrid.

Distributed generation and autoproduction

The purpose of the distributed generation and autoproduction line in 2018 was to create tools and resources to support the development of products based on photovoltaic generation and batteries for end customers, as well as projects such as Growsmarter. Apart from technological developments in the field of photovoltaics and batteries, Naturgy's main contribution in this connection is its vision of the customer, which is a key element when designing control systems that maximise the value to be extracted from these solutions.

Accordingly, it continues to pilot-test commercial solutions in the Autoproduction Laboratory. The goal is to provide the business with technical and economic information about new products that are available in the market. To this end, a cost/benefit analysis methodology has been developed that uses simulation tools developed in-house, such as GENPER and OBAMA, as well as laboratory tests to measure the benefits for specific customer categories. In cooperation with manufacturers and the IREC technology centre, the laboratory also developed an energy manager for Naturgy to optimise battery usage that is compatible with a number of commercial solutions.

Renewables and storage

Naturgy is committed to a balanced energy mix in the group's assets, in which emission-free technologies account for a growing share of its total installed capacity. Innovation in this area focuses on three main lines of action:

- Storage solutions, which facilitate greater grid integration of intermittent renewable electricity, oriented towards further enhancing the quality and reliability of the supply.
- Advanced management of generation facilities (wind, hydroelectric, solar): with initiatives for smart monitoring of assets, application of new technologies for environmental oversight and security, better communication and remote monitoring systems, predictive tools, etc.
- Evaluation of new renewable generation technologies: marine, offshore wind, geothermal, gas-renewable hybridisation, etc.

One of the projects implemented in 2018 was the continuation of activities at the PV Photovoltaic Solar Laboratory in Durango (Mexico), where photovoltaic modules, structures and associated equipment are pilot-tested in order to analyse, monitor and optimise key operational parameters and indicators.

Renewable Gas and Liquefied Natural Gas

As part of Naturgy's commitment to evolve towards a low carbon economy, the company has been working for several years to promote renewable gas by participating in a number of projects, both in Spain and elsewhere in Europe, whose objective is to obtain renewable natural gas from renewable resources, and apply processes to obtain gas of a sufficient quality for injection into the natural gas grid so that it can be used for industrial, mobility, residential and power generation applications. Implementing these innovation projects makes it possible to study how the available technologies work, identify their advantages, and develop new technologies so as to optimise and reduce their production costs.

The company also continues to pursue innovation projects in the area of Liquefied Natural Gas (LNG), with a focus on three lines of action: optimisation of the LNG logistics chain (small scale), development of LNG as a cleaner, more efficient fuel for transport (bunkering), and development of LNG metering.

Some of the principal projects in this area are the Renewable Gas Unit, a joint project of Naturgy and EnergyLab in cooperation with the Bens waste water treatment plant, which has resulted in the commissioning of a biogas upgrading plant located at the WWTP, in order to produce biomethane; and Life Methamorphosis, in which the company developed and implemented the Methagro business line to produce high quality biomethane from agro-industrial waste and other organic waste materials.

Advanced asset management

The goal of this innovation effort is to maximise asset performance using advanced data analysis and new operational strategies in order to:

- Increase asset efficiency, reliability and flexibility.
- Identify new strategies for the optimised asset exploitation.
- Optimise maintenance in the field.

Using new technologies to not only avoid assets' obsolescence but also incorporate new elements that enhance their competitiveness and capacity to generate value in a highly complex environment.

During 2018, the GALA project focused on advanced control of overhead power lines (high voltage and medium voltage) in order to optimise and improve the periodic examinations required by regulation and establish an optimised felling and pruning plan for 2020.

6. Non-financial statement

This Non-financial statement information was drawn up in line with the requirements of Act 11/2018, of 28 December, on non-financial disclosures and diversity, approved by the Spanish Congress on 13 December 2018, which amends the Commercial Code, the consolidated text of the Capital Companies Act approved by Legislative Royal Decree 1/2010, of 2 July, and Act 22/2015, of 20 July, on Auditing, in connection with non-financial disclosures and diversity (from Royal Decree-Act 18/2017, of 24 November).

It was drafted on the basis of the Sustainability Reporting Guidelines issued by the Global Reporting Initiative (GRI), which also serve as a reference for drafting the Corporate Responsibility Report that is published each year and which, this year, complements and elaborates upon these non-financial disclosures.

In this context, through the non-financial disclosures, Naturgy seeks to provide information on environmental, social, personnel human rights issues that are germane to the company in the pursuit of its business activities.

The content of this report was selected and drafted on the basis of the outcome of the materiality analysis carried out at the beginning of 2018 (See Annex III, About this Report).

For each question set out in the Act, the materiality for the company, the policies and risks associated with each one, and the benchmark indicator used for monitoring and evaluating it are set out below.

6.1. Business model and value creation

6.1.1. Business model

Naturgy is an integrated energy group supplying gas and electricity to almost 18 million customers. It focuses on the gas distribution and supply and on generating, distributing and supplying electricity. It also operates other business lines, such as energy services, which enhance the diversification of activities and revenues, staying at the forefront of new market trends, meeting customers' specific needs and offering them an integrated service not confined to selling energy.

Naturgy's mission is:

To meet the needs of...	With vision...	Based on our values
Our shareholders	Offering increasing sustainable profitability	> Commitment to results > Customer-oriented > Sustainability > Interest in people > Social responsibility > Integrity
Our customers	Being leaders in continuous growth and with a multinational presence, offering high-quality products that respect the environment	
Our employees	Offering opportunities for professional and personal development	
Society	Contributing positively through a commitment to global citizenship	

Naturgy's business model is implemented through a number of companies in Spain, elsewhere in Europe, and in Latin America and Africa, and is underpinned by the following main businesses:

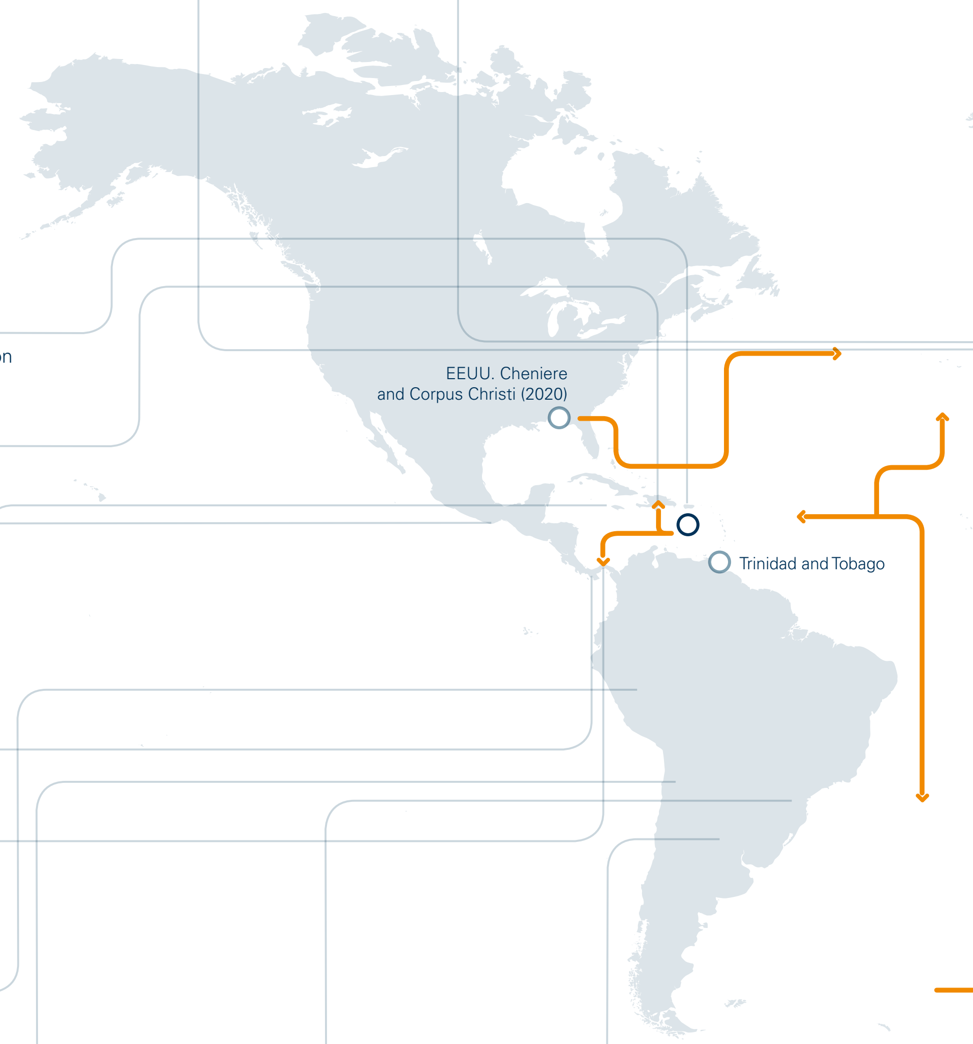
Gas & Power	34% of EBITDA: Spain, Europe and Latin America
Infraestructures EMEA	45% of EBITDA: Spain and Africa
Infraestructures Latam South	20% of EBITDA: Latin America
Infraestructures Latam North	6% of EBITDA: Latin America

Note: -5% other activities

Worldwilde presence

Portugal
NG/LNG and electricity commercialisation.

Spain
Exploration, transportation, distribution and commercialisation of gas and electricity. Generation (combined cycles, nuclear, hydraulic, coal, co-generation, mini-hydraulic and wind).



Puerto Rico
NG/LNG (regasification plant) infrastructure and generation of electricity.

Dominican Republic
Generation (198 MW, fuel-oil).

Mexico
Gas distribution (ten states including Mexico City and 1.8 Mn customers) and generation (2,289 MW, combined cycles and 234 MW, wind).

Jamaica
NG/LNG commercialisation.

Costa Rica
Generation (101 MW, hydraulic).

Panama
Electricity distribution (Panamá Central, West, Inland, Chiriquí and 0.7 million customers) and generation (22 MW, hydraulic).

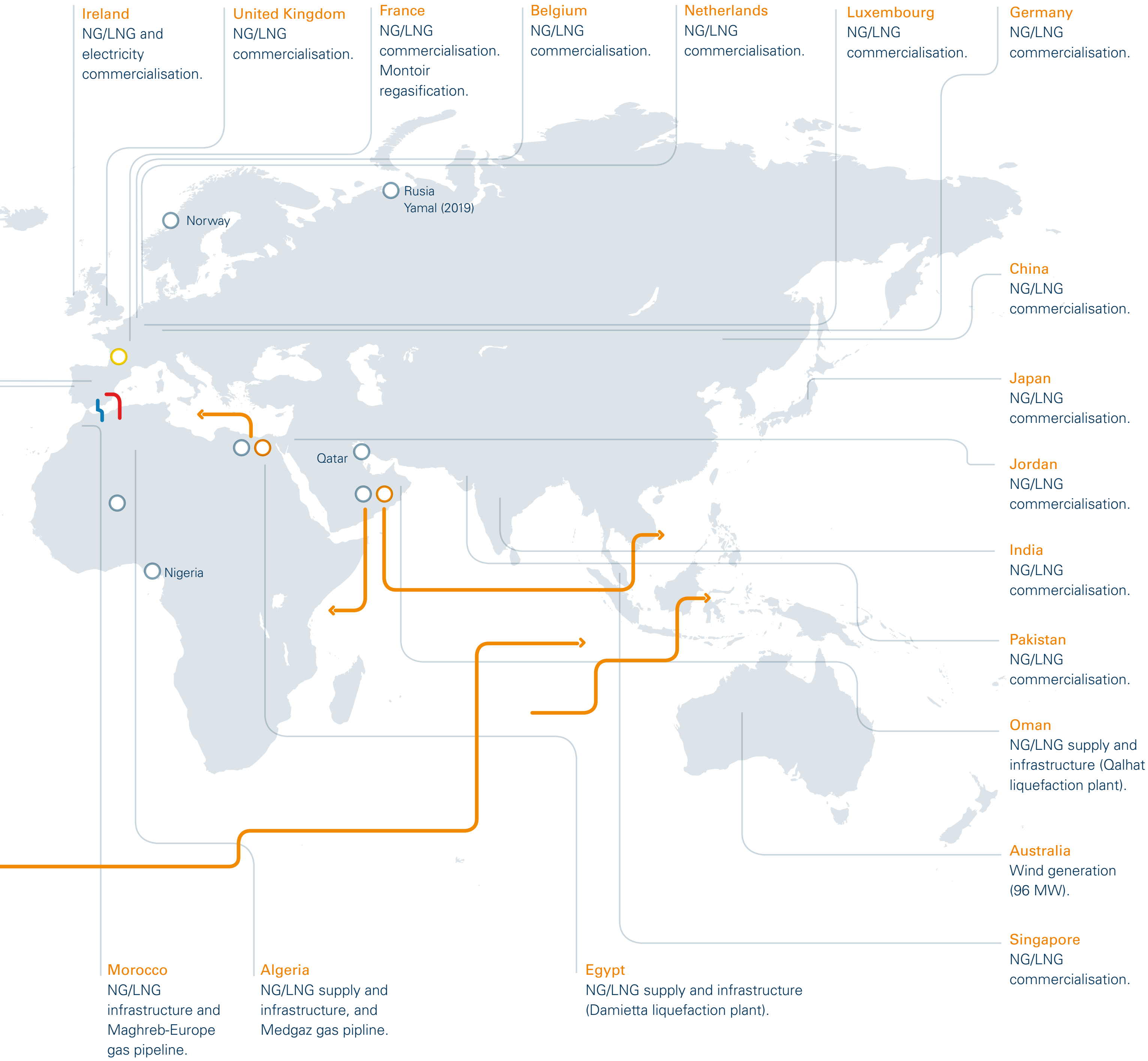
Peru
Gas distribution (Arequipa).

Chile
Gas distribution (18 provinces and 0.6 million customers), electricity distribution and transportation (13 provinces and 2.9 million customers). Wind and solar generation projects.

Brazil
Gas distribution (Rio de Janeiro state, São Paulo South and 1.1 million customers). NG/LNG commercialisation and generation (153 MW solar).

Argentina
Gas distribution (30 municipalities in the north and west of the province of Buenos Aires, 1.7 million customers) and electricity distribution (0.2 million customers).

- Gas flow.
- Maghreb-Europe gas pipeline (Empl).
- Medgaz gas pipeline.
- Liquefaction plant.
- Regasification plant.
- Leased regasification plant.
- Long-term gas contracts.



NB: Does not include the power distribution business in Colombia as the stake in Electricaribe ceased to be consolidated as at 31/12/2016 nor in the gas distribution in Italy and Colombia, electricity distribution in Moldova, electricity generation in Kenia and mining in South Africa business because they have been reclassified to discontinued operations.

Throughout the value chain, Naturgy's business model stands apart as a leader in the gas sector and a key player in the electricity sector, in both cases ensuring a regular supply of gas and electricity, which is essential to providing a quality service and fulfilling the company's social mission; providing a broad range of value-added services and fostering sustainable innovation to drive development.

Business lines

Leadership in the gas business

	Networks	Gas		
	Gas distribution	**Infrastructures**	**Procurement**	**Supply**
	10.6 million distribution connections 119,998 km of network	Eight LNG carriers Two transportation pipelines, Maghreb-Europe (EMPL) and Medgaz	~ 30 bcm supply portfolio	378 TWh of gas supplied
Our positioning	**Spain** Leader in Spain with a 69% market share, distributing natural gas to more than 1,000 municipalities in nine autonomous regions and 5.4 million customers. **Latin American** Latin America's top distributor, catering for more than 5.2 million customers. Presence in Argentina, Brazil, Chile, Mexico and Peru and in six of the ten largest Latin American cities.	Eight LNG carriers (1.3 Mm^3) Management of the main gas pipeline supplying the Iberian Peninsula, the Maghreb-Europe pipeline (EMPL), and a 14.9% interest in the Medgaz pipeline. Interest in one regasification plant (Ecoeléctrica) and two liquefaction plants (Damietta and Qalhat). Proprietary storage capacity of 0.5 bcm and leased capacity of 1 bcm.	Business model based on the diversification and flexibility that have made Naturgy a global operator with a strong international profile. Naturgy has procurement contracts with suppliers worldwide, both in a gaseous state (NG) and in the form of liquefied natural gas (LNG).	Unique access to markets: almost 11 million customers and LNG sales in numerous countries worldwide. A global operator with the flexibility to tap markets offering attractive margins. 39% market share in Spain. Competitive supply to combined cycle plants (CCGT).
Our strength	Naturgy has an outstanding position in the markets where it operates, affording it an platform for organic growth, in terms both of attracting new customers in municipalities with gas and of expanding networks to areas without gas.	Naturgy has an integrated gas infrastructure aimed to afford the business considerable stability, making its operations more flexible and enabling it to transport gas to the best business opportunities. Its storage capacity is seeking to ensure a constant supply, avoiding the impact of seasonal fluctuations or peaks in demand.	Its diversified procurements portfolio enables it to tap value-added markets.	Naturgy has a diversified portfolio of end customers, and supplies gas both in Spain and internationally. Its positioning in international markets is seeking to obtain higher margins through trading. Naturgy is a leader in dual fuel supply and it offers a broad range of value-added services.

Standard-bearer in the electricity business

	Networks	Electricity	
	Electricity distribution	**Generation**	**Supply**
	7.6 million supply connections 215,532 km of network	15.6 GW of power generation capacity	35.4 TWh supplied
Our positioning	**Spain** The third-largest operator in the Spanish market, where it distributes electricity to 3.7 million customers. **Latin America** Presence in Argentina, Chile and Panama (3.8 million customers).	**Spain** Capacity of 12.5 GW, with a significant presence in five technologies: 7 GW CCGT, 2 GW hydroelectric, 1.7 GW coal, 1.2 GW renewable and 0.6 GW nuclear power. Naturgy has a market share of 17.4% in non-renewable generation and 2.1% in renewable generation. **International** Capacity of 3.1 GW: 2.3 GW CCGT (Mexico), 0.2 GW oil-fired (Dominican Republic), 0.1 GW hydroelectric power (Costa Rica and Panama) and 0.5 GW renewables (Mexico, Australia and Brazil).	Leader in the mainstream consumer and residential segments, with a total market share of 14.0% in Spain. One of the main traders in the Spanish market. A dual supply and a broad range of value-added services.
Our strength	Naturgy is a leader in the markets where it operates. Naturgy is one efficient operator in terms of operation and maintenance costs in the electricity distribution business.	The company has considerable know-how in the generation technologies that operates and its infrastructure can adapt to the needs of each energy model and to the reality of each country. The company's good positioning in Spain and Latin America will enable it to make the best of investment opportunities in generation.	Being a leader in the combined supply of natural gas and electricity affords the company major advantages, such as lower service costs, integrated customer care and lower acquisition costs, not to mention greater customer loyalty.

6.1.2. Value creation and sustainable management

The long-term commitment to value creation and sustainable management is specified in the Corporate Responsibility Policy, which provides the common framework for action that guides the company's socially responsible conduct; it was approved and updated by the Board of Directors in December 2015, based on international best practices and the recommendations enshrined in the Code of Good Governance of Listed Companies.

This policy undertakes eight commitments to the company's stakeholders:

1. Commitment to results.
2. Service excellence.
3. Responsible environmental management.
4. Interest in people.
5. Health and safety.
6. Responsible supply chain.
7. Social commitment.
8. Integrity and transparency.

These commitments are horizontal and are present throughout the company's business process, based on the generation of economic, social and environmental wealth.

Naturgy has all the essential kinds of capital with which to develop its business model, which is based on the responsible and sustainable management of all the resources it uses.

	Financial	Human	Manufactured	Environmental	Social
Our capitals	▪ Sustainable cash generation. Free cash flow = €3,054 M ▪ Strict financial discipline. Leverage = 48.4%	▪ Professional development and talent management. ▪ Diversity and equal opportunities. ▪ Extending principles to supplier chain.	▪ Investment and maintenance in gas and electricity distribution networks. ▪ Sustainable innovation. ▪ Operation development of electricity production capacity.	▪ Environmentally-friendly products and services. ▪ Energy efficiency. ▪ Undertaking to reduce emissions.	▪ Relations and dialogue with stakeholders. ▪ Guarantee of supply.

External environment

For further information on the strategic planning cycle, please see the “Forecast group performance” chapter, page 92.

- Economic environment.
- Regulation.
- Environmental policies.
- Technological developments and new business models.

Internal environment

Corporate Governance

Our commitments

- Commitment to results.
- Service excellence.
- Responsible management of the environment.
- Interest in people.
- Health and safety.
- Responsible supply chain.
- Commitment to society.
- Integrity and transparency.

	Financial	Human	Manufactured	Environmental	Social
Our results	▪ Dividends policy. Pay out: €1,400 M ▪ Meeting financial targets. Ordinary Ebitda: €4,413 M Ordinary net profit: €1,245 M	▪ Corporate University and training plans. % Staff trained: 91.0 ▪ Retaining talent. Voluntary rotation: 2.5 ▪ Health and safety. Accident frequency index: 1.00	▪ Gas distribution: 449,259 GWh ▪ Electricity distribution: 54,920 GWh ▪ Gas supply: 378,048 GWh ▪ Net production: 46,658 GWh	▪ Direct GHG emissions : 18.3 $MtCO_2$ eq. ▪ CO_2 emissions/generation: 342 tCO_2/GWh	▪ Economic value distributed : €23,413 M ▪ Social investment: €11 M
Our stakeholders	▪ **Shareholders**	▪ **Employees**	▪ **Customers**	▪ **Customers** ▪ **Society**	▪ **Society**

Following approval of the new Corporate Responsibility Policy and based on the recommendations of the CNMV's Code of Good Governance in connection with corporate responsibility, the Board of Directors approved the 2016-2020 Sustainability Plan in February 2017 which translates the commitments undertaken into specific actions and allows its compliance to be monitored by the Board of Directors and the Remuneration Committee. The action lines relating to each commitment have been fully aligned with the Strategic Plan and with the individual plans for each of the Group's business areas and departments.

6.2. Commitment to results

What resources are relevant to this commitment?	How do we measure our performance?
Financial	EBITDA
Human	Net profit
Social	Investments
	Indebtedness
	Pay-out

What this means for Naturgy?

In a challenging environment, Naturgy' acts with the goal to maintain a solid financial and business profile. Naturgy's business model looks for a balance between regulated contracted activities and unregulated ones while applying a strict financial policy.

What is our commitment?

- To protect our existing businesses while laying the foundations for future growth.
- To continue with the financial track of Naturgy.

Analysis of the 2018 results

The analysis of the consolidated and Naturgy's business results of the 2018 exercise are included in the section Business performance and results of this report.

Sustainability indices, green bonds and sustainable funding

Presence in socially responsible investing indices and ratings

The company occupies significant positions in the leading sustainability indices on the strength of its environmental, social and governance (ESG) performance metrics. Naturgy has been part of the Dow Jones Sustainability Index uninterruptedly for the last 14 years, and in 2018 it ranked first in the world in the Gas Utilities sector for the second consecutive year. The company has also been a member of FTSE4GOOD since the index was created in 2001, and ranks as world leader in the Multiutilities sector. During 2018, Naturgy was assessed by rating agencies Oekom, Sustainalytics and Vigeo. The company is included in the three variants of the Euronext Vigeo index: World 120, Europe 120 and Eurozone 120. Naturgy has also obtained the highest rating — AAA — from MSCI and is included in the MSCI Global Climate Index and MSCI ESG Leaders Index.

In 2018, Naturgy was recognised as a world leader for its action against climate change through inclusion in CDP's Climate Change A List. The company obtained the highest possible score in this climate change index in recognition of its action to reduce emissions, mitigate climate risks and develop a low carbon economy.

Green bonds and sustainable funding

In 2017, Naturgy developed a reference framework for the issuance of green bonds to fund renewable energies. Under this framework, on 15 November 2017, Naturgy issued a green bond for an amount of Euros 800 million, maturing in May 2025. The issue pays an annual coupon of 0.875%. The bonds were issued at 99.77% of par. Additionally, in 2017 the company's auditors certified compliance with the commitments acquired in the framework, and Naturgy's Green Bonds Committee met in December 2018 to assess the suitability and progress with the projects and the degree to which project development conformed to the objectives set in the issue.

In addition, in order to cover its funding needs and in line with its progress in sustainability, in 2017 Naturgy arranged a sustainable loan with ING Wholesale Banking for a total amount of Euros 330 million for 4 years, with the possibility of a one-year extension, whose cost is partially indexed to the company's environmental, social and governance (ESG) performance, as assessed by independent rating agency Sustainalytics, which issues a report and a rating in this connection.

The score by the agency improved in the first credit review, with the result that the interest rate was reduced.

6.3. Service excellence

What does it mean for Naturgy? Risks and management approach

The customer is the centre of operations at Naturgy. Through active dialogue, the company will provide speedy and efficient service which, as well as complying with the legal and profitability requirements, meets the customer's needs.

If the company fails to provide quality products and services, has a customer service that can be improved, and lacks communicative fluidity with the customer, it runs the risk of the customer requesting to finalise the contract or submitting complaints.

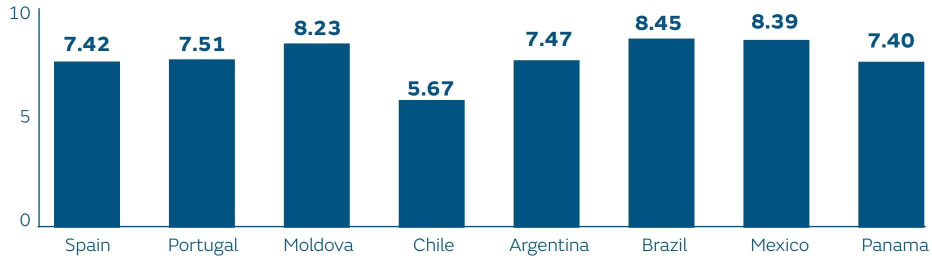
The failure to adapt or lack of flexibility in light of the current context of sector decarbonisation and digitalisation could lead to inefficiencies and losses of market share.

What is our commitment?

- Working towards ongoing improvement of safety, reliability and competitiveness of all products and services, offering the highest possible level of quality in accordance with the best available techniques.
- Fostering active and two-way communication that allows us to understand the expectations and opinions of customers and to adapt the responses of Naturgy to their needs.
- Facilitating relationships with customers through simple and efficient operations.
- Providing innovative products and services that encourage energy efficiency and which contribute towards the sustainability of society.
- Furnishing the customer with a differential value through products and services that adapt to each segment and to their needs.
- Applying technological innovation and the technical enhancements available as a means of maintaining an efficient, safe and sustainable supply.

How do we measure our performance?

Overall satisfaction with service quality



* Chile has been calculated based on a 1-7 scale, unlike other countries which used a 0-10 scale.

What are our main milestones in 2018?

- Raising awareness of the centrality of the customer to our business.
- Advanced CeX training, to enhance the customer's experience with the company.
- Greater dissemination of knowledge about the sector, company and products and services.
- Consolidation of personal experimentation of the customer reality.
- Visible commitment: management commitment to put the customer first.
- Recognition / Pride at belonging: proud to work at Naturgy.
- Evolution of travel and measurement to find out how the customer rates us when covering an energy need with the company.
- COMeX consolidation: to position the marketers in the heart of the distributors.
- Roll-out of the Partners programme: extending the pride of collaboration to collaborating companies.

What are our goals for 2019?

- New paperless digital model in the provision of the Servigas and Servielectric maintenance services.
- Billing digitalisation.
- Greater digital self-management in the customers' area of the website.
- Evolution of the model of efficient customer measurement, at least sufficient.
- Contribution of the Customer Experience to the Business.
- Annual Customer Experience Action Plan.
- Clear Communication Project customised by client.
- Optimal management of complaints.
- Introduction of the Global Customer Experience Policy.
- Evolution of data analytics to improve customer service.

Analysis of the 2018 results

The customer as the focal point

In 2018 the company began a new stage with an overhauled brand that reflects the corporate transformation, an evolution resulting from 175 years' experience and which supports our commitment with the customer to adapt ourselves to both the present and the future.

This new stage reasserts our Customer Centricity vocation as the basic pillar of the 2018-2022 Strategic Plan, placing the customer as the focal point of all decisions in order to offer an excellent service in a simpler, more innovating, more digital, nearer and more environmentally friendly way.

Our value proposal is to offer our customers simple, close at hand and practical solutions that help the customer on a daily basis, supporting ourselves through digitalisation and innovation, in order to provide excellence in service.

Quality and reliability of the service

Maintenance of the gas and electricity facilities is an essential aspect within Naturgy's mission to achieve a level of quality and reliability of the service that satisfies customers and enables us to comply with the regulatory requirements of the countries where we operate and with the most demanding standards of the industry. The aim of maintenance is to improve the safety and reliability of gas and electricity networks, and to maintain a high level of service quality.

Naturgy employs modern and innovative methods and work equipment that are included in safe and efficient work and operation procedures. The company also encourages close collaboration with contractor companies in the permanent quest to achieve best practices in the development of its activity.

A set of inspection and assessment actions are carried out, which help to define the corresponding preventive and mitigation measures to ensure a safe and ongoing supply, maximising the useful life of assets, and which are included in the Maintenance Plan for each type of facility.

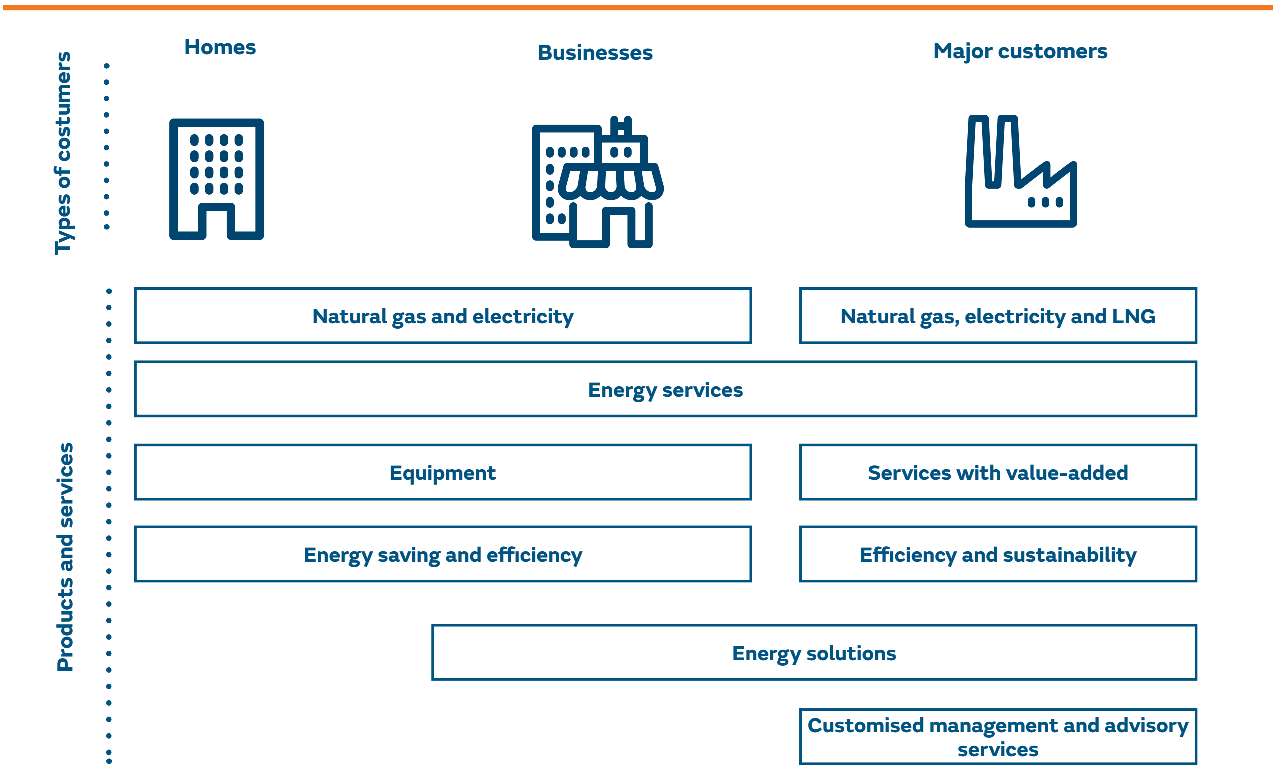
The preventive and corrective maintenance procedures are frequently subject to reviews by the technical quality, safety, and internal auditing, compliance and control divisions.

The maintenance actions performed by the company are reflected in the evolution of the main quality/service indicators, which have revealed a notable improvement in recent years. These indicators measure, *inter alia*, response times to a notification of a malfunction or anomalous situation affecting the grid, the stoppage time per customer or installed power, the kilometres of the grid and facilities inspected, and the number of incidents per kilometre of grid.

To ensure that supply meets demand, Naturgy regularly reviews the operating conditions of its networks, to make sure these are correctly sized or, if appropriate, to determine the potential needs of repowering or enlarging these. Furthermore, in electricity distribution, Naturgy partakes in several R&D&I projects for storage of energy in batteries, the development of smart grids, the application of drones to the maintenance installations and the introduction of predictive maintenance techniques for the main grid equipment.

Products and services adapted to customers' requirements and priorities

Naturgy's commercial offer is targeted at homes, businesses and major customers. The products offered are not restricted solely to the supply of gas and electricity, but encompass other aspects.



The development of new products is based on the needs detected through the mechanisms enabled by the company. The commercial supply seeks efficacy and efficiency above other factors. Efficacy, to satisfy customers' demand; and efficiency, to achieve the maximum competitiveness.

In 2018 we have renewed the commercial catalogue with new tariffs and new services to offer the customer a broader range of choices and to find more appropriate solutions for their needs, whilst simultaneously seeking to simplify the portfolio to provide customers with a simpler and more comprehensive experience. In the domestic area, we have also redesigned promotions by applying benefits according to customers' characteristics and habits.

Customer service

Naturgy has introduced an innovative Customer Service Model that is fully adapted to customers' characteristics and needs, offering close at hand and accessible solutions that allow for greater comfort and flexibility to our customers' requests. This model is included in the quality management system certified in accordance with ISO 9001 by AENOR.

The customer service channels that Naturgy makes available to customers aim to offer customised service that satisfies their expectations, and with a particular focus on digital channels in line with society's evolution, to achieve a swift and flexible resolution with self-management, simplicity and in an environmentally friendly way.

Customer service model

Our model comprises three focal points:

- Operational and training model: the aim is to anticipate customers' needs through predictive and data analysis models.
- Technological model: committed to a technological revolution that encourages greater self-management by customers.
- Procurement and financial model: building a partnership model with suppliers and an alignment of the win-to-win objectives.

Provision of customer service at Naturgy:

- Digital channel.
- Telephone channel.
- Guarantee office.
- Face-to-face channel - Centres.
- Face-to-face channel - Personal manager.

The company manages claims from three different areas: retail commercialisation, wholesale commercialisation and distribution of gas and electricity.

In the retail sphere, in Spain over 650 thousand customer claims were processed, approximately half of them dealing with billing issues. The process with the next highest number of claims was that of entering into contracts and, finally, claims related to payment collection. These three kinds of claims account for approximately 90% of all those received, whilst there are other processes, such as registration for new supplies, management of payment defaults and problems with readings, which make up the difference. The average claim response time was approximately one week.

In the wholesale sphere, around eight thousand claims were processed, down approximately 20% year-on-year. Most claims concerned billing and measuring processes, and none of them were of a relevant nature. Around 80% of these claims were resolved within the deadlines established.

In the area of gas and electricity distribution, any claim or complaint received from customers via the different channels available -whether through their gas or electricity marketer in issues for which the distributor is responsible (meter reading, supply quality, new registrations, etc.), directly with the electricity or gas distributor of the Naturgy Group through the customer service channels of the distributors, via the website contacts, by postal mail or through any competent organisation- is received and processed centrally in our integrated claims management system at the Shared Services Department.

The organisation handles not only customers of the electricity or gas system in its operational area, but also any individual or legal entity that may have a claim or complaint through the action or non-action of our distribution assets (works in progress, technical elements on public thoroughfares, etc.) is dealt with as if they were a customer.

With regard to transparency in communication of claims or complaints submitted, both business of Electricity Distribution in Spain (UFD) and Gas Distribution in Spain (Nedgia) comply with the obligations set out in circular 2 of 2016 issued by the National Securities Market Commission (CNMC), reporting every quarter with regard to the details on the situation of claims processed in accordance with the formats and deadlines established by the regulator.

Customer's satisfaction and experience

Naturgy listens to its customers' opinions and incorporates them into the decision-taking in order to develop innovative products and services that meet their needs and expectations.

The company has a model to measure customers' experience, through which it constantly monitors the satisfaction of its customers and the level of recommendation.

The model is based on three levers:

- Measurement: Naturgy collect the opinion of its customers through surveys that are classified into two supplementary blocks: general surveys and interaction with the company surveys.
- Analysis: the results are added to the daily management reports, which allows us to include the customer's voice in decision taking.
- Close the loop: process that enables immediate corrective action through the management of alerts that activate whenever the minimum satisfaction and recommendation thresholds required to maintain the level of quality that the company imposes with its customer relations are not reached.

Customer Experience programme (CeX)

The Customer Experience programme, based on cultural transformation, was born in 2015 at group level with the purpose of making the company a benchmark at international level in customer satisfaction in the energy sector, measured in terms of recommendation.

With Customer Experience the company introduces a new methodology through which the customer is at the centre the decision-making process, changing the way we do things in order to meet their needs and expectations, but above all, being sensitive to how they perceive the company and their experience within the company.

To this end we introduced a working model based on five pillars:

- Unique company identity (brand and culture).
- Organizational drive (sponsorship and commitment).
- Employees as ambassadors programme.
- Improvement of customer journey and contact points (the journey being the time necessary to cover the customer's needs, from start to finish).
- Continuous real-time measurement of the customer's voice.

As a response to our commitment towards the customer, we have formalised the Customer Experience as a cross-cutting group process and we have developed the Customer eXperience Global Policy for the group.

The Policy sets out the Naturgy action framework to ensure that the Customer Experience is integrated into the company's operations and decision taking.

As a result of this Policy, this year we have introduced the Clear Communication Project in the Customer Service billing area, in retail customers and markets and in infrastructures in Spain, providing the knowledge and tools so that people can develop a clearer and simpler communication for the customer.

Privacy and security of the customer's data

Naturgy, as part of its commitment to the privacy and security of data of employees and customers, has updated the Information Security Policy and the regulatory corpus of information security that ensures proper processing of this data throughout their life cycle collection and processing through to removal or safeguarding this data once the relationship has terminated.

The Policy and the regulatory corpus are communicated to employees, suppliers and customers, and is implemented in line with the legal requirements that govern the processing of information, the internationally accepted best practices and standards.

This regulatory corpus includes a specific technical standard, which is for the purpose of guaranteeing the protection of personal data at Naturgy and applies to all organisational units and companies of the group that capture or process personal data, as well as partners and suppliers that collaborate in such processing. This standard complies with the provisions set out in the EU General Data Protection Regulation (GDPR).

Security forms an essential part of the design, development and exploitation of all processes and systems, in particular those that process information. All of Naturgy's systems include procedures for authentication and administration of authorisations and access and are designed to guarantee that the use of these does not affect the security of the data handled.

6.4. Responsible management of the environment

What does it mean for Naturgy? Risks and management approach

Naturgy is aware of the environmental impacts that its activities have on the surrounding area, and the company therefore pays special attention to environmental protection and the efficient use of natural resources to satisfy the energy demand.

Naturgy goes beyond legal requirements and even the requirements we adopted voluntarily in our care for the environment. We involve our suppliers and we encourage and work with our stakeholders to use energy responsibly.

Inadequate management of climate change and its associated risks can lead to substantial losses for the company, caused by the increase in exposure to natural disasters, the decarbonisation trend of the sector and the loss of affinity on the part of stakeholders.

Improper environmental management can cause environmental impacts and the deterioration of natural conditions and biodiversity in the areas where the company operates. This, in addition to the direct impact on the environment, can cause the company reputational harm. The risk is greater if the company has infrastructures and/or carries out operations in protected areas.

What is our commitment?

- Contributing to sustainable development through eco-efficiency, the rational use of natural and energy resources, minimising environmental impact, encouraging innovation and using the best available technologies and processes.

- Contributing to the mitigation and adaptation of climate change through low-carbon and renewable sources of energy, encouraging savings and energy efficiency and the application of new technologies.

- Integrating environmental criteria in business processes, in new projects, activities, products and services, and in selecting and assessing suppliers.

- Minimising adverse effects on ecosystems and fostering the conservation of biodiversity.
- Encouraging the efficient and responsible use of energy and natural resources, introducing activities aimed at improving the management of these within the framework of the circular economy.
- Guaranteeing the prevention of pollution through ongoing improvement, the use of best available techniques and the analysis, control and minimisation of environmental risks.

How do we measure our performance?

	Unit	2018	2017
Direct greenhouse gas emissions	$MtCO_2e$	18.3	20.5
Emission factor for electricity generation [1]	tCO_2/GWh	342	388
Installed capacity free of emissions [1]	%	27.5	26.4
Net production free of emissions[1]	%	24.9	19.6
Activity with environmental certification[2]	%	88.7	87.7
Water consumption	Hm^3	26.5	28.0
Consumption of raw materials	Kt	6,729	7,580
Natural gas	Kt	4,736	4,638
Coal	Kt	1,630	2,480
Petroleum derivatives	Kt	352	452
Uranium	Kt	11	11
Direct energy consumption[3]	GWh	60,614	64,728
Indirect energy consumption (final use of natural gas distributed/commercialized)	GWh	577,647	613,181
Resources targeted at the prevention of environmental risks[4]	Million euros	494	96

1. Includes hydroelectric, wind, nuclear and solar generation.
2. Percentage of Ebitda certified with regard to that which is certifiable. The ebitda used in the ratio is the November closing ebitda.
3. It includes consumption of renewable, non-renewable and electricity resources and separates the electricity and the heat sold.
4. The 2018 figure includes the investment in renewable energies.

Note: It does not include the information of Moldova, Kenya and South Africa. The figures for Moldova are: GHG emissions: 0.002 $MtCO_2e$, Consumption of raw materials: 0.5 kt (0.0001 kt natural gas, 0.5 kt petroleum derivatives), Direct energy consumption: 254 GWh.

Provisions and guarantees for environmental risks

The company makes financial provisions to cover the materialisation of potential environmental risks, including:

In addition, Naturgy has guarantees to cover the occurrence of environmental risks in the insurance policies it has taken out. The insurance policies that the company has contracted and in which there is environmental coverage are:

- Environmental liability insurance: limit contracted for a value of Euros 150 million per loss event and in the annual aggregate.
- Liability coverage for sudden and accidental pollution in the general public liability policy: limit of Euros 700 million per loss event.
- Protection and compensation insurance: maximum limit of USD 500 million per loss event, in accordance with the Rules of the UK P&I CLUB 2018 (Charterers), to cover the liabilities for pollution arising from chartering vessels.

What are our main milestones in 2018?

- Growth of renewable power with low or zero emission.
- Development of renewable gas projects.

- Promotion of sustainable mobility.
- Extension of the biodiversity actions and plans.
- Progress in the certification of new environmental management systems pursuant to the ISO 14001.

What are our goals for 2019?

- Growth of renewable energies, in line with the goal of the 2018-2022 strategic plan (tripling installed capacity) to contribute to the mitigation of climate change and the energy transition.
- Promote innovation and the development of renewable gas projects as an energy and storage vector that facilitates the transition to a circular and decarbonised energy model.
- Offer sustainable mobility solutions for cities and land and maritime transport that improve air quality.
- Protect biodiversity in operations, applying a preventive approach, implementing best practices and encouraging the creation of natural capital.

Analysis of the 2018 results

Environmental management

Responsible management of the environment is a strategic pillar for Naturgy, which reflects its commitment to the Corporate Responsibility Policy approved and supervised by the Board of Directors. The policy includes the company's action principles, with an emphasis on promoting the sustainable development of society through the supply of competitive, safe energy and with the utmost respect for the environment.

Environmental management is structured around three strategic pillars:

- Climate and air: contributing to the mitigation of climate change, the energy transition and the improvement of air quality.
- Circular economy: promoting eco-efficiency in the use of resources to reduce negative environmental impacts.
- Natural capital and biodiversity: encouraging the preservation of natural and cultural heritage within the areas of operation.

The most significant current and foreseeable effects of the company's activities on the environment are the following:

- Contribution to climate change.
- Pollution of air, water and land.
- Biodiversity loss.
- Consumption of non-renewable raw materials.

To minimise these effects, Naturgy employs a preventive approach throughout the entire value chain of its business:

- Certified and externally-audited environmental management system aimed at preventing pollution and reducing environmental impacts along the entire value chain, involving employees, suppliers and other stakeholders. During the design phase of new facilities and during dismantling, the environmental conditions of the surrounding area are studied, and the projects are adapted, including the necessary preventive, corrective and compensatory measures. During the operational phase, strict monitoring is performed to ensure compliance with legislation and to maintain impacts within the limits set.

- Integration of the environment in the management of risks and opportunities and in the decision-taking processes, paying special attention to climate change and the energy transition.

To ensure consistency and uniformity in the company's key environmental management processes, there are global methodologies and tools for environmental management that are used in different businesses and geographies, including the following:

- Themis, for the identification, registration, monitoring and management of compliance with legal requirements.

- Prosafety, for recording and management of the findings, nonconformities, observations and opportunities to improve environmental management.

- Enablon, for recording and centralized management of environmental indicators related to atmospheric emissions, consumption of raw materials, water and other resources, discharges, waste, etc. The system is also used to monitor environmental targets and action plans.

- Geographical information system of biodiversity, showing the protected natural areas, the group's facilities and the initiatives carried out to protect and improve natural capital.

- Carbon footprint, to determine greenhouse gas emissions throughout the entire value chain, including indirect emissions produced by third parties upstream and downstream of group activities.

- Environmental footprint, to measure the company's environmental performance, distinguishing between the components of atmosphere, waste, climate change, water, biodiversity and resources.

- DAMAS, to identify and assess the direct and indirect environmental aspects of the company, allowing us to establish the most relevant aspects to take into account both in the environmental management of these as well as the environmental targets defined each year.

- Environmental planning, through which action lines are defined, introduced and supervised to reduce environmental impact and for continuous improvement.

- Environmental audits, both external and internal, conducted within the scope of the integrated management system.

Integrated Management System

For years, Naturgy has had an integrated quality, environment, health and safety management system (IMS), certified according to the requirements of the ISO 9001:2015 and ISO 14001:2015 standards. This system is audited externally every year.

The processes certified through this system are:

- Extraction and injection of natural gas.

- Transport and operation of the Maghreb-Europe gas pipeline.

- Electricity generation (thermal, hydraulic, wind and solar origin).

- Distribution of natural gas and electricity.

- Wholesale and retail commercialisation of natural gas and electricity.

- Development and execution of engineering projects.

- Energy management in organised Iberian electricity markets.

- Corporate activities involving customer service, billing and payment, training and management of office buildings.

Environmental risk management

Naturgy identifies, records and analyses all the environmental risks and events that have occurred in order to define, apply and disseminate preventive measures to reduce potential damage to the environment. To do this, facilities with environmental risk are assessed using recognised standards as a reference. The first element for management is self-protection plans and their associated procedures, in which the most appropriate risks and responses are identified in light of potential accidents and emergency situations that can cause environmental damage.

In addition, there are global and uniform procedures and systems in the different businesses and geographies for reporting, classifying, monitoring and managing environmental events (Prosafety).

This methodology allows not only an adequate and uniform monitoring of environmental events, but also the identification, analysis, development, application and exchange of preventive measures and best practices in risk management at a global level.

For management of the climate change risk, Naturgy has a specific tool, developed in Ms Excel and @Risk, which allows us to estimate the Group's exposure to risks at an aggregate level and broken down by business and geography. This tool analyses the impact of climate change on different businesses and technologies, over time periods (short, medium and long term) and geographies. This allows us to estimate the impact of different climate change scenarios (IPCC) through different indicators:

- Physical: impact forecasts on energy (produced, traded, purchased, etc.) water level with regard to the height of the corporation's facilities, availability of hydric resources, etc.

- Environmental: emissions of CO_2.

- Business: market shares and penetration levels.

- Economic: impact forecasts on level of revenue, Ebitda, cash flow and present value of the business, as well as estimates of the value at risk for different confidence levels.

In addition, it means we can simulate new scenarios based on new products and services, etc. and the implementation of R&D&I actions, generating different scenarios to assess the impact.

1. Climate and air quality

Naturgy believes that climate change is a global environmental challenge and is committed to offering its customers eco-efficient and less CO_2-intensive energy products and services to help mitigate climate change and the energy transition.

The main strategic lines of action in terms of climate are:

- Favouring the mitigation of climate change and the improvement of air quality, displacing carbon-intensive fuels and encouraging the promotion of energy savings and efficiency both in our own facilities and at our customers.

- Contributing to the decarbonisation of the system, increasing the use of gas and renewable electricity and encouraging their integration through the development of smart grids.

- Supporting international climate change negotiations and mechanisms that foster technological neutrality and industrial competitiveness, promoting the development of the most appropriate technologies at each stage of the energy transition.

Naturgy has a voluntary goal for GHG reduction. This target is aligned with science to avoid an increase in temperature above 2°C (Science Based Targets Initiative. Tool V8): Average reduction of 26% of total direct emissions for the 2013-2025 period, taking 2012 as the base year.

The main lines of action carried out to reduce GHG emissions:

- Displacement of carbon intensive fuels.
- Fostering renewable electricity.
- Promoting renewable gas.
- Encouraging the gas-renewable binomial in generation.
- Reducing fugitive emissions.
- Increasing energy efficiency in our facilities.
- Promoting energy efficiency at our customers.
- Exploring and developing technologies to reduce emissions.

For management of climate change, the following means are available:

- Measurement and control tools for GHG emissions and operational plans implemented to reduce them, including the annual calculation of the group's carbon footprint.
- Transparency and dissemination of information, publishing the carbon footprint report and participating in the international benchmark indexes on climate change, such as the CDP.
- Participation in the following initiatives related to climate action:
  - Carbon Pricing Leadership Coalition (CPLC).
  - Caring for Climate.
  - Statement on fiduciary duty and climate change disclosure.
  - Corporate commitment with the Science Based Targets climate policy initiative.

2. Circular economy

Naturgy is committed to promoting the circular economy through the efficient use of resources to reduce environmental impacts. To do this, different lines of action are developed, focused fundamentally on:

- Improving eco-efficiency in the use of resources, energy, water and raw materials, reducing pollution, waste and its impact on the environment.
- Innovating for the promotion of renewable gas (biomethane and hydrogen) as an energy and storage vector that facilitates the transition to a circular and decarbonised economy model.
- Offering sustainable mobility solutions for cities and land and maritime transport that reduce atmospheric contamination and improve air quality.

Within the framework of the integrated management system, Naturgy develops management and control procedures aimed at minimising the waste that is disposed of in landfills, through prevention, reuse, recycling and/or energy recovery.

Most water consumption at the facilities of Naturgy is due to the operation of thermal power stations. Specifically, the majority is produced through the evaporation of water in the cooling towers; the rest corresponds to consumption in other processes, in the water-steam cycle and in other auxiliary services. Most of the water collected is returned to the environment. Depending on its origin, the main source of supply is the sea, with fresh water accounting for a much smaller contribution. It is important to note that Naturgy, aware of the scarcity of water in the environments of some of its power plants, introduced systems for the reuse of wastewater in these facilities.

Regarding effluent discharges, at power stations we monitor and analyse not only the effluents but also of the waters of the environment receiving the effluent discharges. The treatment equipment and systems worked as planned in 2018, complying with environmental permits. In addition, studies of the receiving environment reveal that no significant impacts were generated in the aquatic ecosystems where the effluent discharges are made.

Furthermore, Naturgy also promotes energy efficiency, both in its own facilities and at its customers, helping to reduce environmental impacts due to unconsumed energy. Moreover, numerous innovation initiatives are under development in the field of renewable gas, in order to promote this new energy vector, which allows the recovery of organic waste and reduces GHG emissions.

3. Natural capital

Naturgy is committed to the preservation of natural capital, biodiversity and cultural heritage in the areas around its facilities, with special attention paid to protected areas and species. To this end, it is based on the precautionary principle, conducting prior environmental studies during the design phase that minimise the negative impacts of the complete life cycle of the facilities.

Introducing additional voluntary measures contributes to the knowledge and mitigation of the impacts arising from the development of new projects and the operation of the facilities once they have been introduced. The company also takes into consideration the opinion of stakeholders in places where activities and projects are developed.

In addition, in the areas surrounding the facilities, especially in those that are close to protected areas or of high value for biodiversity, studies are carried out to improve the knowledge of the natural spaces and to reduce impacts.

The development of Naturgy's activities requires the occupation of land. When the facilities are being designed, environmental impact studies are carried out, in which the protected areas that have a high ecological value are analysed, adapting the project to avoid or minimise the impacts on biodiversity. In those cases in which it is not possible to completely avoid the impact, the required compensatory measures are introduced.

Once the facilities are operational, they are integrated into a Geographical Information System, where they are crossed-checked with the protected natural spaces to identify, quantify and monitor the impacts on biodiversity.

To minimise these effects, the company applies operational control procedures and, at those facilities where there can be greater potential risk, we carry out environmental assessment studies and define environmental emergency plans to prevent the incident before it occurs, or to minimise any damage. We also regularly perform environmental emergency drills to test the procedures that have been defined.

The key impacts on biodiversity that may arise from the company's operation in the area of the sites and in the areas adjacent to them, are the following:

- Temporary condition affecting the fauna present in the environment, as a consequence of the construction of transportation and distribution infrastructure of gas and electricity.

- Permanent condition affecting bird life and arboreal vegetation, as a result of the operation of transport networks and the distribution of electricity.

- Impact on the abiotic and biotic environment of the environments around the facilities, as a consequence of emissions arising from combustion.

- Condition affecting the populations of species present in the environment, as a consequence of changes in land use and the permanent presence of the facilities in the natural environment.
- Effect on the aquatic environment, as a result of effluent discharges.
- Relevant effect on biodiversity (positive and negative), as a consequence of the creation of reservoirs associated with hydraulic power stations.

6.5. Interest in people

What does it mean for Naturgy? Risks and management approach

For Naturgy it is essential to foster a quality working environment, based on respect, diversity and personal and professional development. Naturgy also has a Code of Ethics that establishes the guidelines governing the ethical behaviour of all employees in their daily work and, specifically, with regard to the group's relations and interactions with its stakeholders.

Persons that suffer any kind of discrimination or do not feel themselves to be fairly rewarded tend to reduce their pride of belonging and lower their productivity. Furthermore, research reveals that the increase of pay inequality is associated with lower profits, productivity and business competitiveness.

The major transformation of the energy sector and digitalisation require new expertise and skills which, if they are not covered in a flexible way, would place the company at a disadvantage with its competitors, with the resulting consequences this could have on the business.

What is our commitment?

- Applying best practices in identifying, attracting and retaining the talent necessary for the development of the businesses, ensuring the principles of fairness and non-discrimination on any grounds whatsoever (disability, age, gender, work history, etc.).
- Encouraging the professional development of persons as part of the talent management model, ensuring that all professionals have the means, programmes and tools necessary to foster their skills and expertise.
- Promoting a motivational work setting that guarantees internal recognition of the culture of effort, the autonomy required to be able to create, develop and innovate, and an overall framework of compensation that is commensurate with this.
- Ensuring the effective introduction of flexibility mechanisms that facilitate the balance between professional and personal life, and which favour the human and social development of persons.
- Promoting diversity and equal opportunities in an environment of respect, understanding and ongoing dialogue, with a special focus on the inclusion of disabled persons and extending this commitment to suppliers and collaborating companies.
- Fostering constant liaison between the company and workers' representatives that enables feedback in order to take decisions.

How do we measure our performance?[1]

Distribution of employees by age group, country, gender, and employee category

	2018												
	Nº employees	18-35 (%)	36-50 (%)	>50 (%)	Management team		Middle managers		Technicians		Operators	
					Men (%)	Women (%)	Men (%)	Women (%)	Men (%)	Women (%)	Men (%)	Women (%)
Germany	7	14.3	57.1	28.6	-	-	-	-	71.4	28.6	-	-
Argentina	767	21.3	37.4	41.3	3.7	0.8	13.7	3.5	15.1	4.8	45.0	13.4
Australia	8	50.0	37.5	12.5	-	-	-	-	25.0	-	62.5	12,5
Belgium	3	66.7	33.3	-	33.3	-	-	33.3	-	33.3	-	-
Brazil	478	25.7	61.5	12.8	5.2	2.9	12.8	7.1	15.5	11.5	29.3	15,7
Chile	3,046	27.2	49.1	23.7	2.2	0.8	12.6	3.2	26.5	11.0	33.7	10.0
Colombia	84	36.9	48.8	14.3	10.7	13.1	6.0	9.5	17.9	22.6	8.3	11.9
Costa Rica	20	20.0	65.0	15.0	5.0	-	5.0	-	10.0	-	75.0	5.0
Spain	6,532	11.1	59.9	29.0	11.0	4.4	15.2	4.6	19.9	15.0	19.2	10.6
France	66	57.6	40.9	1.5	10.6	3.0	6.1	7.6	28.8	31.8	3.0	9.1
Holand	7	28.6	71.4	-	14.3	-	14.3	-	28.6	28.6	14.3	-
Ireland	40	50.0	45.0	5.0	12.5	2.5	12.5	5.0	32.5	27.5	7.5	-
Israel	15	73.3	26.7	-	-	-	13.3	6.7	53.3	26.7	-	-
Morocco	93	7.5	43.0	49.5	3.2	1.1	39.8	2.2	11.8	2.2	29.0	10.8
Mexico	989	37.1	54.5	8.4	5.8	1.3	16.5	4.0	23.7	10.5	27.2	11.0
Panama	362	37.0	36.2	26.8	5.0	2.5	21.3	9.9	12.7	11.6	25.4	11.6
Peru	21	52.4	42.9	4.8	-	4.8	14.3	4.8	33.3	14.3	9.5	19.0
Portugal	18	38.9	61.1	-	-	11.1	-	-	16.7	44.4	5.6	22.2
Puerto Rico	5	20.0	20.0	60.0	40.0	-	40.0	-	-	-	-	20.0
Dominican Rep.	84	19.0	66.7	14.3	1.2	2.4	23.8	9.5	3.6	7.1	50.0	2.4
Singapur	4	75.0	25.0	-	25.0	-	-	-	75.0	-	-	-
Uganda	51	66.7	29.4	3.9	2.0	-	39.2	5.9	-	2.0	43.1	7.8
TOTAL	**12,700**	**20.1**	**54.3**	**25.6**	**7.4**	**2.9**	**14.8**	**4.5**	**21.0**	**12.8**	**25.8**	**10.8**

1. The indicators that represent the evolution over the year include information from companies held for sale (Moldova, Kenya) or sold prior to the year-end (South Africa) provided that the opposite is not specified, while the indicators that represent information at the year-end do not include information about these companies.

Annual average of indefinite and temporary contracts by age, gender and professional category

percentage of workforce by type of contract		2018
Permanent contract	Men	67.7
	Women	30.1
Temporary contracts	Men	1.2
	Women	1.0
Total		**100.0**

Average annual workforce temporary contract by professional category	2018	
	Men	Women
Executives	2	-
Technicians	102	70
Administrative staff	-	-
Operatives	109	62
Total	**213**	**132**

Average annual workforce temporary contract by age	2018	
	Men	Women
18-35	136	92
36-50	68	38
>50	9	2
Total	**213**	**132**

Rotation and voluntary rotation index

(%)	2018	2017
Rotation	17.4	6.4
Voluntary Rotation	2.5	2.9

Number of dismissals by age group, gender, and professional category

	2018	
Dismissals by profesional category and gender	**Men**	**Women**
Executives	9	2
Technicians	111	32
Administrative staff	-	-
Operatives	70	55
Total	**190**	**89**

	2018	
Dismissals by age group and gender	**Men**	**Women**
18-35	60	23
36-50	72	44
>50	58	22
Total	**190**	**89**

Salary gap[1]

Below is a detail of the salary gap measure according to which a % above zero represents the % that women earn less than men:

	2018			
	Executives	**Technicians**	**Administrative staff**	**Operative**
Argentina	21.4%	12.8%	11.6%	17.8%
Brazil	22.7%	14.7%	-	24.1%
Chile	38.1%	6.1%	18.0%	17.8%
Colombia	10.2%	28.0%	(2.4%)	-
Spain	13.1%	4.5%	6.2%	13.3%
France	23.7%	18.1%	8.2%	-
Ireland	38.9%	19.6%	-	-
Morocco	4.5%	6.7%	7.1%	-
Mexico	4.5%	(2.1%)	(26.6%)	(30.1%)
Moldova	2.3%	2.5%	(17.9%)	(2.1%)
Panama	(20.4%)	(16.1%)	15.9%	-
Dominicana Rep.	-	(10.0%)	22.7%	-

1. Data is provided about the most relevant countries for Naturgy. The difference in salary shown by the results is in line with the context of the sector and generated mainly by the company's past gender make-up, which means greater average seniority of men in comparison with women. The reason why boxes are left blank is because there are no employees of one gender or another in said professional category.

Average remuneration by age group, gender, and employee category[1]

	2018							
	Executives		Technicians		Administrative Staff		Operative	
	Men	Women	Men	Women	Men	Women	Men	Women
Argentina	59,279	46,587	22,995	20,060	17,868	15,799	20,135	16,555
Brazil	51,148	39,534	21,571	18,399	-	18,494	14,887	11,306
Chile	156,804	96,992	46,327	43,515	28,184	23,125	17,951	14,456
Colombia	83,685	75,116	15,804	11,377	6,156	6,305	-	-
Spain	102,177	88,797	45,203	43,135	33,346	31,269	31,691	27,498
France	100,743	76,888	52,909	43,353	35,231	32,339	-	-
Ireland	99,000	60,500	56,000	45,000	-	-	-	-
Morocco	93,061	88,902	34,577	32,248	13,090	12,155	17,532	-
Mexico	33,186	31,693	14,442	14,747	6,828	8,646	6,567	8,544
Panama	38,576	46,463	17,256	20,036	18,896	15,899	14,128	-
Dominicana Rep.	-	73,110	23,216	25,545	12,210	9,439	11,946	-

It includes only the fixed remuneration.

	2017							
	Executives		Technicians		Administrative Staff		Operative	
	Men	Women	Men	Women	Men	Women	Men	Women
Argentina	78,404	63,187	31,615	28,602	24,812	22,116	26,555	25,626
Brazil	75,051	65,270	26,068	23,699		20,518	15,449	15,034
Chile	128,109	87,065	41,803	38,023	25,064	20,438	15,191	13,140
Colombia	63,952	54,794	13,550	12,569	6,564	6,455	6,227	6,615
Spain	99,531	84,576	50,329	45,813	42,004	35,990	38,876	29,529
France	97,143	82,911	52,146	42,623	34,596	31,617	-	-
Ireland	312,231	67,600	46,680	41,656	-	-	-	-
Morocco	85,786	81,598	33,235	29,675	9,499	12,013	16,277	-
Mexico	31,796	29,357	12,741	12,849	6,478	8,188	5,617	5,585
Panama	41,041	43,775	16,393	18,152	16,216	15,082	13,098	-
Dominicana Rep.	46,643	73,699	20,009	24,309	11,915	9,045	11,683	-

It includes only the fixed remuneration.

Average remuneration by age (Spain)	Amount
18-35	34,446
36-50	48,737
> 50	56,196

Average remuneration of directors and executives

The remuneration of the executives of Naturgy is detailed in an individual basis in Note 26 of the annual accounts.

The average remuneration of directos of Naturgy (without taking into account indemnities detail in the section of the Corporate governance) amounted 808 thousand of euros in the exercise 2018.

Disabled persons integration rate

	2018	2017
Employees with disabilities (%) in Spain	2.40	2.50

Percentage of employees covered by collective bargaining agreements

	2018		2017	
	Not covered by collective bargaining agreement	Covered by collective bargaining agreement	Not covered by collective bargaining agreement	Covered by collective bargaining agreement
Germany	-	100.0	-	100.0
Argentina	19.3	80.7	23.0	77.0
Australia	-	100.0	-	100.0
Belgium	33.3	66.7	18.2	81.8
Brazil	25.5	74.5	24.6	75.4
Chile	4.6	95.4	4.8	95.2
Colombia	47.6	52.4	45.5	54.5
Costa Rica	-	100.0	-	100.0
Spain	32.0	68.0	29.8	70.2
France	72.7	27.3	71.3	28.7
Holand	-	100.0	-	100.0
Ireland	100.0	-	95.1	4.9
Israel	-	100.0	-	-
Morocco	34.4	65.6	33.0	67.0
Mexico	19.0	81.0	18.3	81.7
Panama	61.9	38.1	59.9	40.1
Peru	-	100.0	-	100.0
Portugal	-	100.0	-	100.0
Puerto Rico	-	100.0	44.4	55.6
Dominicana Rep.	3.6	96.4	3.9	96.1
Singapur	100.0	-	100.0	-
Uganda	-	100.0	-	100.0
Total	**24.1**	**75.9**	**22.8**	**77.2**

Training[1]

	2018	2017
Workforce trained (%)	91.0	93.7
Total course hours	645,311	613,623

	2018				
	Management team	Middle managers	Technicians	Operators	Total
Total course hours	113,262	137,823	204,617	189,609	**645,311**

1. They do not include Kenya or South Africa. They do not include figures for companies and/or countries that do not have access to the Success factor platform (Energía de San Juan, S.A., Ireland and Israel).

What are our main milestones in 2018?

New organisational model of the group

- Scaling up the use of people analytics in the preparation of diagnostics and in taking decisions that concern persons.
- Implementation of new ways of working and new methods of collaboration that accompany the evolution of the businesses.

What are our goals for 2019?

- Application of the new People Model
- New ways of working project: TEAM
- Launch of the Transformational Leadership Academy
- Naturgy in-house Communication Plan focused on: corporate priorities, the executive role in communication, and fostering participation

Analysis of the 2018 results

People management model

During 2018 the people management strategy at Naturgy has revolved around the transformation and creation of value, as set out in the company's roadmap. The empowerment of people is one of the levers that drives the transformation the company is introducing, and, in this regard, management of people has focused on defining its management model, bridging the new strategic targets with people and simplifying processes to accompany the creation of value.

The people management model is designed as a dynamic ecosystem that enables people to be part of the company's evolution, and is one of the key levers, together with customers and shareholders, in the creation of value. The Naturgy people model applies at corporate level and incorporates three major areas, where a series of focal points and their associated processes come together to ensure consistency and solidity of the model:

- Commitment and loyalty, which works on attracting, retaining and the segmentation of talent.
- Total compensation, which links the professional category, remuneration and the working environment.
- Training, as an element of evolution and development of the company's professionals.

Measures to foster employment

Naturgy has a pool of young professionals with sound technical and management training, through the annual programmes of work experience and the agreements for Dual VT. A pool that enables us to respond to the company's needs and to attract the best talent in those spheres of knowledge in which Naturgy is the leader:

- Professional practices programme: Naturgy has partnerships with the main universities and higher education centres in those countries where it operates, through which it selects young people for work experience each year.
- The Dual VT offers Naturgy the opportunity to participate in the vocational training of young people, developing academic content adapted to the needs of the company, ensuring rapid adaptation to the working environment.

Diversity and equality

For Naturgy it is essential to promote diversity and equal opportunities in an environment of respect, understanding and ongoing dialogue, with a special focus on gender diversity targets, on the inclusion of individuals with various disabilities and extending this commitment to suppliers and collaborating companies.

In 2013, Naturgy established an Equality Plan at corporate level together with the union representations that was published in the Official State Gazette under Registration Number 90100073112013. It is based on 14 strengths to be maintained and 14 weaknesses to be corrected identified by outsourced experts, giving rise to 32 actions in issues of *communication* and raising awareness, culture and leadership, development and promotion, remuneration, flexible employment and work-life balance, selection, prevention of harassment, measurement and monitoring.

The creation and activation of a specific protocol against harassment; the best practices protocol in the selection processes, or the communication guide for business professionals that need to intervene for some reason in the selection process, are just some of the measures introduced and which, together with the Integrated Diversity Plan, approved at the end of 2015, have propitiated major advances in diversity and equal opportunities.

The protocol against sexual harassment lays out some preventive actions to avoid situations of harassment that include informing all employees about the protocol; training the entire workforce in the issue, and in particular employees with personnel under their charge; the obligatory nature and responsibility of each employee to establish their relationships with respect and dignity and for each employee to report any case of harassment to their superior.

The action procedure in the event of detecting any situation of harassment sets out two channels:

- Informal procedure: through which the affected party informs the alleged aggressor that this behaviour is not welcome, that it is offensive and interferes with their work. And if the situation is not resolved, then the formal procedure will be instigated.

- Formal procedure: through which the harassment situation is reported, following these steps:

  – Notification to the Code of Ethics Committee or reporting to their superior or to the Human Resources Department, who will decide whether to accept it for processing.

  – Investigation, gathering the information and conducting interviews with the affected parties and witnesses, if there are any.

  – Possibility of introducing precautionary measures.

  – Report on conclusions and resolution of the procedure, which will include the corrective measures and the introduction of the following solutions: filling of the report or commencement of the disciplinary file depending on the seriousness of the offence.

The protocol offers a series of guarantees, inter alia the complete anonymity of the informant; the process will be completed as expeditiously as possible; the intervention of the workers' representatives may be requested and an impartial hearing guaranteed, along with fair treatment for all of the affected parties. No reprisals will be allowed, and the identity of the informers will be protected.

In 2018, the company's commitment to diversity remained strong, consolidating the Integrated Diversity Plan which brings together specific initiatives, in all geographies and territories, for people management, classified into three areas: gender, disabilities and age.

As regards integration and accessibility of people with different capabilities, the Management of Naturgy acts as an impetus for a range of actions targeted at standardising management of functional diversity:

- Family Plan: this provides relatives of employees with advice from professionals and experts in disability and employment integration, so that from the earliest ages they can develop the skills and abilities that enable persons with disabilities to increase their autonomy and employability.
- Capacitas Plan: this aims to promote the employment of people at risk of social exclusion on grounds of disability.
- Aflora Plan: this encourages those employees of Naturgy with some degree of disability to contact the company for information on new measures specifically designed to achieve the full integration of everybody in a unique environment of diversity.
- Bequal Plus certificate: Naturgy renewed this certificate in 2018, substantiating our commitment in corporate social responsibility and disability.

The Equality Plan has encompassed the development of best practices protocol to avoid discrimination in the selection processes, and which includes the following measures:

- Open up the spectrum of recruitment sources to associations and foundations to guarantee equal job opportunities at the company.
- In the publication of job offers:
  - No discriminatory terminology is used.
  - Put the feminine gender first followed by the masculine.
  - Gender separation will always be carried out with slashes.
  - Do not use any notation as a requisite that does not offer equal conditions to the different candidates on the grounds of gender, appearance, disability, age, religion or personal beliefs of any kind.
  - Only specify the need for a driving licence when the job requires this.
  - Do not use possession of own vehicle as a requirement.
  - Do not use the need to reside near the place of work as a requirement.
- In the selection process:
  - In the case of disabled candidates, make sure we have the accessibility required so that they can attend the interview with us.
  - Avoid prejudices and stereotypes associated to gender, appearance, disability, age, religion, religious beliefs of any kind.
  - Transmit the corporate image.
  - Avoid personal questions and, if necessary, justify them.
  - Avoid preferential treatment.
- In the finalisation of the process:
  - Explain the result of the process.
  - Explain the next steps if they have passed the process.

- On joining the company:
  - Inform them about the equal opportunity policies.
  - Transmit values.
  - Non-discriminatory social benefits.
  - Career plans based on merits and capabilities.

Training and development

Training is one of the key areas of the Naturgy People Model. The Naturgy training and development model is instrumented through the Naturgy Corporate University, as this is a strategic lever of transformation that serves the business to build the future, create value and achieve the goals set out in the Strategic Plan.

The Corporate University's mission is to help develop professionals that make Naturgy's vision a reality and its aim is to ensure adequacy between the job position and the person, the acquisition of expertise linked to new needs of the organisation and the development of skills and abilities related to the Naturgy leadership and culture model.

Its advisory board guarantees a steadfast connection between the company's strategy and the activity of the Corporate University. The board comprises representatives from the company's senior management as well as external advisers from prestigious academic institutions.

The Corporate University has a quality management system pursuant to the ISO 9001:2015 standard, renewed in 2017 and with CLIP (Corporate Learning Improvement Process) accreditation from the European Foundation for Management Development (EFMD) since 2003 and last renewed in 2018 for a five-year period. This certificate recognises the quality of learning and development processes of people of corporate education organisations.

2018 has seen consolidation of the introduction of Evolution as an on-line training platform of the Corporate University and the evolution of the company's new training model based on three levers: employee experience, personalisation of the training available and centralised global operations.

The Corporate University's management model responds to the training needs through its two academies:

- The Tech Academy guarantees the transfer of specific technical knowledge in each business, thus permitting its efficient development and ensuring quality and uniformity in all countries.
- The Transformational Leadership Academy, focused on transformation through the development of leadership of the executive, director and management team of Naturgy.

Flexibility

Naturgy is committed to promote an appropriate work-life balance through a significant number of flexible employment measures, services and benefits adapted to employees' needs.

Global FRC certification

Naturgy is a benchmark of the new socio-labour and business culture. This is recognised in the Global Family Responsible Company (FRC) certification, obtained in 2013, renewed in 2016 for another three years and reviewed in 2017 and 2018, respectively. We were the first and only company to obtain this qualification issued by the Más familia Foundation. This certification is audited by AENOR, and is supported by the Ministry of Health, Consumer Affairs and Social Welfare.

This certification is an endorsement of the country-specific local measures on conciliation and development, but it also identifies 20 measures that are common to all of them and which are promoted at corporate level. Among these 20 measures, we can highlight those expressly related to the principles set out in the Global FRC Standard 1000/23 on time flexibility (flexible working day and paid leave); support to the personal environment (support to the family environment and spaces of integration between employees and relatives), personal development (with non-work integration activities), and job quality (use of technological tools to avoid travel, along with health, safety and well-being measures).

Time Bank

Naturgy provides its employees with a space, both physical and virtual, where they can delegate the performance of daily tasks in order to increase the free time they can spend on the most enriching aspects of their personal life. The range of services available to them is extensive and structured into three blocks:

- Administrative tasks: advisory and assistance services for frequent administrative tasks.
- Advantages club: an exclusive virtual space with more than 500 offers.
- Easylife space: outreach services and acquisition of products.

The Time Bank also offers services available on a quotation basis, such as technical services, courier services, returning clothes to stores and currency exchange, or special services provided during Christmas or back-to-school campaigns, among others.

In addition, in April 2018 we introduced the Easybox service which makes all of these tasks even easier and more flexible, through an interactive drop-point service and a website where users can request more than 20 different services, with the benefit of being able to deliver and collect at the most convenient time.

Access to these services is built into the My Benefits platform, on the corporate Intranet. Leadership and talent programmes have helped promote professional development and training, strengthening the human potential of the company.

Compensation and remuneration

Naturgy's remuneration policy is governed by equity on an internal scale and competitiveness from the market point of view. There are two models:

- The remuneration level of employees included in the collective bargaining agreement depends on the professional group and subgroup to which they belong.
- For those employees not included in the collective bargaining agreement, it is established on an individual basis according to the remuneration policy approved by the Board of Directors' Appointments and Remuneration Committee.

The remuneration package of Naturgy employees is supplemented with a social benefits system, which includes a pension plan, the main vehicle of funding post-employment commitments.

In the case of Spain, the Joint Pension Plan for Employees of the Naturgy group is a defined contribution plan for retirement and defined benefits in the event of death or incapacity whilst actively working.

The plan currently has assets totalling more than Euros 500 million, distributed among more than 6,300 active employees, and close to 2,000 beneficiaries.

On the international stage, the group's retirement policy at all companies revolves around retirement savings instruments and coverage for death or incapacity while an active worker. These provide employees with benefits that complement the public systems of social security and are always introduced in accordance with the particular nature and needs of the social welfare issues of each country.

By the same token, the company provides a series of social benefits that supplement employee remuneration packages, irrespective of their type of workday.

Internal communication with employees

The purpose of Naturgy's internal communication is to assist compliance with the company's strategic goals, aligning the entire organisation and strengthening corporate culture and values.

Naturgy has a range of channels to disseminate these messages, such as the corporate Intranet, Naturalnet, and the magazine Natural, which is distributed internationally and the social network Yammer. In February this year the company set up a new channel, Naturalnews, which operates as the digital newspaper of Naturgy and provides information on the company's latest news.

Labour relations

Respect for the freedom to join a union; fundamental rights; collective bargaining, and the agreement culture represent the key principles of what we do. Furthermore, we respect workers' representatives freely elected in all countries where the company operates, and we have also introduced communication channels with these representatives as a major part of our corporate action principles.

The collective bargaining agreements include several communications channels with representatives, under the form of committees to deal with the many and varied aspects of general interest.

One of the mechanisms for consultation and employee participation are the regular health and safety meetings held in all areas of the company. This means that all employees have a channel of direct participation available to them through the joint meetings between management and employees, and 100% of the workforce is represented at meetings.

It should be noted that the holding of these meetings is to not replace the various health and safety committees required under labour legislation and which correspond to each country. The main issues, formerly dealt with during 2018 of these kinds of meetings with the workers' representatives, were:

- Health and safety commitment.
- Analysis of the accident rate.
- Launch of new regulations.
- Comprehensive health.
- Quarterly monitoring of measures.

6.6. Health and safety

What does it mean for Naturgy? Risks and management approach

Naturgy plans and carries out its activities with the firm belief that nothing is more important than health, safety and well-being of people. In this regard, the company's action goes beyond compliance with legal obligations and other requirements that it voluntarily adopts, driving continuous improvement in working conditions and in management of health, safety and well-being. This not only involves people who work for Naturgy, but also suppliers, collaborating companies, customers and other stakeholders, in order to avoid and to prevent accidents and damage to health, providing a safe and healthy environment as well as promoting health and well-being.

A company with a high accident rate or which does not look after the health of its employees has to face the costs associated to the absence of these or to a reduction in its productivity. Furthermore, it could have a negative influence on attracting and retaining talent, as well as the perception of the company by its stakeholders.

What is our commitment?

- Guarantee that health and safety are non-delegable individual duties, and that they are taken on by senior management through a visible collective commitment, proactively accepted and implemented by the entire organisation, and by our suppliers and collaborating companies.
- Establish health and safety as an individual responsibility and as a condition of employment at Naturgy and of the activity of its collaborating companies.
- Ensure that any potential risk situations that may affect employees, suppliers, customers, the general public and the safety of facilities are brought to attention, assessed and managed in the appropriate manner.
- Work to maintain a risk-free working environment by integrating prevention of occupational risks and the protection and promotion of health and well-being.
- Establish learning as the driver of a safety culture, by means of ongoing training, accident and incident analysis, the dissemination of lessons learnt, education and the promotion of health.
- Incorporate health and safety criteria into business processes, new projects, activities, facilities, products and services, and in the selection and assessment of suppliers and collaborating companies, non-compliance with which will condition the commencement or continuity of their activity.
- Invest in new strategies of health education and health promotion, which allow the workplace to become the vector of transmission of healthy conduct for workers and their environment.
- Implement measures targeted at improving the quality of life, well-being and health of people within the communities where the company operates.
- Provide the resources and necessary means to enable compliance with established safety standards at all times.

How do we measure our performance?

Accident indicators

	2018		
	Total	**Men**	**Women**
Accidents requiring sick leave (Nº of employees)	28	25	3
Days lost	1,524	1,497	27
Mortalities	-	-	-
Frequency rate	1.00	1.30	0.35
Severity rate	0.055	0.078	0.003
Incidence rate	1.99	2.58	0.69

It does not include the information of Moldova, Kenya and South Africa. The accident rates including Moldova and South Africa are: No. of accidents with sick leave: 34, Days lost: 1,745, Mortalities: 1, Frequency rate: 1.138, Severity rate: 0.058, Frequency rate: 2.204.

Occupational illness

There have been no occupational illnesses registered in 2018.

Absenteeism

	Lost Hours [1]
Spain	382,147
Chile	250,980
Argentina	33,912
Brazil	15,749
Colombia	3,160
Costa Rica	813
France	3,836
Kenya	1,072
Morocco	2,899
Mexico	9,840
Moldova	33,415
Panama	8,790
Peru	152
Dominican Republic	3,184
South Africa	54,720
Uganda	313
Total	**804,981**

1. We have considered the hours of absenteeism for occupational illness and non-occupational illness, and the total number of hours worked in 2018 was 30,010,519.

What are our main milestones in 2018?

- Launch of the predictive health and safety analysis tool DaVis (Data Visualization).
- Introduction of the "Meeting Point" two-way information exchange channel with suppliers and collaborating companies.
- Launch of the security of consumers and communities management programme "Spear". The implementation of the new management model of health and safety training in the global scope of the company.
- Plan to assist employees while they are on sick leave.
- Consolidation of the healthy business model in countries already certified.

What are our goals for 2019?

- Horus: multi-factor analytical preventive analysis.
- Integra: exchange of best practices and learning through collaboration with collaborating companies.
- Kepler: ongoing innovation applied to prevention.
- Optimise the approach to cases of colon cancer.
- Optimise the approach to osteomuscular injuries.

Analysis of the 2018 results

Health and Safety Strategy

Safety as strategy guides the way in which Naturgy operates. Health and safety are key parts of the company's business strategy, which is referred to as the "Health and Safety Commitment", one of the major undertakings established in the Corporate Responsibility Policy. A common culture has been achieved in which all levels of the company, spearheaded by the Board of Directors, have acquired a firm commitment to continuous improvement in this area.

The preventive culture of health and safety at Naturgy has consolidated itself thanks to the evolution in 2018 of the "Health and Safety Commitment" throughout the company. The actions at all levels of the organisation are based on the motto "nothing is more important than health and safety".

Since 2017, the health and safety strategy has revolved around four pillars, leading to the development of different strategic objectives and goals to be achieved. The four pillars are:

- Consolidating health and safety as a strategic lever to align and to capture efficiencies.
- Maintaining Naturgy as a worldwide benchmark in health and safety issues.
- Drastically reducing the accident rate at collaborating companies.
- Implementing the commitment in all countries where the company will have a presence.

The Health and Safety Commitment Plan, implemented between 2012 and 2016, involved overcoming the implementation stage until we were able to reach the "Health and Safety Commitment".

First of all, we analysed the initial situation, which allowed us to characterise the integration and management of the company's commitment. Next, we established responsibilities for each one of the defined work areas and strengthened the management and dissemination tools. All this involved a major impulse for the new health and safety culture.

The definitive consolidation of the plan came about in 2016, with the "Health and Safety Commitment". Achieving the commitment has involved integration of health and safety as an ongoing and stable value, taken into consideration by everybody that makes up the organisation.

This new approach has closed a cycle whose driving force has been the ongoing improvement into the daily life of the company, the increased efforts to achieve the desired objectives and the proposal for innovative initiatives.

These new steps of the strategy maintain the four lines of action of the "Health and Safety Commitment": leadership, employees, collaborating companies, and facilities and processes, each one of which has its own "network" charged with spearheading development. Furthermore, the transversal networks continue working in the quest to provide support in areas such as communication, systems, training and corporate aspects.

The cultural change has served to transfer the company's principles of health and safety to daily activity, and it reaches our collaborating companies and any new businesses that join Naturgy.

Health and safety leadership

Leadership is considered the driver of cultural change in the company. This means efforts have to be made at all organisational levels, and promoted by the management, with a visible, solid and firm commitment in taking all decisions, with health and safety paramount at all times. Naturgy's commitment to the target of zero accidents is strengthened through the involvement of senior management in the management of safety in all activities.

Senior management and the various committees have the tools necessary and the power to control and apply the appropriate measures in the event of any sign or anomaly concerning safety issues in all activities and geographies.

Risk prevention

To ensure safety in the activities of Naturgy, measures aimed at preventing accidents and incidents have been introduced. Risk prevention is a key factor that governs business leadership and is supported on these principles:

1 Nothing is more important than health and safety	... not production, not sales, not profits.
2 All accidents can be avoided	... there are no inevitable accidents.
3 Safety is Management's responsibility	... and it must be managed as such.
4 Safety is an individual responsibility	... and a condition of employment, and of procurement for collaborating companies.
5 All work must be planned and carried out with a focus on safety	... ours, that of our employees, collaborating companies, visitors, customers and the community.

This is the commitment of Naturgy and also the one that must be shared and applied by its collaborating companies.

Furthermore, we have also developed mechanisms to learn from events that occur and to avoid them in the future. These actions revolve around the main cultural axes of the company's health and safety, the cornerstone of its commitment.

Risk assessment and management mechanisms

The process of occupational risk assessment aims to estimate the magnitude of those risks that could not be avoided. In these cases, the company obtains information for the adoption of effective preventive measures.

Naturgy uses a general procedure that applies to the entire group and which establishes the guidelines and principles to be followed for the identification, assessment and control of occupational risks. The following review periods are established:

- Risk assessments every three years.
- Yearly checks of the health and safety conditions.
- Monitoring of preventive measures to be introduced as a result of the risk assessment and regular checks every quarter.

Prevention of risks at collaborating companies: suppliers, contractors and subcontractors

Naturgy acquires the undertaking to provide a safe working environment not only for its employees but for all those who make the activity of the company possible.

For this reason, the growth of involvement of the collaborating companies within the health and safety culture has been essential.

Safety is an indispensable condition of procurement for all collaborating companies and is taken into consideration in the assessment and award of tenders and bids. Furthermore, the criterion of red lines that cannot be crossed is applied, and if this rule is broken the contract can be terminated or the supplier's approval withdrawn.

Naturgy develops other mechanisms designed to ensure that the safety level of collaborating companies is the same as for its own staff. In recent years an impact plan has been introduced for all collaborating companies of Naturgy. Among other things, this plan encompasses site inspections, the introduction of training itineraries, the application of Preventive Safety Observations, the creation of check-lists prior to commencement of works and the planning of coordination meetings.

Training and awareness

The training of each employee in the prevention of occupational risks and industrial security associated with their job is the basic tool for achieving the target of reducing the number of occupational accidents. To provide adequate training, the company receives support in management from the Occupational Risk Prevention Classroom, a tool that the Corporate University has in order to comply with the goals established.

Certifications

As included in the strategic lines of the commitment, the certification according to health and safety standards enables consistency and standardisation of working conditions at Naturgy.

The company has a Global Certification Plan for the Occupational Health and Safety System; its aim consists of achieving global certification according to the OHSAS 18001 international standard. For its fulfilment, multi-discipline working parties were created as advised by the Prevention Service.

Safety audits and process diagnostics

To verify compliance with the country's prevailing rules and regulations, Naturgy has conducted safety audits of the company's different technical processes, of the technical procedures introduced by the group and the own internal regulations of the business unit.

To contribute value to the business lines and to assist in the ongoing improvement of processes, there is monitoring and control of the operational risks concerning technology, accidents and malfunctions and impacts on the environment, and of the relevant management parameters.

As regards diagnostics, these are conducted on technical processes and on request by the different business units. The aim is to show the degree of control of the business, the monitoring mechanisms and, if anomalies are found, the appropriate actions for correction can be carried out.

Safety among customers and society

Naturgy conducts accident prevention campaigns for customers of the company, through giving advice that is communicated through the global communication channels.

Additionally, the company uses the bills as a direct communication channel with customers. The company uses the bill as a way of introducing, inter alia: campaigns to raise awareness and information on specific actions concerning situations of risk, and campaigns that explain good use of devices and the maintenance of these.

Health

Naturgy is firmly committed to offering its employees a healthy working environment and well-being. The Comprehensive Medical and Health Assistance Unit is based on excellence and ongoing innovation to make available to employees, their relatives, collaborating companies, customers and the social environment in which the company operates, a global, health and welfare strategy that encompasses everything necessary for their benefit, both with regard to prevention, promotion and health care, in a customised way, as well as training and information with regard to healthy habits, taking into account both individual needs as well as the particular circumstances of each country.

Master Health Plan

This plan defines the strategic guidelines and establishes the general framework for action of Naturgy in the field of healthcare, ergonomics and psychosociology. The responsibilities under the plan correspond to each and every one of the business areas and countries within the group. In addition, comprehensive medical and health assistance services act as advisers for the development, monitoring and control of the plan in each of the areas.

Master Health Plan targets	
Standardised actions	Ensuring the health of workers, developing standardised actions respecting differences inherent in each country.
Compliance with regulations	Monitoring compliance with the relevant regulations to each area in health.
Development of activities by external collaborators	Coordinating the development of activities by external collaborators and establish monitoring and control measurements.
Definition of indicators	Defining the indicators necessary to assess the implementation and development of the Master Health Plan, as well as all of the involved activities.
Continuous training	Ensuring continuous training of professionals in the activity, information about the latest technological developments and promoting creativity for innovation.

6.7. Supply chain

What does it mean for Naturgy? Risks and management approach

Suppliers and collaborating companies are key players in the optimum performance of the value chain of Naturgy, and the company therefore promotes relations based on trust, that are stable, sound and of mutual benefit, under the principles of transparency and risk management.

Naturgy establishes objective and impartial mechanisms of assessment and selection of suppliers, ensuring that the supply chain complies with the principles set out in the Supplier Code of Ethics, to which all suppliers have to adhere and the content of which comes from the Code of Ethics of Naturgy, from the Human Rights Policy, from the Health and Safety Policy, from the Anti-Corruption Policy, as well as the internationally acknowledged good governance principles.

The risks to the company extend beyond its activity, as it can be severely impacted by the inadequate performance of its suppliers and contractors in terms of the environment, health and safety, human rights, labour practices or corruption.

What is our commitment?

- Extending the culture of Naturgy to the supply chain, passing on the target of excellence in service, efficient use of resources and the company's principles of acting responsibly, and encouraging the incorporation of sustainability criteria in their daily management.
- Fostering compliance with the codes and policies of Naturgy in the supply chain, in particular in the area of human rights, ethics, health and safety and the environment.
- Encouraging the hiring of suppliers from the country or region where the company performs its activities against similar competitiveness in other locations, supporting the generation of a positive social impact.
- Fostering practices that encourage traceability and fair trade of raw materials at source.

How do we measure our performance?

	2018	2017
Total number of suppliers	8,670	9,877
Total purchase volume awarded (euros millions)	3,147	3,428
Number of ESG assessed suppliers	6,906	4,758
Number of critical suppliers	2,584	2,457
Official-approval suspended suppliers	1	7

Environmental, Social and Governance (ESG): The suppliers ESG assessment is conducted at the main subsidiaries of the group where the Achilles tool is implemented, and through which the business classification of suppliers is carried out.

NB: Two thirds of the overall amount awarded corresponds to service suppliers that fundamentally take part in the following business areas:
• Development and maintenance of grids, both natural gas and electricity.
• Operators and maintenance workers of energy plants.
• Commercial management services.
The remaining third corresponds to suppliers that provide materials required for the construction and maintenance of grids and plants, as well as those support services that complement the general activity.
The development of this activity essentially takes place in the following geographical areas: Argentina, Australia, Brazil, Chile, Costa Rica, Spain, Kenya, Morocco, Mexico, Moldova, Panama, Peru, Dominican Republic and South Africa.

The evolution of data with regard to 2017 reveals a decrease in the purchase volume, number of suppliers and number of suppliers assessed. The decrease of the purchase volume is fundamentally due to the divestment in Italy, in some companies in Colombia (those that represented the highest volume) and to a lower business volume in Mexico (Euros 135 million) and Australia (Euros 85 million). In general, there has been a decrease in the remaining countries except Chile, which in 2018 contributed a higher amount (Euros 160 million more) through business growth.

As regards the number of total suppliers and suppliers assessed, the change is due to the removal of Italy and the companies in Colombia, and the increase of critical suppliers is due to the entry of new suppliers in Chile through business growth generally associated to critical activities.

What are our main milestones in 2018?

- Conducting audits at suppliers of any country of the group with the highest purchase volume in activities with a high ESG risk.
- ESG audits conducted with tier-2 suppliers.
- Review of the ESG risks matrix.

What are our goals for 2019?

- Quarterly monitoring of successful suppliers based on reputational, economic-financial and CSR ratings of external data sources.
- Introduction of the updated risk matrix throughout the group.

Analysis of the 2018 results

The supply chain of Naturgy

Suppliers, contractors and outsourced partners are key players in the optimal functioning and sustainable management of the value chain, demonstrating Naturgy's commitment as an efficient, responsible and innovative company, in a process of continuous improvement that guarantees safety, reliability and competitiveness of the supply chain.

In 2018, Naturgy set up trade relations with a total of 8,670 suppliers which accounted for a total expenditure of Euros 3,147 million.

Naturgy performs the procurement of works, goods and services, as well as the assessment, monitoring and development of suppliers in accordance with the general principles established in the company's policies, rules and procedures, as well as internationally recognised principles of good governance, ensuring a uniform, efficient and sustainable model.

The main goals of Naturgy in terms of sustainability with respect to the supply chain are:

- Extend the corporate culture to the supply chain in a sustained way, passing on the objective of excellence in service.
- Guarantee sustainable management of the supply chain in an ongoing way, safeguarding the group's reputation.
- Promote continuous improvement and drive the development of suppliers by identifying opportunities for collaboration and innovation.

The values transmitted:

- Transparency: guaranteeing fairness, independence and free competition.
- Integrity: we commit to acting with honesty, fairness, dignity and morality.
- Sustainability: the strategic horizon for our activities goes beyond immediate economic interests, contributing to economic, environmental and social development.
- Commitment to results: we develop plans, fix objectives and make decisions that comply with the objectives of our Vision, assuring compliance with the commitments made.

Management of the supply chain

Purchasing model

The Purchasing and Supplier Management Model introduces a management process with unified and overarching criteria for Naturgy's entire scope of operations. The corporate unit is responsible for defining the policy, general principles and the model of application and for ensuring compliance. The business units develop, implement and ensure traceability of the processes of contracting and management of suppliers, applying the established principles.

We encourage the aggregation of demand in purchases in which there is a single supplier market that covers most of the group's business needs and countries. In the remaining cases, the contracting of suppliers from the country or region where the company performs its activities is encouraged, supporting the generation of a positive social impact through the creation of wealth and investment in the local community, generating economic inclusion in the company's spheres of influence.

Transparency in purchasing

In terms of procurement, Naturgy is committed to ensure free competition, objectivity, impartiality, transparency and traceability throughout the procurement process.

The use of secure electronic means, the Jaggaer Advantage platform, for management of all bids brings greater transparency to the procurement process and ensures information traceability. In addition, communication channels have been established with the supplier that facilitate access to all the information necessary for their participation in the procurement processes.

Naturgy actively participates at associations, national and international fairs on supply chain management. In this regard, the company is member of the Association Representing Purchasing and Materials Management Professionals in Spain (Aerce) and RePro in Argentina, Brazil, Chile, and Spain.

Furthermore, the company subscribes to the worldwide Procurement Leaders network and in 2018 took an active part in the CPOnet Congress.

Human rights at suppliers

Naturgy has a Human Rights Policy that extends to the supplier's Code of Ethics, thus transferring to the supply chain the commitment to protect Human Rights within their sphere of influence, especially since international growth has led us to operate in some environments where their protection takes on special relevance

Supplier Code of Ethics

Naturgy is keen to extend the corporate culture to the supply chain, ensuring that collaborating companies comply with the principles set out in the Supplier Code of Ethics, which all group suppliers have to adhere since 2016.

Reporting Channel

All suppliers, contractors and outsourced collaborating companies of Naturgy that wish to report a violation of the Code of Ethics that they may have observed in the exercise of their functions may contact the Code of Ethics Committee through the email address published in the Naturgy Supplier's Code of Ethics.

Supply chain management process

In order to promote responsible management in the supply chain, Naturgy has a comprehensive purchase process, with application of unified and universal contractual conditions for the company's entire sphere of operation and which is publicly available on the Naturgy website "The group's general procurement conditions" and where supplier management is of vital importance.

Risk management of the supply chain

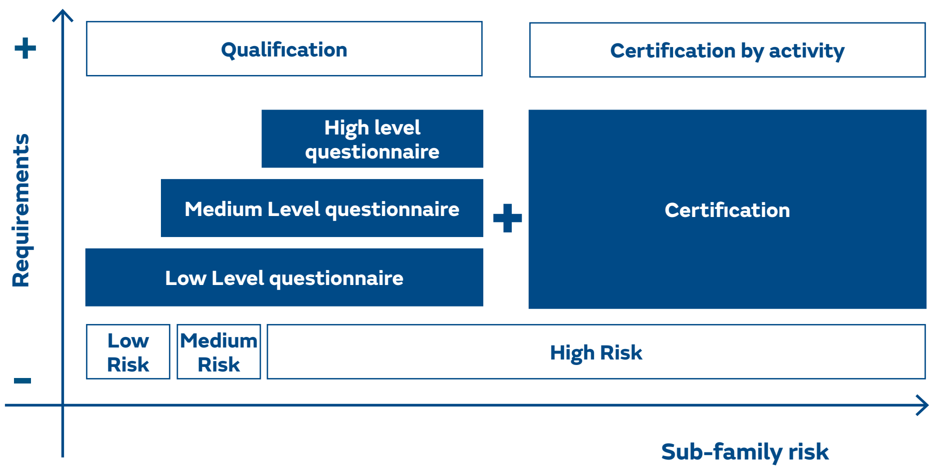
The risk factors of the supply chain are elements, conditioning factors or situations inherent to the same and which are considered significant in achieving our goals.

Risk factors assessed:

- Health and safety: this measures the potential risk of an incorrect action, service and/or product fault with regard to the life or physical integrity of persons.
- Quality: the impact that breach by the supplier with regard to the expected or agreed quality levels would have at Naturgy.
- Environmental, social and corporate governance (ESG): this measures the existing risk of purchasing products or contracting services that are not environmentally friendly, which are manufactured or generated under socially unfair conditions, or using labour practices that are ethically incorrect. Naturgy performs "responsible purchasing" through a management process that encourages the acquisition of products and services that are environmentally friendly, and which are manufactured under socially fair conditions.
- Operational risk: the potential impact on operations incurred by Naturgy as a consequence of a lack of continuity in the supply of a good or service by suppliers that have been awarded contracts.
- Legal risk: possibility of infringements and breaches by providers of laws, rules and practices that apply to them.

Assessment of suppliers

Assessment of suppliers is introduced in the processes of Business Classification of suppliers and Approval of suppliers and products.



With the risk evaluation of the purchase categories that are managed worldwide and assessing the risks of the countries where the company usually contracts, we obtain the risk of each purchase category in accordance with its activity and the country where the activity is conducted.

This combination allows us to assign a high, medium or low risk to each purchase category, which is integrated into the map, thus obtaining the risk of each purchase category by country.

Suppliers with a high level of risk in any of the assessed risk factors associated with the purchase categories they supply will be considered by the company as critical suppliers.

Naturgy also identifies the "suppliers with high risk in sustainability", considering those that reveal a high-risk level in the Health and Safety and ESG factors.

Supplier classification

This process is based on the assessment of compliance at business level of what is required by Naturgy in the different risk factors, in order to participate in the procurement process of goods and services. All suppliers must pass this process before maintaining commercial relations with Naturgy.

The classification is conducted using self-assessment questionnaires that take into consideration legal, economic-financial, criminal, solvency, experience, business organisation, quality, safety, human rights, environmental, social and employment practices criteria.

Official approval and management of supplier quality

Naturgy has introduced the goal whereby all suppliers that perform critical activities through being defined with a high risk in any of the ESG, quality and health and safety risk factors must be approved.

The approval process is based on audits conducted at the supplier's facilities or by distance depending on the critical nature, to check compliance with the specific requirements defined for the service or material. Any non-compliances detected during the audits lead to corrective actions that the supplier must introduce within the deadlines agreed between Naturgy and the supplier, and this deadline is always less than one year.

Naturgy also approves the Non-Tier 1 suppliers corresponding to categories of purchase of critical products, over which audits are conducted based fundamentally on quality-related aspects.

Products corresponding to critical categories may be subjected to inspections, technical acceptances or FAT at the production centres before the material is shipped.

Every year approval plans are drawn up to audit suppliers in-situ. These approvals are for an open-ended period depending on the critical nature of the service or product and the purchase volume.

The approval process may unveil anomalies that lead to a plan of corrective actions, or the non-approval of the supplier, which would prevent such supplier from performing this activity for Naturgy.

The corrective action plan identifies the development actions and corrective actions to be introduced to achieve compliance with the requirements and standards established by the company.

During 2018 one supplier was suspended and disqualified from holding a contractual relationship with Naturgy for significant breaches related to security, quality and other aspects.

Monitoring, follow-up and development of suppliers

The Supplier Code of Ethics sets out that suppliers must take the utmost care to preserve the image and reputation of Naturgy in their professional actions and to monitor the respect and proper use of Naturgy's image and corporate reputation by its employees and that of its subcontracted companies.

In addition, other analyses based on reputational risk and corporate social responsibility are carried out with suppliers assessed as suitable at the high-risk level.

In 2018 no supplier was disqualified on the grounds of fraud or unethical practices.

Performance follow-up is carried out on the most relevant suppliers with a contractual relationship with the company and this involves carrying out surveys with the Naturgy units to measure their level of satisfaction with the suppliers.

Regarding the development of suppliers, one of the most important aspects is to extend Naturgy's culture to the supply chain, performing actions that allow the company's values to be transferred.

During 2018, Naturgy continued to form part of Bettercoal, an initiative launched by the main European utility companies for the purchase of coal from suppliers that comply with a series of social, environmental and corporate governance criteria, and was represented on its Board of Directors. Over the year, 94% of coal purchased by Naturgy was from mines that had agreed to follow an evaluation process with regard to these criteria.

6.8. Commitment to society

What does it mean for Naturgy? Risks and management approach.

Naturgy is committed to the economic and social development of those regions where it performs its activities, providing expertise, management capacity, as well as spending part of its profits on social investment. Fluid and ongoing dialogue with society enables to be aware of the expectations and interests of those communities where it operates and thus be able to involve itself in their development.

Inadequate management in access to energy can cause significant costs through non-payments and theft of electricity. By the same token, depriving vulnerable groups from receiving energy could have an impact on the company's reputation.

The lack of involvement and participation with local communities and their needs in those territories where the company operates could result in rejection and unease in the community, which could lead to lobbying for the company to cease its operation in these territories.

What is our commitment?

- Guarantee fluid and two-way dialogue and to encourage involvement in local communities, respecting the culture, rules and the environment, so that their concerns are responded to appropriately and expeditiously.
- Assess the social impact that the company's activity could cause, to avoid or mitigate the adverse effects these could generate and to foster positive effects.
- Develop initiatives to create shared value and to have a positive social impact in energy projects.
- Promotion of education, cultural wealth, health, research and the inclusion of the more underprivileged collectives through social investment.
- Transfer knowledge and values to society through partnership agreements with the academic community and the supply chain.

How do we measure our performance?

Sponsorship and social action investment

	Million euros
Sponsorship and social action investment	11

What are our main milestones in 2018?

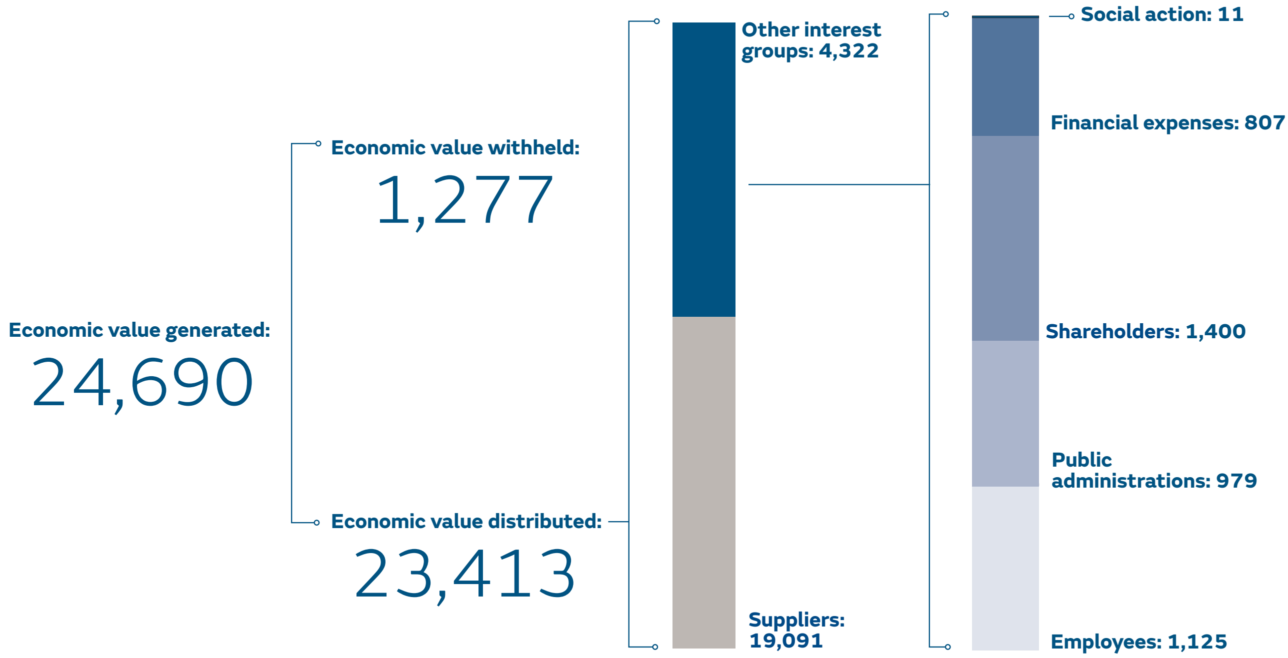
- Launch of the Energy Vulnerability Social Fund.
- Review and update of the General Regulations on Sponsorship and Donations.
- Launch of actions to support dissemination of the Vulnerability Plan and the promotion of energy efficiency.

What are our goals for 2019?

- To continue promoting the Energy Vulnerability Plan
- Approval of the General Procedure of Sponsorship and Donations and its introduction in all countries and societies.
- Smart energy and mobility to improve air quality

Analysis of the 2018 results

Economic Value Distributed. Detail by group of interest (euros million)



Sponsorship and social action investment

Economic contributions to social investment and sponsorship programmes are another important part of the Naturgy commitment. In 2018, they totalled Euros 11 million.

The aim of the company is to generate a higher corporate commitment to society of which it forms a part. The programmes to which these resources are therefore allocated form part of the business development strategy.

Creation of wealth and well-being where the company operates

Naturgy develops its commitment to society through four main lines of action that are aligned with the company's core activities:

1. Energy vulnerability

Naturgy performs its activity in areas where the energy supply does not reach the entire population. The company considers it a priority to reach the people that live in these areas. This is why it actively works in developing its distribution networks to offer these populations a service under safe conditions.

The company has extensive experience in this regard. Accordingly, the project carried out at Cuartel V in Argentina or the CGE group agreement in Chile made it possible to provide access to clean and reliable energies to tens of thousands of people.

Energy Vulnerability Plan in Spain

During 2018, Naturgy, together with the Foundation, continued the development of the Energy Vulnerability Plan throughout Spain to protect vulnerable customers. The plan has become a new core focus; the actions to mitigate energy poverty are now a priority for the Foundation.

The objectives of the plan are:

- Improve management and customer relations in cases of energy vulnerability.
- Streamlining the exchange of information with town and city councils for better identification of situations of vulnerability.
- Implementing activities with associations that work to alleviate energy poverty cases and to detect vulnerabilities.

During this year there have been three new initiatives:

- Creation of the Energy Rehabilitation Solidarity Fund, to finance improvements at vulnerable homes through donations from individuals and a contribution from the Foundation.
- Job Circle project: commencement of a training course to refurbish 15 homes, performed by long-term unemployed persons with an undertaking from the companies to recruit 25% of course participants.
- Social entrepreneurs: we have strengthened the corporate volunteer programme with this initiative, the purpose of which is to enable Naturgy employees to encourage initiatives promoted by not-for-profit organisations and which are related to energy (energy poverty, energy efficiency) and the environment.

2. Relationship with communities

Naturgy, under its Human Rights Policy, makes a firm commitment to the respect of local communities. To achieve this commitment, the social impact that the company activities may have on affected communities and contributing to improving the living conditions of these communities are key aspects.

Naturgy has a method based on the Measuring Impact methodology of the World Business Council for Sustainable Development (WBCSD) and the aim is to define initiatives and programmes for the effective management of social impacts associated with the company's business.

The company bases its relationship with communities on the following principles:

- Identifying communities affected by the company's activity and finding out their needs and aspirations.
- Analysing the potential environmental and social impacts that its activity could cause in the communities, using the social impact assessment methodology designed for this purpose.
- Reporting to, and inviting participation from, the community at the different stages of the project through a consultation procedure that enables us to listen to their concerns and questions as well as benefit from their contribution.
- Incorporating the opportunities identified through dialogue with the communities and which encourage sustainable development of the community into the impact assessment studies.
- Introducing a system of communication and relations with communities that ensures that these communities receive project information in a clear, updated and efficient way.

The company currently prioritises the performance of social impact assessments in those locations where the company is looking to carry out new investment projects. These assessments serve to measure numerous impacts (positive and negative) that the company may produce as a consequence of its activity, both in local communities as well as in the territory. These include:

- Impact on human rights.
- Displacement or relocation of local communities.
- Modification to the traditional ways of life.
- Changes in the traditional uses of territory.
- Attracting new technologies.
- Creation of skilled and unskilled jobs.
- Temporary occupation of the communication routes.
- Impact on landscapes.
- Noise.

The most prominent projects in this sphere are:

- Bujagali hydroelectric power station (Uganda): with local procurement programmes, development of suppliers, health and prevention, training and the fight against energy poverty.
- Biĭ Hioxo wind farm (Mexico): with actions to support fishermen, improve highways and delivery of material, support to the fire brigade, health campaigns, improved education infrastructures, support to culture and technology and guided tours of the wind farm.
- Nairobi thermal power station (Kenya): with education support programmes, health campaigns, environmental protection and promotion of art and local culture.
- Torito hydroelectric power station (Costa Rica): with support to local schools with the supply of academic material. As well as improvements along the local roads surrounding the power station.
- La Joya hydroelectric power station (Costa Rica): with support to local schools with the supply of academic material.
- CGE (Chile): development of a plan to encourage relations with social organisations to foster their links with neighbourhood councils, through participatory meetings.

During 2018 we started implementation of the Quilombola Basic Environmental Project (QBEP), associated to the Sobral I photovoltaic plant in the municipality of São João do Piauí (Piauí, Brazil) as a measure to mitigate and offset the impacts this facility could cause in the local communities of the territories of Riacho dos Negros and Saco/Curtume. To carry out this project, we mobilised a social manager responsible for channelling ongoing communication between the company and the local community, supporting the introduction of the measures developed in the QBEP.

The project involves 4 action lines and 12 activities, of which the following have been implemented this year:

- Mobilisation of the social technical team required to undertake ongoing communication with the community, and introduction of the QBEP measures.
- Meetings and workshops to disseminate and gather information.

- Collection of information about wells in the region that could be improved with the set-up of a solar pump kit.
- Collection of information on the needs and expectations of technical and higher training for young people in the region.

3. Social action

In 2011, when the Latin America Operational Centre was created, pillars were established, and social investment programmes designed for unified development in all countries where the company has a presence.

Types of COIL projects	
Inclusive business	Projects that promote the inclusion of the most disadvantaged social sectors through inclusive programmes. For this project type, we continued with the programme called Energy of Flavour, launched in 2016, which aims to promote social inclusion of disadvantaged groups through training linked to gastronomy. Through the Training Classrooms programme we offer a training workshop on the ceramics technique which since last year has integrated persons with mild intellectual disability.
Responsible consumption	Encompasses projects targeted at providing knowledge about energy in general, safety and efficient use, of both gas and electricity. They also promote environmental stewardship among customers and society. As part of this pillar, the following traditional programmes were carried out: • Responsible Consumption of Gas, in versions for children and adults. • Responsible Consumption of Electricity, in versions for children and adults. In 2018 we created the Sowing the Future programme through which we created a vegetable garden at a school in Buenos Aires together with the students. To achieve this, the students were trained and instructed in the acquisition of expertise and the development of theoretical and practical skills to be able to set up the vegetable garden and maintain it over time.
Talent promotion	This pillar promotes projects that foster the studies and access to employment for the children and relatives of collaborators: • The "Planning your Future" programme provides a financial grant for those who are starting college. • "Natural Vocation" seeks to contribute to the vocational and professional decision process that relatives of collaborators go through. • "Summer Internship", offers the possibility of work experience in the company in the summer months.

4. Sponsorship, patronage and donations

The resources assigned to cultural, social and environmental programmes pays special attention to those community projects that generate greater value for society, while also strengthening the company's commitment to positive integration in each community and country where the group operates.

Through the General Regulations on Sponsorship and Donations of the company, the general management principles are established for sponsorships and donations by the company and to define the processes that regulate and control its development. Similarly, activities related to sponsorship and donations are subject to a process of 100% transparency. The regulations also provide priorities, which can be summarised in social action, culture and energy, and the environment.

- Educational initiatives: Naturgy carries out educational activities for young people on the correct use of energy and sustainable development. By the same token, the company implemented a wide range of collaboration, participation and sponsorship initiatives with different educational entities in Spain and Latin America.
- Social action focused on underprivileged groups: the company drives, and support projects targeted at integrating the most vulnerable social groups and to mitigate problems stemming from social exclusion. It therefore collaborates financially with foundations and associations whose corporate purpose is to help mitigate or minimise these problems in some of the countries where it performs its activity.
- Promotion of health and research: among the different programmes in which Naturgy participates to promote research and health, we can highlight research targeted at improving the life quality of the infirm and their relatives, or research into cardiovascular diseases, which are the leading cause of mortality worldwide, through the Procnic Foundation, as well as with other international entities.

- Promotion of music, theatre and films: Naturgy maintains its undertaking to contribute towards the development of culture that goes beyond its business activity and which involves extensive sponsorship work in initiatives that generate high value for society. We sponsor musical cycles and artistic seasons of different institutions throughout the territory.

- The company's support to the Gran Teatre del Liceu and the Teatro Real have been strengthened with twin celebrations declared to be "events of exceptional public interest".

Corporate volunteers and employee participation

Through corporate volunteering, Naturgy aims to promote social cohesion, values and a spirit of solidarity.

To achieve this, Naturgy has defined the programme objectives in three areas simultaneously -corporate, employees and the environment-, and an integrated structure of committees that includes both the areas of people as well as communication and the environment of all countries that form part of the programme.

During 2018, the company has promoted environmental, social and energy volunteer actions, in which employees contributed their time and their personal and professional skills.

Naturgy Foundation

The Naturgy Foundation, founded in 1992 by Naturgy, and with a presence in those countries where the company is active, is tasked with the dissemination, training, information and raising society's awareness in issues of energy and the environment, as well as the development of business and academic programmes. It also develops social action programmes in the national and international arenas, with a particular focus on actions targeted at relieving energy vulnerability.

During 2018, the foundation continued to provide seminars on energy and the environment in Spain, as well as presentations of the book Air quality in cities. A worldwide challenge; taking advantage of the presentations to give temporary exhibitions about air quality in Barcelona and Guadalajara. There was also an exhibition about "Smart Ports" in Málaga. One new item this year has been the commencement of two new action lines as part of the "energy and technology" and "smart energy and mobility" sphere.

In 2018, to once again drive its educational activity and provide access to its teaching programme throughout the territory, the Foundation turned the Gas Museum into a travelling one. This allowed us to multiply the Foundation's participation throughout the year in a great many anniversaries related to education of technology in the energy sphere, through innovative and flexible agendas adapted to all kinds of audiences.

The international activities of the Foundation were developed in seven countries: Algeria, Argentina, Brazil, Chile, Morocco, Mexico y Panama.

6.9. Integrity and transparency

What does it mean for Naturgy? Risks and management approach.

Naturgy considers that the trust of its stakeholders is based on integrity, which is understood to be action which is ethical, honest, responsible and in good faith of each one of the people who work in and for the group.

To respond to the risks related to integrity and transparency, Naturgy has developed a series of mechanisms that introduce the guidelines that are to cover ethical and transparent behaviour of the directors and employees of the company and their daily performance, as set out in the Code of Ethics, the Anti-Corruption Policy, the Human Rights Policy and the Fiscal Policy of Naturgy.

Corruption, fraud and bribery can have a major impact for the company, leading to sanctions imposed by the administrations, loss of contracts, legal consequences, loss of customers and loss of reputation that could also see investors disappear or the non-purchase of shares by investors that consider these aspects in their investment decisions.

What is our commitment?

- Reject corruption, fraud and bribery in business dealings and establishing measures to prevent and combat them, developing internal channels allowing communication of irregularities while preserving anonymity.
- Comply with national and international laws and standards in force in which the company operates, in particular, abiding by the principles expressed in the United Nations Universal Declaration of Human Rights, in the Declaration of the International Labour Organisation (ILO), in the United Nations Global Compact, in the United Nations Guiding Principles on Business & Human Rights, and the OECD Principles of Corporate Governance.
- Act with responsibility in management and complying with fiscal obligations in all jurisdictions in which the company operates, undertaking to act transparently and collaborate with tax authorities.
- Compete fairly on the market and prevent misleading, fraudulent or malicious conduct through which the company could obtain an unfair advantage.
- Promote transparency in information and responsible, truthful, efficient, complete and timely reporting, with regular publication of financial and non-financial information to measure the company's activities.
- Maintain, at all times, permanent dialogue with stakeholders through adequate and accessible channels.

How do we measure our performance?

Queries and notifications to the Code of Ethics

	2018	2017
Queries	76	37
Notifications	123	104
Total	**199**	**141**
No. of messages received per 200 employees	**3.18**	**1.67**

What are our main milestones in 2018?

- Analysis, content design and drafting of the Conflict of Interest Policy.
- Launching of the Compliance Communication Plan (Campaign "Compliance Café").

What are our goals for 2019?

- Approval and dissemination of the Conflict of Interest Policy.
- Update of the Corporate Responsibility Policy.
- Audit the implementation of the Human Rights Policy.
- Approval of update of the Human Rights Policy text to concepts and terminology of the United Nations Guiding Principles on Business & Human Rights.

Analysis of the 2018 results

Code of Ethics Management Model

The Code of Ethics of Naturgy, formulated and approved by the Board of Directors, is the document that establishes guidelines that must govern the ethical behaviour of managers and employees of Naturgy, in their daily work, with regard to relationships and interactions with all its stakeholders. The principles for the company's employees are related to corruption and bribery, respect for people, professional development, equal opportunities, relation with collaborating companies, occupational health and safety, and caring for the environment, among others.

Since 2005, when it was adopted, the code has been regularly renewed to adapt it to the new situations that affect the company. The code sets out the undertakings entered into by Naturgy in the fields of good governance, corporate responsibility and questions of ethics and regulatory compliance.

In addition, Naturgy has an Anti-Corruption Policy, which establishes the principles which must be used to guide the conduct of all employees and administrators of the companies of the group with regard to the prevention, detection, investigation and correction of any corrupt practice within the organisation.

The company also has a Code of Ethics and an Anti-Corruption Policy Management Model, headed by the Compliance Unit, whose targets are to ensure the knowledge, application and fulfilment of the code.

This model also provides that the Audit Committee of the Board of Directors must receive regular reports from the Ethics and Compliance Committee on the most relevant issues related to the dissemination of and compliance with the Code of Ethics and the Anti-Corruption Policy. The Ethics and Compliance Committee, which in 2018 has fully assumed the functions that were previously performed by the Code of Ethics Committee, is responsible for supervising the dissemination and compliance with the Code of Ethics and the Anti-Corruption Policy through supervision and control of the safeguard systems:

- Whistleblowing channel (the "Code of Ethics Channel"), through which all the employees and suppliers can send the Ethics and Compliance Committee queries or notify breaches of the code, in good faith, in a confidential manner and without fear of reprisal.

- Annual declaration procedure: through which all the employees repeatedly declare that they have read, understood and comply with the code.

- Online courses: on the issues included in the Code of Ethics and the Anti-Corruption Policy, mandatory for all employees. Certain groups of employees also receive classroom training sessions on a range of issues in the sphere of regulatory compliance, which include the content of the Code of Ethics.

In 2018, 24% of the notifications received were related to alleged fraud, none of which had any significant impact.

No notifications were reported related to labour or child exploitation or in relation to the rights of the corresponding local communities and human rights.

A total of 24% of the notifications were related to the people management, and they were all solved appropriately.

In 2018, it was not necessary to repair damages relating to impacts caused by human rights cases.

In 2018, the work plan of the Ethics and Compliance Committee included:

- Project to improve the Code of Ethics Channel.

- Training and informative actions on the Code of Ethics, Anti-Corruption Policy and Corporate Hospitality Policy, targeted at the company's employees.

- Collaboration with the Supply Unit to introduce improvements in communications and supplier evaluation related to compliance with the Code of Ethics.

- Updating of the Code of Ethics.

The company has introduced local committees in countries where the company has the greatest activity. The main mission of these is to make everyone aware of the Code of Ethics and the Anti-Corruption Policy and to reproduce the functions the committee carries out in Spain in each country to cover the company's entire sphere of operation.

Code of Ethics chapter to which notifications refers	Queries	Notifications	Total
Respect for the law, human rights and ethical values	3	3	6
Respect for the individual	1	35	36
Professional development and equal opportunities	2	13	15
Cooperation and dedication	-	2	2
Occupational health and safety	-	2	2
Corruption and bribery	17	23	40
Use and protection of assets	-	3	3
Irregular payments and money laundering	-	-	-
Corporate image and reputation	2	1	3
Loyalty to the company and conflict of interest	30	13	43
Processing of information and knowledge	3	1	4
Customer relations	13	14	27
Shareholders relations	-	1	1
Relations with collaborating companies and suppliers	5	10	15
Respect for the environment	-	2	2
Total	**76**	**123**	**199**

Crime Prevention Model

The company has a Crime Prevention Model which is updated annually. Thus in 2018, the model was subject to a process of adaptation to the new organisational structure in force at Naturgy.

The model incorporates the already established Naturgy internal control structure. Its purpose is to effectively prevent the occurrence of offences under the Organic Law 5/2010 governing the Amendment of the Penal Code. This modification introduces in Spain the criminal responsibility of artificial persons in cases in which they do not exercise due control over the systems of individuals subject to their authority.

The model contains 18 crimes that have been identified, together with definitions of their impact and probability of occurrence, mechanisms for their control and minimisation, and responsibilities with regard to their fulfilment.

Worldwide, the group has deployed crime prevention models in countries with laws governing the civil liability of legal persons.

During 2018, we have continued with the online training course mandatory for all employees on the Crime Prevention Model, the Code of Ethics and the Anti-Corruption Policy in order to emphasise the importance of compliance, ensure implementation of preventive and control activities and to inform all employees of the current status in these matters.

Anti-fraud and anti-corruption policies and plans

Although fraud and corruption are covered in the crime prevention system, the company worked to improve and update its internal regulations and define specific protocols and mechanisms in this area.

The Naturgy Anti-Corruption Policy complies with national and international legislation on corruption and bribery.

This policy has the object of establishing the principles which must be used to guide the conduct of all employees and administrators of the companies of Naturgy with regard to the prevention, detection, investigation and correction of any corrupt practice within the organisation. It covers all the actions in this area and avoid conduct that may give rise to fraud or corruption and lead to situations that are damaging for the company, its administrators and employees from a legal point of view or in relation to its reputation.

The policy establishes 14 principles of action, including aspects such as promoting integrity and transparency in the processing of information, money laundering, conflicts of interest and relationships with third parties.

The focus of the Naturgy Anti-Corruption programme covers three key areas:

- Establishment of an anti-fraud and anti-corruption culture through training and awareness.
- Implementation of proactive measures to assess the risk of fraud and corruption, monitoring and controls.
- Development of measures and response plans in the event of situations that constitute fraud and corruption. These plans and measures include the investigation of the episodes, the definition of solutions and the establishment of disciplinary measures.

Naturgy organises regular training initiatives based on the programme with the aim of raising awareness of the importance of fighting against corruption and ensuring that administrators, employees and suppliers are given enough and appropriate information to act accordingly.

Some of these regular initiatives include the following:

- Update of the NaturalNet space which concerns the Code of Ethics and the Anti-Corruption Policy.
- Publication of information about the Ethics and Compliance Committee activities (notifications received, activities carried out, etc.).
- Training course on Crime Prevention Model, Code of Ethics and Anti-Corruption Policy.
- Specific training in relation to the Crime Prevention Model and Anti-Corruption Policy for new employees and administrators.
- Presentations in Boards of Directors and Management Committees of the Crime Prevention Model.
- Regular declaration of compliance with the Code of Ethics and Anti-Corruption Policy.

Likewise, Naturgy has introduced a Corporate Hospitality Policy, within the framework of the Code of Ethics and the Anti-Corruption Policy. The purpose of this policy is to regulate the conditions in which the directors and employees of Naturgy can accept/offer business courtesies from or to their business counterparts within the framework of performing their professional duties, to ensure effective compliance with the principles set out in the Code of Ethics and in the Anti-Corruption Policy of Naturgy.

The directors and employees of the group cannot accept or offer, whether directly or indirectly, business courtesies for the purpose of improperly influencing their commercial, professional or administrative relations, whether with public or private entities.

In 2018 there was a specific dissemination campaign concerning the Corporate Hospitality Policy, targeted at all employees and, in addition, one of the modules of the “Compliance Café” campaign carried out in the same year was exclusively dedicated to this Policy.

In addition, in all operations involving risk, the company conducts due diligence processes systematically, both for high-risk suppliers, and company relationships with third parties (partners, joint ventures, etc.).

The counterparty due diligence procedure aims to ensure that, across the board, reputational risk and corruption are analysed and assessed efficiently and in a standard way when third parties intervene in business relationships of the companies forming the group.

Naturgy has the mechanisms, procedures and policies that seek to prevent and, where appropriate, detect and react to those possible breaches in the area of prevention of money laundering that are detected in the performance of its activity.

We can divide these measures into three control levels that seek to prevent, detect and, if appropriate, react to money laundering:

- Prevention: both the Naturgy Code of Ethics as well as its Anti-Corruption Policy have specific sections that expressly establish the prevention of money laundering as one of the principles that presides over the operations of the company and all of its employees. All Naturgy employees receive training on the content of the Code of Ethics, the Anti-Corruption Policy and the conduct guidelines that they must heed.

  In addition, Naturgy has other more specific policies and procedures that establish a full series of controls in its day-to-day work and in the operations it performs, which encompass the prevention of money laundering. Key among these are the counterparty due diligence procedure; the general external procurement standard; the procedure on granting the signing level, or the internal control procedure for the processing of payments and cash movements, among others.

- Detection: some of the foregoing policies and procedures also allow the risk of money laundering to be detected.

  Every year, those in charge of controls at Naturgy are subject to a self-assessment in the Crime Prevention Model on compliance with the same, including those where there is a risk of potential money laundering. In addition, to ensure efficiency of this model, it is reviewed regularly and audited every year by an independent expert.

  Internal Auditing periodically reviews the different processes of Naturgy to detect possible breaches that may have occurred in the different operational risks. These reviews include checks of revenue and payments that may be subject to the risk of money laundering.

  Naturgy also has an Internal Control System on Financial Reporting that is audited every year by an independent expert.

  In addition, Naturgy provides both its employees as well as stakeholders with channels so they can report to the Ethics and Compliance Committee concerning any breach or irregular or suspicious conduct in this area. They can perform these communications through the website channel of the Naturgy Code of Ethics or through ordinary or internal mail. In addition, in accordance with what is permitted under new data protection legislation, these communications may be carried out anonymously.

- Reaction and response: Naturgy has an investigation and response protocol as well as a disciplinary system so that, if it becomes aware of any denouncement or irregularity it can introduce all measures within its reach to rectify this and, if appropriate, adopt the measures required to prevent future repetition.Furthermore, Naturgy collaborates with the competent authorities of each country in the fight against money laundering and the financing of terrorism, furnishing all the information they request in accordance with prevailing regulations. The company also reports any suspicious transactions.

Fiscal policies

Tax strategy and tax risks control and management policy

At a meeting on 9 January 2018, the Board of Directors approved the Tax Strategy and Tax Risks Control and Management Policy, which sets out the basic principles governing Naturgy's tax function and the main lines of action to mitigate and guide proper control of tax risks.

The basic principles governing Naturgy's tax strategy are as follows:

- Responsible compliance with tax obligations.
- A low tax risk profile.

- Adoption of tax treatments based on economic reasons.
- Transparency of tax information.
- Cooperation with the tax authorities.

The main lines of the Tax Risks Control and Management Policy are as follows:

- Tax governance clearly defined.
- Procedures for controlling the tax risk arising from compliance.
- Procedures for assessing and controlling tax approaches where there is uncertainty.
- Oversight of the performance of the Tax Control Framework.
- Regular reporting of the tax situation to the Board of Directors.

All of Naturgy's tax policies are aligned with:

- The Naturgy Corporate Social Responsibility Policy, in which one of the commitments and principles of action is to "adopt responsible business management practices and comply with all tax obligations in all jurisdictions in which the company operates, accepting the commitment to accountability and collaboration with the corresponding tax agencies."
- Naturgy's Code of Ethics, which establishes that "All employees of the group must comply with the laws in force in the countries where they conduct their activities, thereby heeding the spirit and objectives of the laws and behaving ethically in all their actions".
- The Code of Best Tax Practices (CBTP), approved on 20 July 2010 by the Plenary session of the Large Business Forum, a body established by the Spanish National Tax Agency with Spain's largest companies, including Gas Natural SDG, S.A. The CBTP contains recommendations by the tax authorities, which Naturgy has adopted voluntarily, that are aimed at improving the application of the tax system by enhancing legal certainty, reducing litigation, fostering mutual cooperation based on good faith and legitimate trust, and the application of responsible tax policies.

To align Naturgy's tax policies with these principles, the group has a General Regulation governing the Tax Control Framework, designed in accordance with the guidelines of the Organisation for Economic Co-operation and Development (OECD) for multinational enterprises, and for the design and implementation of a Tax Control Framework.

Naturgy also has a Risk Map that specifically identifies the tax risks and issues regarding the interpretation or application of tax law. The main matters with a tax impact are detailed in Note 21 "Tax situation" in the notes to the consolidated financial statements.

Tax havens

The incorporation or acquisition of undertakings domiciled in countries or territories designated as tax havens must be reported to the Board of Directors via the Audit Committee.

At 2018 year-end, the Naturgy Group did not have any company in a territory designated as a tax haven under the related Spanish regulations (Royal Decree 1080/1991, of 5 July, and Royal Decree 116/2003, of 31 January).

Buenergía Gas & Power, Ltd. (the company that indirectly owns a single industrial holding that engages in power generation using a combined cycle gas turbine in Puerto Rico (Ecoeléctrica, L.P.)), which was domiciled in the Cayman Islands and in which Naturgy holds a 95% stake, changed its domicile to Puerto Rico on 2 February 2018.

Gasoducto del Pacífico (Cayman), Ltd. (a dormant company acquired by the group as part of the CGE acquisition), which was domiciled in the Cayman Islands and in which Naturgy held a 52.2% stake, was liquidated on 12 January 2018 and dissolved and deregistered on 12 April 2018.

Tax contribution

Naturgy gives priority to fulfilling its obligation to pay the taxes that are due in each territory in accordance with the applicable regulations.

Naturgy's total tax contribution amounted to Euros 3,268 million in 2018 (3,272 million in 2017). The following table shows the breakdown of the taxes actually paid by Gas Natural Fenosa in each country, segmented into those that represent an actual expense for the group ("own taxes") and those that the company withholds from or charges to other taxpayers (third-party taxes):

	Own taxes						Third-party taxes								Total	
Country	**Income tax [1]**		**Others [2]**		**Total**		**VAT**		**Tax on hydrocarbons**		**Others [3]**		**Total**			
	2018	**2017**	**2018**	**2017**	**2018**	**2017**	**2018**	**2017**	**2018**	**2017**	**2018**	**2017**	**2018**	**2017**	**2018**	**2017**
Spain	**62**	**112**	**621**	**537**	**683**	**649**	**1,056**	**845**	**409**	**342**	**270**	**228**	**1,735**	**1,415**	**2,418**	**2,064**
Argentina	10	15	17	67	27	82	9	19	-	-	39	34	48	53	75	135
Brazil	52	51	46	67	98	118	73	74	-	-	13	7	86	81	184	199
Colombia	-	60	-	57	-	117	-	-	-	-	-	11	-	11	-	128
Chile	31	101	13	11	44	112	60	81	-	-	47	22	107	103	151	215
Mexico	71	66	2	4	73	70	39	57	-	-	13	19	52	76	125	146
Panama	6	10	7	9	13	19	-	-	-	-	4	4	4	4	17	23
Rest of LatAm	7	8	2	1	9	9	5	4	-	-	8	4	13	8	22	17
Total LatAm	**177**	**311**	**87**	**216**	**264**	**527**	**186**	**235**	**-**	**-**	**124**	**101**	**310**	**336**	**574**	**863**
Europe	**24**	**15**	**8**	**35**	**32**	**50**	**161**	**170**	**80**	**111**	**3**	**14**	**244**	**295**	**276**	**345**
Total	**263**	**438**	**716**	**788**	**979**	**1,226**	**1,403**	**1,250**	**489**	**453**	**397**	**343**	**2,289**	**2,046**	**3,268**	**3,272**

1. Income tax actually paid in the year that figures in the Cash Flow Statement in the Consolidated Annual Accounts. Does not include accrued amounts. The reconciliation between reported "income tax" and that which would result from applying the nominal tax rate in force in the parent company's home country (Spain) to "Profit before taxes" is detailed in Note 21 ("Tax situation") to the consolidated financial statements.
2. Includes energy taxes in Spain amounting to 306 million in 2018 (Euros 260 million in 2017), local taxes, employer social security contributions and other specific taxes in each country.
3. Includes basically employee withholdings and employee social security contributions.

Income by country

2018	**Million Euros**
Spain	**(3,297)**
Argentina	41
Brazil	37
Chile	106
Mexico	104
Panama	13
Rest of LatAm	(63)
Total LatAm	**238**
Europe	**237**
Total	**(2,822)**

Received Grants

The movements of the received capital grants are breakdown in the Note 15 of Annual consolidated accounts. The received amount is Euros 1 Million in 2018 (Euros 4 million in 2017). The amount of the received operating grants is detailed in the Note 24 of the Annual consolidated accounts and amounted Euros 1 million in 2018 (Euros 1 million in 2017).

Human Rights Policy

The company's commitment to respect for and protection of human rights is expressed in both the Corporate Responsibility Policy and the Code the Ethics. The Human Rights Policy, approved in 2011 by the Management Committee, defines and precisely establishes how the company believes it has to include these principles in its business management.

The Human Rights Policy acquires its full meaning in those locations where local legislation does not afford a suitable level of protection of human rights, and its compliance is horizontally integrated within the company and is the responsibility of each business area.

The policy establishes ten commitments, which were determined on the basis of the main risks that affect human rights in the company, and accepts the United Nations Guiding Principles on Business and Human Rights. It is also focused on the most important principles which have the greatest impact on the company's business.

Human Rights Policy Principles
1. Avoiding any practices which are discriminatory, or which might compromise people's dignity
2. Eradicating the use of child labour
3. Helping to ensure freedom of association and collective negotiation
4. Protecting people's health
5. Offering dignified employment
6. Commitment towards people linked to suppliers, contractors and collaborating companies
7. Supporting and publicly promoting respect for human rights
8. Respecting for indigenous communities and traditional ways of life
9. Protecting facilities and people on the basis of respect for human rights
10. Helping to fight corruption

The company encourages the policy to be known and to be complied with using a communication and training plan, which includes a compulsory online course for all employees, seminars based around explaining principles of the policy and conflicts which could arise, and guidance sessions about the policy and its role in business activity.

Naturgy undertakes to engage the resources necessary to guarantee the effective implementation of this Human Rights Policy. In this regard, the company regularly analyses the human rights issues that are applicable to its activity and will introduce mechanisms that enable it to assess the risk of breach of these in the environments in which it operates.

During the initial stages of investment projects, and in the analyses of the social and environmental impact, the company will consider their impact on the protection and promotion of human rights and will define indicators in this regard. Similarly, the company will introduce specific measures for management of potential impacts and risks to human rights from the projects and investments and will ensure that sufficient resources are targeted at the implementation of the corrective measures identified.

In the due diligence processes prior to formalisation of collaboration agreements, also with governmental agencies, the company undertakes to assess the human rights policies and practices of its counterparts and to act in accordance with the principles laid out in the policy.

Any breaches, whether of the policy or any other aspect related to the respect of human rights will be studied in accordance with the internal procedures, legal regulations and the prevailing agreements, and could give rise to disciplinary or employment measures as determined in the internal regulations and legislation.

Employees of Naturgy are obliged to report any breach of the undertakings set out in this policy to the company, confidentially and without fear of reprisals. Those people who, without being company employees, witness potential malpractice in this area may also report this.

6.10. Table of contents required by Law 11/2018, of December 28, 2018 amending the Commercial Code, the revised Capital Companies Law approved by Legislative Royal Decree 1/2010, of July 2, 2010 and Audit Law 22/2015, of July 20, 2015, as regards non-financial information and diversity

Content	Page	Reporting Criteria
Business model		
– Description of the business model	107	GRI 102-2
– Geographical presence	108	GRI 102-3 GRI 102-4 GRI 102-6 GRI 102-7
– Objectives and strategies	113	GRI 102-14
– Main factors and trends that affect future evolution	113	GRI 102-15
Reporting framework used	107	GRI 102-54
Social and personnel issues		
– Management approach	128	
– Employment		
▪ Number and distribution of employees by country, gender, age group and employee category	129	GRI 102-8
▪ Distribution of employment contract types and the annual average by gender, age group and employee category	129	GRI 102-8
▪ Number of dismissals by gender, age group and employee category	130	GRI 401-1
▪ Average remuneration by gender, employee category and age group	130	GRI 405-2
▪ Salary gap	130	GRI 405-2
▪ Average remuneration of directors and executives	131	GRI 102-38
▪ Payments to the savings and pension schemes	137	GRI 102-38 GRI 201-3
▪ Introduction of policies on disconnecting from work	137	GRI 401-2 GRI 401-3
▪ Percentage of employees with disabilities	132	GRI 405-1
– Work organisation		
▪ Organisation of work time	137	GRI 401-2 GRI 401-3
▪ Absenteeism	140	GRI 403-2
▪ Measures to facilitate work-life balance	136	GRI 401-2 GRI 401-3
– Health and safety		
▪ Health and safety conditions in the workplace	141	GRI 403-2 GRI 403-3 GRI 403-4
▪ Indicators of work injury	140	GRI 403-2
▪ Occupational illness	140	GRI 403-2
– Social relations		
▪ Organisation of social dialogue	138	GRI 402-1 GRI 403-1 GRI 403-4
▪ Percentage of total employees covered by collective bargaining agreements	132	GRI 102-41
▪ Balance of the agreements in the field of health and safety	138	GRI 403-4
– Training		
▪ Policies introduced in the field of training	136	GRI 404-2
▪ Training indicators	132	GRI 404-1
– Universal accessibility of people with disabilities	132	GRI 405-1
– Equality	134	GRI 405-1 GRI 405-2
Environmental issues		
– Management approach	120	
– Environmental management	122	GRI 102-11 GRI 307-1

Content	Page	Reporting Criteria
– Measures to prevent pollution	122	GRI 305-1 GRI 305-2 GRI 305- 3 GRI 305-6 GRI 305-7
– Circular economy and waste prevention	121	GRI 306-2
▪ Sustainable use of resources	121	GRI 301-1
▪ Consumption of raw materials	121	GRI 302-1
▪ Direct and indirect energy consumption	121	GRI 303-1
▪ Consumption of water	121	GRI 302-4 GRI 302-5
▪ Measures to improve energy efficiency	124	GRI 302-1
– Climate change		
▪ Greenhouse gas emissions	121	GRI 305-1 GRI 305-2 GRI 305- 3
▪ Measures to adapt to climate change	125	GRI 201-2
▪ Goals to reduce greenhouse gases	125	GRI 305-5
– Biodiversity		
▪ Measures to preserve or restore biodiversity	126	GRI 304-3
▪ Impacts caused by the activity	126	GRI 304-2
Information on respect for human rights		
– Management approach	157	
– Application of due diligence procedures	166	GRI 102-16 GRI 102-17 GRI 412-2
– Prevention and management measures of possible abuses	166	GRI 102-16 GRI 102-17 GRI 412-2
– Complaints on violations of human rights	159	GRI 102-17
– Promotion and compliance with the ILO provisions	158	GRI 102-16 GRI 407-1 GRI 408-1 GRI 409-1
Information on the fight against corruption and bribery		
– Management approach	157	
– Measures to prevent corruption and bribery	161	GRI 102-16 GRI 102-17
– Anti-money laundering measures	162	GRI 102-16 GRI 102-17
– Contributions to foundations and not-for-profit associations	157	GRI 201-1 GRI 413-1
Social commitment		
– Management approach	151	
– The commitment of companies to sustainable development	151	GRI 102-43 GRI 413-1 GRI 413-2
– Responsible supply chain management	147	GRI 308-1 GRI 414-1
– Management of customers relations	114	GRI 416-1 GRI 417-1
– Tax information and transparency	163	GRI 201-1 GRI 201-4

7. Additional information

7.1. Treasury shares

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.

Movements during 2018 and 2017 involving the treasury shares of Naturgy Energy Group, S.A. are as follows:

	Number of shares	Amounts in million euro	% Share capital
At 1 January 2017	**750,545**	**13**	**0,1**
Acquisitions	7,623,586	147	0,8
Share Acquisition Plan	(336,625)	(7)	(0,1)
Disposals	(8,037,506)	(153)	(0,8)
At 31 December 2017	**-**	**-**	**-**
Acquisitions	19,421,635	427	1,9
Share Acquisition Plan	(354,422)	(7)	-
Disposals	(13,669,476)	(299)	(1,4)
At 31 December 2018	**5,397,737**	**121**	**0,5**

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 accordance with the resolutions adopted by the Naturgy Energy Group, S.A. shareholders at the General Meeting held on 20 April 2017, the resolutions relating to FY 2017 and 2018 within the Share Acquisition Plan 2017-2018-2019, aimed at Naturgy employees in Spain who decide voluntarily to take part in the Plan, was set in motion. The Plan enables participants to receive part of their remuneration in the form of shares of Naturgy Energy Group, S.A. subject to an annual limit of Euros 12,000. During 2018, 354,422 of the Company's own shares were acquired for Euros 7 million to be handed over to the employees taking part in the Plan (336,625 own shares amounting to Euros 7 million during 2017).

In 2018, the profit on transactions involving treasury shares of Naturgy Energy Group, S.A. amounted to a loss Euros 0.4 million, recognised under "Other reserves" (Euros 0.5 million profit in 2017).

Note 11 of the Notes to the Annual accounts of Naturgy Energy Group, S.A. contains all the information on treasury shares.

7.2. Average supplier payment period

Disclosure of deferrals of payment to suppliers Additional Provision 3 "Duty of disclosure" of Law 15/2010/5 July

The total amount of payments made during the year, with details of payment periods, in accordance with the maximum legal limit under Law 15/2010 of July 5, which laid down measures against late payment, is as follows:

	2018	2017
Total payments (million euro)	4,663	4,452
Total payments outstanding (million euro)	52	80
Average supplier payment period (days) [1]	17	20
Transactions paid ratio (days) [2]	17	20
Transactions pending payment ratio (days) [3]	34	23

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.

7.3. Subsequent events

Events subsequent to the end of the period are described in Note 30 of the Notes to the Naturgy Energy Group, S.A. Financial Statements.

8. Annual Corporate Governance Report

Attached as an annex and forming an integral part of this Directors' Report is the Annual Report on Corporate Governance 2018, as required by article 526 of the Capital Companies Act.

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
22/06/12	1,000,689,341	1,000,689,341	1,000,689,341

Please indicate if there are different types of shares with different rights associated:

YES ☐ NO ☒

Class	Number of shares	Face value	Number of voting rights	Different r ights

A.2 List the direct and indirect holders of significant ownership interests in your company at year-end, excluding directors[1]:

Name or company name of shareholder	% voting rights attributed to the shares		% voting rights through financial instruments		% of total voting rights
	Direct	Indirect	Direct	Indirect	
Global Infrastructure Management LLP		20.000%			20.000%
Société Nacionale pour la Recherche, la Production, le Transport, la Transformation et la Commercialisation des Hydrocarbures	3.850%				3.850%
Criteria Caixa S.A.U.	20.422%	5.23%			25.652%
CVC Capital Partners SICAV-FIS S.A.		20.072%			20.072%

Detail of the indirect holding:

Name or company name of the indirect holder	Name or company name of the direct holder	% voting rights attributed to the shares	% voting rights through financial instruments	% of total voting rights
Global Infrastructure Partners III	GIP III Canary 1, S	20.000%		20.000%
Criteria Caixa S.A.U.		20.422%		20.422%
Criteria Caixa S.A.U.	Energía Boreal S.A.	5.0%		5.0%
Criteria Caixa S.A.U.	G3T S.L	0.10%		0.10%
Criteria Caixa S.A.U.	BCN Godia S.L.U	0.13%		0.13%
CVC Capital Partners SICAV-FIS S.A.	Rioja Bidco Shareholdings, S.L.U	20,072%		20.072%

1. According to information on significant shareholdings reported to the CNMV by the reporting parties.

Indicate the most significant changes in the shareholder structure occurred during the year:

Name or company name of shareholder	Date of the transaction	Description of the transaction
Repsol, S.A.	18-05-2018	Sale of all of its holding to Rioja Bidco Shareholdings, S.à.r.l
Criteria Caixa S.A.U.	3-10-2018	It transfers 5% of the share capital to Energía Boreal 2018, S.A.

A.3 Complete the following tables regarding the members of the company's Board of Directors who hold voting rights over the company shares:

Name or company name of director	% voting rights attributed to the shares		% voting rights through financial instruments		% of total voting rights	% voting rights that can be transferred through financial instruments	
	Direct	Indirect	Direct	Indirect		Direct	Indirect
Mr Francisco Reynés Massanet		0.008			0.008		
Rioja Bidco Shareholdings	20.072				20.072		
Theatre Directorship Services	0				0		
Mr William Alan Woodburn	0				0		
Mr Pedro Sainz de Baranda Riva	0				0		
Mr Ramón Adell Ramón	0.001				0.001		
Mr Enrique Alcántara-García Irazoqui	0.003				0.003		
Mr Claudio Santiago Ponsa	0				0		
Mr Marcelino Armenter Vidal	0.001				0.001		
Mr Francisco Belil Creixell	0.001				0.001		
Ms Helena Herrero Starkie	0				0		
Mr Rajaram Rao	0				0		

% total voting rights held by the Board of Directors	20,086%

Detail of the indirect holding

Name or company name of director	Name or company name of the direct holder	% voting rights attributed to the shares	% voting rights through financial instruments	% of total voting rights	% voting rights that can be transferred through financial instruments
Mr Francisco Reynés Massanet	Frinvyco, SL	0.008			

Observations:

A.4 Indicate, where applicable, the family, commercial, contractual or corporate relations which could exist between the owners of significant stakes, provided they are known by the company, unless they are irrelevant or arise from normal trading activities, excluding those enquired about in section A.6:

Name or company name of related parties	Relationship type	Brief outline

Observations:

See section A. 7

A.5 Indicate, where applicable, the commercial, contractual or corporate relations which could exist between the holders of significant shares and the company and/or its group, unless they are irrelevant or arise from normal trading activities:

Name or company name of related parties	Relationship type	Brief outline
Criteria Caixa S.A.U.	Commercial	The existing relationships derive from ordinary commercial traffic and are referred to in section D.2 and in the annual accounts.
Repsol, S.A.	Commercial	The existing relationships derive from ordinary commercial traffic and are referred to in section D.2 and in the annual accounts.
CVC Capital Partners SICAV-FIS S.A.	Commercial	The existing relationships derive from ordinary commercial traffic and are referred to in section D.2 and in the annual accounts.
GIP III Canary 1, S.à r.l.	Commercial	The existing relationships derive from ordinary commercial traffic and are referred to in section D.2 and in the annual accounts.

A.6 Describe the relationships, unless they are scarcely relevant to the two parties, that exist between the significant shareholders or those represented on the board and the directors, or their representatives, in the case of legal entity administrators.

Explain, where appropriate, how significant shareholders are represented. Specifically, give details of those directors who have been appointed on behalf of significant shareholders, those whose appointment would have been promoted by significant shareholders, or who are linked to significant shareholders and/or entities of their group, with a specification of the nature of such relationships. In particular, mention shall be made, where appropriate, of the existence, identity and position of board members, or representatives of directors, of the listed company, who are, in turn, members of the administrative body, or their representatives, in companies that hold significant holdings in the listed company or in entities of the group of said significant shareholders.

Name or company name of related director or representative	Name or company name of significant related shareholder	Company name of the significant shareholder group	Description of the relationship/position
Mr Marcelino Armenter Vidal	Criteria Caixa S.A.U.	Criteria Caixa S.A.U.	Proprietary/Managing Director Criteria Caixa
		Caixa Capital Risc, S.G.E.I.C. S.A.	Deputy Chairman– CEO
		Inmo Criteria Caixa, S.A.U.	Director
		Mediterránea Beach & Golf S.A.U.	Chairman
		Saba Infraestructuras, S.A.	Director
		Caixa Innvierte Industria, S.C.R., S.A.	Chairman
		Caixa Capital Biomed, S.C.R. S.A.	Physical person representing the Sole Administrator of Caixa Capital Risc, S.G.E.I.C, S.A.
		Caixa Capital Fondos, S.C.R. S.A.	Physical person representing the Sole Administrator of Caixa Capital Risc, S.G.E.I.C, S.A.
		Caixa Capital Micro, S.C.R. S.A.	Physical person representing the Sole Administrator of Caixa Capital Risc, S.G.E.I.C, S.A.
		Caixa Capital Tic, S.C.R. S.A.	Physical person representing the Sole Administrator of Caixa Capital Risc, S.G.E.I.C, S.A.
		Criteria Venture Capital, S.I.C.C. S.A.	Physical person representing the Sole Administrator of Caixa Capital Risc, S.G.E.I.C, S.A.
Mr Enrique Alcántara García-Irazoqui	Criteria Caixa S.A.U.		Proprietary
Mr William Alan Woodburn	Global Infrastructure Management LLP		Proprietary
Mr Rajaram Rao	Global Infrastructure Management LLP		Proprietary/Shareholder
Mr Javier De Jaime Guijarro	CVC Capital Partners SICAV-FIS S.A.		Proprietary
Mr José Antonio Torre de Silva López de Letona	CVC Capital Partners SICAV-FIS S.A.		Proprietary/Employee

A.7 Indicate whether or not the company has been notified of parallel shareholders agreements that affect it as per Articles 530 and 531 of the Corporate Enterprises Act. Where applicable, give a brief description and list the shareholders associated with the agreement:

YES [X] NO [ ]

Parties to parallel shareholders agreements	% of share capital affected	Brief outline of agreement	Expiration date of the agreement, if there is one
Criteria Caixa, S.A.U GIP III Canary 1, S.à r.l.	45.65%	The agreement reported in Relevant Fact No. 242612 of 12/09/2016. specifies that the intervening parties assume certain undertakings concerning corporate governance of the Company and which are for the purpose of respecting the rights to proportional representation both on the Board as well as on Committees.	
Alba Europe S.à r.l. and Rioja Investment S.à r.l	20.072%	The agreement reported in Relevant Fact No. 265818 of 18 May 2018 affects 1. The proposal for designation of directors in representation of Rioja Bidco Shareholdings, 2. The adoption of decisions on the Board and at the Meeting, and 3. The system for transfer of shares.	
Criteria Caixa, S.A.U and G3T, S.L. Criteria Caixa, S.A.U and BCN Godia, S.L.U.	5.123%	The agreement reported in Relevant Fact No. 270130 of 3 October 2018 deals with regulating the exercise of the voting rights of the indirect holding of G3T and BCN Godia S.L.U (through Energía Boreal 2018, S.A.) in Naturgy, indicating that it will do what Criteria specifies.	

Indicate whether or not the company is aware of the existence of concerted actions among its shareholders. Give a brief description as applicable:

YES [ ] NO [X]

Parties to concerted action	% of share capital affected	Brief description of the concerted action	Expiry date of the concerted action, if there is one

If any modification or cancellation of said agreements or concerted actions has taken place during the year, please make express mention of this:

When Repsol sold its entire stake in the Company, it ceased to be part of the paracorporate agreement that it maintained with Criteria Caixa, S.A.U. and GIP III Canary 1, S.à.r.l.

A.8 Indicate whether any individual or legal entity currently exercise control or could exercise control over the company in accordance with article 5 of the Securities Market Act. If so, identify:

YES [ ] NO [X]

Name or company name

Observations

A.9 Complete the following tables on the company's treasury share:

At year-end:

Number of direct shares	Number of indirect shares (*)	% of total share capital
5,397,737	8,639,595	14,037,332

Observations:

Explain the significant changes over the year:

Details of significant changes
As reported in the relevant facts dated 3 August, 1 October and 6 December, Naturgy has acquired 8,639,595 shares that will be kept in a separate corporate vehicle to generate a yield that will finance the long-term incentive of certain executives if the established conditions are met -see section B.7 of the Annual Remuneration Report. On the other hand, at 31 December 2018, a further 5,397,737 shares were held for the purpose of repurchasing shares for possible redemption, providing for the acquisition of shares for up to Euros 400 million in the period ending on 30 June 2019.

A.10 Give details of the terms and conditions corresponding to the General Meeting of Shareholders' current mandate to the Board of Directors for issuing, repurchasing or assigning own shares.

The General Meeting of Shareholders held on 14 May 2015, in item 14 of the Agenda, authorised the Board of Directors to agree the acquisition of the Company shares in exchange for valuable consideration and to do so within a deadline of five years, under the following conditions:

Fourteenth.- Authorisation to the Board of Directors for the derivative acquisition of own shares, either directly or through group companies of Naturgy Energy Group S.A., in the terms agreed by the General Meeting and with the legally established restrictions, thus cancelling the authorisation agreed by the Ordinary General Meeting of 20 April 2010.

Fourteen 1.- To cancel, in the unused part, the authorisation granted to the Board of Directors by the General Meeting held on 20 April 2010 to acquire company shares by onerous title.

Fourteenth 2.- To authorise the Board of Directors to acquire in a term of no longer than five years fully paid-up company shares to a maximum of 10% of share capital by onerous title, on one or more occasions, or the maximum applicable figure in accordance with the legislation in force at the time of acquisition, provided that the aforesaid percentage between the shares acquired by the company directly or indirectly and those already held by the company and its subsidiaries should never exceed 10% of share capital or any other legally prescribed percentage of capital. The minimum and maximum acquisition price shall be the share price on the Continuous Market of the Spanish Stock Exchange, with an upward or downward variation of 5%.

If the shares are not listed, the maximum and minimum acquisition price shall be established at between one and a half times and twice the book value of the shares, as per the latest audited consolidated balance sheet. The Board of Directors is authorised to delegate this authorisation to the Executive Committee or to the person or persons it deems pertinent. This authorisation is understood to apply to the acquisition of the company's shares by owned companies.

Likewise, the General Meeting of Shareholders held on 20 April 2017, in item 14 of the Agenda, authorised the Board of Directors to agree on the increase in share capital, and to do so within a deadline of five years, under the following conditions:

Fourteenth.- Authorisation for the Board of Directors, with substitution powers on the Executive Committee, in accordance with the provisions laid down in Article 297.1 b) of the Corporate Enterprises Act, so that, within the maximum term of five (5) years, if it considers it appropriate, it can increase the share capital, to the maximum quantity corresponding to 50% of the share capital of the company, with the possibility of incomplete subscription, on the date of the authorisation, issuing shares with or without the right to vote, with or without a premium, up to half the share capital, in one or more times and on the occasions and to the amount it considers appropriate, up to the limit of 20% of the share capital at the time of this authorisation, rewriting the articles of the Articles of Association and cancelling the authorisation agreed by the Ordinary General Meeting held on 20 April 2012.

Fourteenth.

1) Taking into consideration the current share capital figure, to authorise the Board of Directors, with the power to delegate this to the Executive Committee, to increase the share capital by FIVE HUNDRED MILLION THREE HUNDRED AND FORTY FOUR THOUSAND AND SIX HUNDRED AND SEVENTY EUROS (Euros 500,344,670), within five (5) years from this date (20/4/2017), through a cash contribution, in one or more payments and as appropriate for the amount decided, duly issuing ordinary, privileged and redeemable shares, with or without the right to vote, with or without a premium, without the need for fresh authorisation from the General Meeting, as well as to amend the Articles of Association required for the share capital increase(s) carried out by virtue of the foregoing authorisation, not fully subscribed. All the foregoing is in accordance with the provisions laid down in Article 297.1.b) of the Corporate Enterprises Act, rendering null and void the authorisation agreed by the Ordinary General Meeting of 20 April 2012.

2) The Board of Directors is expressly empowered, with the power to delegate this to the Executive Committee, to fully or partially exclude the preferential subscription right with regard to all or any of the issuances agreed in accordance with the provisions of this authorisation. This power is limited to the fact that the exclusions of the pre-emptive subscription right do not exceed, as a whole, 20% of the Company's current share capital.

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

"Transitory article - delegation to the board of directors.

The company's Board of Directors, with the powers of replacing this delegation with the Executive Committee, has been authorised to increase the share capital by FIVE HUNDRED MILLION THREE HUNDRED AND FORTY FOUR THOUSAND AND SIX HUNDRED AND SEVENTY EUROS (Euros 500,344,670), within five (5) years from this date (20/04/2017), through a cash contribution, in one or more payments and as appropriate for the amount decided, duly issuing ordinary, privileged and redeemable shares, with or without the right to vote, with or without a premium, without the need for new authorisation from the General Meeting, up to the limit of 20% of the share capital at the time of this authorisation, as well as to amend the Articles of Association required for the share capital increase carried out by virtue of the foregoing authorisation, not fully subscribed. All the foregoing is in accordance with the provisions laid down in Article 297.1.b) of the Corporate Enterprises Act".

A.11 Estimated floating capital:

	%
Estimated floating capital	30.426

A.12 Indicate whether there is any restriction (statutory, legislative or of any other nature) on the transferability of securities and/or any restrictions on the voting rights. In particular, the existence of any type of restrictions that may make it difficult to take control of the company through the acquisition of its shares in the market, as well as those authorisation or prior notification systems that apply to acquisitions or transfers of financial instruments of the company through sectoral regulations, will be reported.

YES [X] NO [ ]

Description of the restrictions
As a company that incorporates certain regulated and quasi-regulated assets and activities into its Group, the acquisition of Naturgy Energy Group S.A. shares may be subject to the provisions laid down in Additional Provision 9 of Law 3/2013, of 4 June, governing the National Commission on Markets and Competition. Given its nature as a major operator in the gas and electricity markets, the holding of its shares is subject to the restrictions laid down in article 34 of Decree-Law 6/2000, governing Urgent Measures to intensify competition in the goods and services markets.

A.13 Indicate whether the General Meeting has agreed to take up measures of neutralisation against a takeover bid by virtue of the provisions laid down in Law 6/2007.

YES [ ] NO [X]

If appropriate, explain the measures approved and the terms under which the restrictions would not be enforceable:

A.14 Indicate whether the company has issued securities not traded in a regulated market of the European Union.

YES [ ] NO [X]

If appropriate, indicate the different types of shares and, for each type of share, the rights and obligations conferred.

B. General Meeting

B.1 Indicate and, where applicable, give details of whether the quorum required for constitution of the General Shareholders' Meeting differs from the system of minimum quorums established in the Corporate Enterprises Act.

YES [ ] NO [X]

	% quorum different to that laid down in Article 193 LSC for general cases	% quorum different to that laid down in Article 194 LSC for special cases
Quorum required for the first call to meeting		
Quorum required for the second call to meeting		

Description of the differences

B.2 Indicate and, as applicable, describe any differences between the company's system of adopting corporate agreements and the framework established in the Corporate Enterprises Act (LSC):

YES ☐ NO ☒

Describe how the system differs from that of the LSC.

	Reinforced majority other than that laid down by Article 201.2 LSC for the cases of 194.1 LSC	Other cases of reinforced majorities
% laid down by the institution for the adoption of agreements		

Describe the differences

B.3 Indicate the rules governing amendments to the company's Articles of Association. In particular, indicate the majorities required to amend the Articles of Association and, if applicable, the rules for protecting shareholders' rights when changing the Articles of Association.

The amendment of the Articles of Association is regulated in article 6.2 of the Articles of Association and in article 12 of the Regulations on the General Meeting, which is supplemented with the corresponding provisions of the Corporate Enterprises Act.

The shareholders constituted in a duly convened General Meeting, shall generally decide by simple majority vote on the matters which fall to the terms of reference of the meeting. In such case an agreement shall be deemed adopted when it obtains more votes in favour than against of the share capital either present or represented.

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

In order for the ordinary or extraordinary General Meeting to validly agree the issue of bonds, the increase or reduction of share capital, the removal or limitation of the preferential subscription right for new shares or convertible bonds, as well as the transformation, merger, spin-off or global assignment of assets and liabilities, the transfer of the company's registered office abroad and, in general, any modification to the Articles of Association, will require, at the first call to meeting, the attendance of shareholders, either present or represented, that hold at least fifty percent (50%) of the subscribed share capital with voting rights. In the second call to meeting, it will be sufficient for twenty-five percent (25%) of the share capital to be present.

The modification of the Articles of Association must be agreed by the General Meeting and requires the concurrence of the following requisites:

1) The Board of Directors or, where appropriate, the shareholders that make the proposal, must compile a written report with justification for the amendment.

2) The call to meeting must clearly express the proposed points of change, as well as the right all shareholders have to examine, at the registered office, the full text of the proposed modification and a report on this. They also have the right to ask for handover or free-of-charge sending of said documents.

3) The agreement must be adopted by the General Meeting in accordance with the provisions set out in these Articles of Association.

4) Under all circumstances, the agreement must be set out in a public deed, which will be registered with the Mercantile Registry and published in the Official Bulletin of the Mercantile Registry.

B.4 Indicate the attendance data of the General Meetings held during the financial year to which this report refers:

Date of General Meeting	Attendance data				
	% physical presence	% represented	% remote voting Electronic vote	Other	Total
04/05/2016	68.67%	8.77%	0	0	77.44%
Of the floating capital 2016	0.13%	8.77%	0	0	8.9%
20/04/2017	68.66%	13.34%	0%	0%	82%
Of the floating capital 2017	0.1%	13.3%	0%	0%	13.4%
27/06/2018	68.69%	15.13%	0%	0%	83.82%
Of the floating capital 2018	0.2%	15.1%	0%	0%	15.3%

B.5 Indicate whether at the General Meetings held during the year there has been any item on the agenda that, for whatever reason, has not been approved by the shareholders.

YES ☐ NO ☒

Agenda items that have not been approved	% of votes against (*)

* If the non-approval of the item is for a reason other than a vote against, this will be explained in the part of the text and "n/a" will be placed in the "% of votes against" column.

B.6 Indicate whether or not there is a statutory restriction to the minimum number of shares required to attend the General Meeting.

YES ☐ NO ☒

Number of shares required to attend the General Meeting	
Number of shares required to vote remotely	

Observations

B.7 Indicate whether it has been established that certain decisions, other than those established by Law, which involve the acquisition, disposal, the contribution to another company of essential assets or other similar corporate operations must be submitted to approval of the general meeting of shareholders.

YES ☐ NO ☒

Explanation of the decisions that must be submitted to the board other than those established by law

B.8 Indicate the URL of the company and the means of access to corporate governance content and other information concerning the general meetings and which must be made available to shareholders through the company's website.

With regard to the Corporate Governance section, the route is as follows: https://www.naturgy.com/accionistas_e_inversores/gobierno_corporativo/normas_de_gobierno

With the following itinerary www.naturgy.com → Shareholders and Investors → Corporate Governance.

With regard to the General Meeting section, the route is as follows: https://www.naturgy.com/accionistas_e_inversores/gobierno_corporativo/junta_general_de_accionistas, with the following itinerary www.naturgy.com → Shareholders and Investors → General Meeting.

C. Structure of the Company's Management

C.1 Board of Directors

C.1.1 Maximum and minimum number of directors stipulated the Articles of Association and the number set by the General Meeting:

Maximum number of directors	15
Minimum number of directors	11
Number of directors set by the General Meeting	12

Observations:

C.1.2 Complete the following table with Board members' details.

Name or company name of director	Representative	Type of director	Position on the board	Date of first appointment	Date of last appointment	Election procedure	Date of birth
Mr Francisco Reynés Massanet		Executive	Chairman	06/02/2018	27/06/2018	Agreement General Meeting of Shareholders	08-04-1963
Mr Ramón Adell Ramón		Independent	Coordinating director	18/06/2010	27/06/2018	Agreement General Meeting of Shareholders	09-01-1958
Mr Enrique Alcántara-García Irazoqui		Proprietary	Director	27/06/1991	20/04/2017	Agreement General Meeting of Shareholders	21-10-1944
Mr Marcelino Armenter Vidal		Proprietary	Director	21/09/2016	20/04/2017	Agreement General Meeting of Shareholders	02-06-1957
Mr Francisco Belil Creixell		Independent	Director	14/05/2015	27/06/2018	Agreement General Meeting of Shareholders	24-05-1946
Ms Helena Herrero Starkie		Independent	Director	04/05/2016	04/05/2016	Agreement General Meeting of Shareholders	13-06-1959
Mr Rajaram Rao		Proprietary	Director	21/09/2016	20/04/2017	Agreement General Meeting of Shareholders	03-04-1971
Rioja Bidco Shareholdings, S.L.U.	Mr Javier de Jaime Guijarro	Proprietary	Director	17/05/2018	27/06/2018	Agreement General Meeting of Shareholders	-----
Mr Claudi Santiago Ponsa		Independent	Director	27/06/ 2018	27/06/2018	Agreement General Meeting of Shareholders	20-09-1956
Mr Pedro Sainz De Baranda		Independent	Director	27/06/ 2018	27/06/2018 (aceptado 6-07-2018)	Agreement General Meeting of Shareholders	23-03-1963
Mr William Alan Woodburn		Proprietary	Director	30/09/2016	20/04/2017	Agreement General Meeting of Shareholders	14-01-1951
Theatre Directorship Services Beta, S.À.R.L.	Mr José Antonio Torre de Silva López de Letona	Proprietary	Director	18/05/2018	27/06/2018	Agreement General Meeting of Shareholders	----

Total number of directors	**12**

Indicate the removals from office due to resignation, dismissal or for any other reason, that have occurred on the Board of Directors during the reporting period:

Name or company name of director	Category of director at time of vacancy	Date of last appointment	Date of vacancy	Specialist committees of which he or she was a member	Indicate whether the removal from office occurred before the end of the mandate
Isidro Fainé Casas	Proprietary	18/05/2015	6/02/2018	EXC	Yes
Rafael Villaseca Marco	Executive	14/05/2015	6/02/2018	EXC	Yes
Josu Jon Imaz Sanmiguel	Proprietary	20/4/2017	22/02/2018	EXC	Yes
Luis Suarez de Lezo Mantilla	Proprietary	20/4/2017	17/05/2018	EXC, AUC	Yes
Miguel Martinez Sanmartín	Proprietary	14/05/2015	6/3/2018	EXC, ARC	Yes
Iñigo Alonso de Noriega Satrústegui	Proprietary	6/3/2018	17/05/2018	ARC	
Guillermo Llopis García	Proprietary	6/3/2018	18/05/2018	AUC	Yes
Cristina Garmendia Mendizábal	Independent	14/05/2015	27/06/2018	ARC, AUC	Yes
Benita Ferrero-Waldner	Independent	14/05/2015	27/06/2018	EXC	No
Xavier Añoveros Trias de Bes	Independent	14/05/2015	27/06/2018	AUC	No
Alejandro García- Bragado Dalmau	Proprietary	21/09/2016	21/05/2018	EXC, ARC	No
Mario Armero	Proprietary	20/04/2017	27/06/2018	--	Yes
Theatre Directorship Services Delta, S.À.R.L. (Represented by Mr Juan Arbide Estensoro)	Proprietary	17/05/2018	27/06/2018	--	Yes
					No

Reason for the resignation and other observations
The exit of Repsol's share capital and the simplification and reduction of the size of the Board and its Committees has led to a reduction in the number of proprietary directors, which is why several of them tendered their resignation. The Proprietary Director Mr García-Bragado resigned, alleging differences of opinion in the selection of new directors, which were not shared by the other members of the board. With regard to the independent directors, the reason for their removal from office was the expiration of their mandates.

C.1.3 Complete the following tables on board members and their respective categories:

Executive directors

Name or company name of director	Position in the company's management structure	Profile
Mr Francisco Reynés Massanet	Executive Chairman	Engineering and international business profile: Industrial Engineer, specialising in mechanics, with a degree from the Polytechnic University of Barcelona, and an MBA from IESE; he has also completed Senior Management programmes in the United States and Germany.

Total number of executive directors	1
% of the entire board	8.33%

Observations

External proprietary directors

Name or company name of director	Name or title of significant shareholder represented by the director or that has proposed the director's appointment	Profile
Mr Enrique Alcántara-García Irazoqui	Criteria Caixa S.A.U.	Legal profile: Former Public prosecutor. He is Secretary of the Board of Directors and of the Trusts of multiple Societies and Foundations.
Mr Marcelino Armenter Vidal	Criteria Caixa S.A.U.	Economics and business profile: Degree in Business Administration and Management and a Master's degree in Business Administration and Management from ESADE.
Mr Rajaram Rao	Global Infrastructure Partners III	IT, economics and international business profile: Qualified Electronic and Telecommunications Engineer. He also holds an MBA from the University of Delhi and a Master's degree in Finance from the London Business School.
Mr William Alan Woodburn	Global Infrastructure Partners III	International technical engineer profile: MS and BS degrees in Engineering from Northwestern University and the US Merchant Marine Academy.
Rioja Bidco Shareholdings, S.L.U. (Mr Javier de Jaime Guijarro)	CVC Capital Partners SICAV-FIS S.A.	
Theatre Directorship Services Beta, S.à.r.l. (Mr José Antonio Torre de Silva López de Letona)	CVC Capital Partners SICAV-FIS S.A.	Economics and Business profile. Degree in industrial Engineering from the Higher Technical School of the Comillas Pontifical University (ICAI) and an MBA from the University of Navarre (IESE).

Total number of proprietary directors	6
% of the entire Board	50.00%

Observations

External independent directors

Name or company name of Director	Profile
Mr Ramón Adell Ramón	Expert financial and accounting profile: Doctorate in Economics and Business Administration. Graduate in Law. Professor of Financial Economics and Accounting at the University of Barcelona. An academic from the Royal Academy of Economic and Financial Sciences of Spain and Honorary Member of the European Doctorate Degree Holders and Dr H.C. (Consedoc).
Mr Claudi Santiago Ponsa	IT and international business profile; energy sector: Degree in Computer Engineering from the Autonomous University of Barcelona (UAB) and International executive programme (INSEAD) through the Executive International Business at Georgetown University.
Mr Francisco Belil Creixell	Engineering and international business profile: Senior Engineer. He has been CEO of the Southwest Europe region at Siemens and Chairman of the German Chamber of Commerce for Spain and the Federation of the Spanish Chemical Industry.
Mr Pedro Sainz de Baranda Riva	Engineering and international business profile; capitals market: Mining Engineer from the University of Oviedo, PhD in Engineering, Rutgers University of New Jersey and an MBA from the Sloan School of Management of Massachusetts, Institute of Technology (MIT).
Ms Helena Herrero Starkie	IT and R&D&i and international business profile: Degree in Chemical Sciences. She is the Chairperson and CEO of Hewlett Packard (HP) for Spain and Portugal.

Total number of independent directors	5
% total of the board	41.66%

Observations

Indicate whether or not any director qualified as independent receives from the company, or from its group, any amount or benefit for an item other than remuneration as director, or holds or has held, over the last year, a business relationship with the company or any other group company, whether in their own name or as a significant shareholder, Director or senior executive of an entity that maintains or has maintained any such relationship.

Where appropriate, include a reasoned statement from the board on the grounds why it believes this director may perform his duties as an independent director.

Name or company name of director	Description of the relationship	Reasoned statement
Ms Cristina Garmendia Mendizábal	Director of Science & Innovation Link, Office (SILO), an entity that has rendered services to a company of the Naturgy Group.	The business relationship maintained with Science & Innovation Link Office is not significant given its intangible amount.

Other external directors

Identify all other external directors and explain why these cannot be considered proprietary or independent directors and detail their relationships with the company, its executives or shareholders:

Name or company name of director	Reasons	Company, executive or shareholder with whom the relationship is maintained	Profile
Ms Cristina Garmendia Mendizábal	She was considered external from 17-05-18 to 27-06-18.	Indirect link with the significant shareholder CVC Capital Partners SICAV-FIS S.A., being a Director of Corporación Financiera Alba, a company that has concluded a paracorporate agreement with CVC	Business management and innovation

Total number of other external directors	
% total of the board	

Observations

List any changes in the category of each director which have occurred during the year.

Name or company name of director	Date of change	Former category	Current category
Ms Cristina Garmendia Mendizábal	17-05-2018	Independent	Other external director until 27/06/18

Observations

C.1.4 Complete the following table with information regarding the number of female directors at the close of the last four financial years, and their category:

	Number of female directors				% of total directors of each type			
	Financial year t	Financial year t-1	Financial year t-2	Financial year t-3	Financial year t	Financial year t-1	Financial year	Ejercicio t-3
Executive	0	0	0	0	0	0	0	0
Proprietary	0	0	0	0	0	0	0	0
Independent	1	3	3	2	8.33%	17.65%	17.65 %	11.76%
Other external	0	0	0	0	0	0	0	0
Total:	1	3	2	2	8.33%	17.65%	17.65%	11.76%

Observations
In the preceding table, the number of female directors at the end of each year has been recorded.

C.1.5 Indicate whether the company has diversity policies in relation to the Board of Directors of the company with regard to issues such as age, gender, disability, or professional training and experience. Small and medium-sized enterprises, in accordance with the definition contained in the Accounts Auditing Law, will at least have to report the policy they have established in relation to gender diversity.

YES [ ] NO [ ] Partial policies [X]

If yes, describe these diversity policies, their objectives, the measures and the way in which they have been applied and their results over the year. Also indicate the specific measures adopted by the Board of Directors and the Appointments and Remuneration Committee to achieve a balanced and diverse presence of directors.

If the company does not apply a diversity policy, explain the reasons why

Description of the policies, objectives, measures and manner in which they have been applied, as well as the results obtained
Naturgy's director selection policy includes guidelines aimed at selecting candidates whose appointment fosters professional, expertise and gender diversity on the Board of Directors. In any case, it should be noted that said policy is applied with full respect to the right of proportional representation legally recognized to shareholders The Appointments and Remuneration Committee ensures that the screening procedures do not include any implicit bias that could involve any discrimination whatsoever. Throughout 2018 there has been a significant renewal process of the Board of Directors, which has affected both proprietary directors and independent directors. With respect to proprietary directors, the process of renewal of directors has been linked to two circumstances: 1. Changes in the shareholding structure of the Company, which have caused the exit of the proprietary directors representing Repsol and the entry of the directors representing CVC. 2. The reduction in the number of board members, which has led to a reduction in the number of proprietary directors representing each shareholder, from three to two. Within the framework of this process of renewal of proprietary directors, the Company has first all been respectful of the right to proportional representation that lawfully corresponds to shareholders. The detail of the assessment made by the Appointments and Remuneration Committee of the different candidates proposed by the shareholders is included in the corresponding report of the Committee that was published with the call to Meeting. With regard to independent directors, the expiration of the term of a significant number of them, as well as the decision to reduce the number of directors, led to the appointment of four independent directors to the General Meeting of Shareholders, until there were a total of five directors in accordance with the new configuration of the board. At the time of formulating the proposal for appointing independent directors, the Appointments and Remuneration Committee was well aware of the conclusions of the self-assessment process of the board's performance in 2017, which was carried out with the assistance of an outsourced consultant. This self-assessment process helped the board, assisted by said consultant, to identify those profiles that were deemed necessary to strengthen with regard to the appointment of independent directors. In particular, the need to take into account in the appointment and renewal processes of independent directors the following profiles: industrial, regulatory in the matter of energy and technology, as well as, in general, more international profiles. It was considered desirable for the new candidates to have knowledge of the energy sector acquired outside of Naturgy and also have specialized profiles in the capital market. The proposal for the appointment of directors that the board submitted to the General Meeting of Shareholders was consistent with that analysis. The detail of the relevant professional elements of the proposed directors was given in the corresponding report of the Appointments and Remuneration Committee that was published together with the other documentation of the Meeting.

C.1.6 Explain the measures which, where appropriate, have been agreed by the Appointments Committee so that the selection procedures are unaffected by any implicit bias that hampers the selection of female directors, and which show that the company purposefully seeks and includes women that satisfy the professional profile sought among the potential candidates:

Explanation of the measures
The Appointments and Remuneration Committee is tasked with reviewing the necessary skills of candidates required for each vacancy, compliance with the requirements needed for each category of director and the incorporation process of new members, forwarding the opportune reports or proposals to the Board as necessary. For covering new vacancies, selection processes shall be guaranteed that are not subject to implicit bias that prevents the selection of female directors, with special value place on, under the same conditions and among potential candidates, women who meet the professional profile being sought.

When, despite the measures adopted, the number of female directors is zero or few, explain the reasons for this:

Explanation of the reasons
The Company's Appointments and Remuneration Committee fully respects the legally recognised right to proportional representation of its significant shareholders.

C.1.7 Explain the Appointments Committee's conclusions on the checks carried out to ensure that the director selection policy is being complied with. Particularly whether the policy pursues the goal of having at least 30% of total board places occupied by female directors before the year 2020.

The Appointments and Remuneration Committee has verified that the Policy for the Selection of Directors has been complied with as regards the provision of existing vacancies on the board, all within the framework of the Company's shareholding structure, which imposes respect of certain legal requirements of proportional representation of the shareholders. The recommendations of good corporate governance must conform to this condition. The Committee has verified that in the selection processes for directors, the balance of criteria such as: i) expertise, ii) skills, iii) diversity and iv) experience has been taken into account.

The percentage of female profiles among independent directors represents 20% of the total, although it is lower than in previous years, it is expected to increase again when it is appropriate to make new proposals.

C.1.8 Where applicable, explain why proprietary directors have been appointed at the request of shareholders whose shareholding in the capital is less than 3%:

Name or company name of shareholder	Explanation

Indicate whether or not formal requests have been accepted for presence on the board from shareholders whose holding is equal to or higher than that of others for whom proprietary directors have been appointed. If so, explain why these requests have not been answered:

YES ☐ NO ☒

Name or company name of shareholder	Explanation

C.1.9 Indicate, in the event that they exist, the powers and faculties delegated by the Board of Directors to directors or to board committees:

Name or company name of the director or committee	Brief outline
Mr Francisco Reynés Massanet	He has delegated extensive powers of representation and administration in accordance with the nature and requirements of the position of Executive Chairman.

C.1.10 List the Directors, if any, who hold office as directors or representatives of directors in other companies belonging to the listed company's group:

Name or company name of director	Company name of group entity	Position	Do they have executive duties?

Observations:

C.1.11 Identify, where applicable, the directors or representatives of legal persons of your company, who are members of the Board of Directors or director representatives, legal persons of other companies listed on official stock exchanges in Spain other than those of your group, that have been reported to the company:

Name or company name of director	Corporate name of the listed company	Position
Mr Ramón Adell Ramón	Oryzon Genomics, S.A.	Independent Director/Audit Committee's Chairman
Mr Marcelino Armenter Vidal	Grupo Financiero Inbursa	Representative of the director Criteria Caixa S.A.U.
Mr William Alan Woodburn	Hess Midstream Partners	Director
Mr Pedro Sainz de Baranda Riva	Zardoya Otis S.A.	Physical representative of the Director
Mr Pedro Sainz de Baranda Riva	Gestamp Automoción, S.A.	Director
Mr José Antonio Torre de Silva López de Letona	Cortefiel, S.A.	Representative of the Director Theatre Directorship Service Beta, S.À.R.L.

C.1.12 Indicate and, where appropriate, explain whether the company has established rules about the maximum number of company boards on which its directors may sit, identifying how this is regulated where appropriate:

YES ☐ NO ☒

Explanation of the rules and identification of the document where it is regulated

C.1.13 Indicate the amounts of the following items relating to the overall remuneration of the board of directors:

Overall remuneration earned by the Board of Directors during the year (thousands of euros)	22,724
Cumulative amount of rights of current directors in pension scheme (thousands of euros)	360
Cumulative amount of rights of former directors in pension scheme (thousands of euros)	3,680

Observations

C.1.14 Identify members of senior management who are not also executive directors, and indicate the total remuneration they earned during the year:

Name or company name	Position/s
Mr Carlos Javier Álvarez Fernández	Chief Financial Officer
Mr Antonio Gallart Gabás	Director of Business Infrastructures Latin America South Zone
Mr José García Sanleandro	Director of Business Infrastructures Latin America North Zone
Mr Antonio Basolas Tena	Manager Corporate Strategy & Development
Mr José María Egea Krauel	Pipe Project Manager
Mr Manuel Fernández Álvarez	Business Director Gas & Electricity
Mr Manuel García Cobaleda	General and Board Secretary
Mr Jordi García Tabernero	Communication & Institutional Relations Managing Director
Mr Daniel López Jordà	Director of the Digitalization Project
Mr Antoni Peris Mingot	Corporate Resources Manager
Ms Rosa María Sanz García	España & Empl – Medgaz Infrastructure Business Managing Director
Mr Sergio Aranda Moreno	Colombia Project Manager
Mr Miguel Angel Aller Blanco	Lean Project Manager
Mr Steven Fernández Fernández	Capitals Market Director
Mr Jon Ganuza Fernandez de Arroyabe	Controlling
Mr Carlos Ayuso Salinas	Director of Internal Audit

Total remuneration of senior management (in thousands of euros)	17,940

Observations
Mr Daniel López Jordà and Mr Sergi Aranda Moreno stopped working for the company in December 2018. Mr Steven Fernández Fernández joined the company in June 2018.

C.1.15 Indicate whether or not there has been any modification to the regulations of the board during the year:

YES [X] NO [ ]

Description of modifications
At the meeting of 21 May 2018, the Board Regulations were substantially modified in order to simplify their content. After the Shareholders' Meeting was held, on 27 June 2018 the Regulations were amended once again as regards the number of members of the Appointments and Remuneration Committee to comply with recommendation 47 of the CNMV Good Governance Code.

C.1.16 Indicate the procedures for appointing, re-electing, evaluating and removing directors. Provide details of the competent bodies, the procedures to be followed and the criteria applicable in each procedure.

The procedures for the appointment, re-election, evaluation and removal of directors are regulated in article 7 of the Articles of Association and in articles 9 and 10 of the Regulations for the Organisation and Functioning of the Board of Directors and its Committees, supplemented by the provisions of Article 529 decies of the Corporate Enterprises Act.

1. Appointment:

The General Meeting is competent for appointing directors and establishing the number thereof, subject to the limits stipulated in Article 7 of the Articles of Association.

If vacancies were to arise during the term for which the directors were appointed, the board shall be entitled to designate, using the co-option system, the persons to occupy these vacancies until the first General Meeting of Shareholders is held.

The status of shareholder is not required to be appointed director.

Anyone who is in any of the situations that, pursuant to prevailing legislation, prevents such characterisation, cannot be proposed, appointed or qualified as independent directors.

It will be necessary to appoint persons who not only satisfy legal provisions and those laid down in the Articles of Association for the position, but who have a prestigious position and are equipped with the professional skills and expertise required to perform their duties.

Directors are appointed and re-elected in accordance with a formal and transparent procedure, following a previous report/ proposal from the Appointments and Remuneration Committee.

In particular, the proposals for the appointment of directors which the Board of Directors submits to the General Shareholders' Meeting, as well as appointments adopted by the Board by virtue of its powers of co-option, must be made subject to a proposal from the Appointments and Remuneration Committee in the case of independent directors, or a report for the remaining directors. When the Board does not follow the recommendations of said committee, it will have to explain the reasons and record the said reasons in the minutes.

2. Re-election:

Directors elected as of 27 June 2018, will hold office for a maximum term of four years, and may be re-elected (those elected up to that date have a term of three years). The directors appointed by co-option will exercise their position under the terms established in prevailing legislation.

The Appointments and Remuneration Committee is also entrusted with evaluating the quality of the work and the dedication of the directors proposed during the preceding mandate. It will make suggestions regarding independent directors and report on the remaining directors, on a compulsory basis, on the proposals for the re-election of directors which the Board of Directors chooses to submit to the General Meeting.

The independent directors shall not remain in their post for a period of more than 12 years.

3. Replacement or removal:

Directors shall be replaced in their position for the length of the term for which they were appointed, unless they are re-elected, and when so determined by the General Meeting by virtue of the powers granted thereto. Likewise, directors shall be replaced in all other circumstances where applicable pursuant to the Law, the Articles of Association and Regulations of the Board of Directors.

Directors shall be compelled to tender their resignation to the Board of Directors and proceed with the pertinent resignation, if the latter deemed it appropriate, in the following cases:

a) When executive directors step down from their executive positions.

b) When they are subject to any of the conditions of professional prohibition or incompatibility pursuant to applicable laws, the Articles of Association or these regulations.

c) When they commit a serious breach of their obligations as directors, jeopardising the interests of the Company.

d) When the reason why they were appointed as independent, executive or proprietary directors is no longer applicable.

In any case, the Board of Directors pays special attention to issues of diversity and not only gender diversity, within the framework of full respect for the right of shareholders as recognised by the Law on Proportional Representation. As explained in previous sections, and in accordance with the analysis carried out within the framework of the self-assessment process with an outsourced consultant, profiles have been identified whose reinforcement was considered relevant in order to strengthen the diversity of the Board. This has meant that current members of the Board of Directors respond to professional profiles and different career paths that complement each other: it is made up of directors who respond to financial, industrial, business management, and legal profiles related to the world of innovation and new technologies, or finally with experience in the capital market and accounting. During 2018, the Board made a special effort to increase the international profile of its members. The Board of Directors considers this circumstance particularly relevant because it helps to promote a more complete and integrating vision when analysing the different issues submitted to the board.

C.1.17 Explain, if applicable, to what extent this annual evaluation has prompted significant changes in its internal organisation and the procedures applicable to its activities:

Description of modifications
LThe evaluation of the Board of Directors for 2017 included the participation of an independent expert as consultant. Notwithstanding the fact that the outsourced consultant reported the highly satisfactory functioning of the Board and its Committees, the Board verified the possibility of progressing in certain areas of improvement to simplify its operation, which led to an Action Plan on the subject of corporate governance that was agreed on 6 March 2018, with measures aimed at this simplification and which have been implemented throughout 2018. The framework of this process must include the modification proposed by the Board to the General Meeting of Shareholders with regard to the Company's new Articles of Association, a reduction of the number of directors, the removal of the Executive Committee, the attribution to the Appointments and Remuneration Committee of new powers in matters of corporate governance. In addition, as explained in the previous sections, the 2017 annual evaluation report of the Board allowed us to identify the professional profiles whose incorporation was important to achieve in order to advance in the diversity of its composition. In particular, the need to take into account the following profiles in the appointment and renewal processes of independent directors: industrial, regulatory in the matter of energy and technology, as well as, in general, more international profiles, and also specialized profiles in the capital market.. This analysis was taken into account in relation to the proposals for the appointment of independent directors submitted to the General Meeting of Shareholders in 2018.

Describe the evaluation process and the areas evaluated by the Board of Directors, assisted by an outsourced consultant, regarding the operation and composition of its committees, and any other area or aspect that has been subject to evaluation.

Description of the evaluation process and areas evaluated
The Board was advised by an external consultant for the self-assessment of its operation during 2017, which allowed it to have a base with which to address the process of simplification and the broad renewal of the Board in June 2018. For this reason, the Board has not resorted to such external consultation in 2018, on the understanding that it is appropriate to let a certain period of time pass in order to adequately analyse the effectiveness of the agreed measures, since they have been implemented throughout 2018

C.1.18 Explain, for any of the years in which the evaluation has been assisted by an external advisor, the business relationship the adviser or any group company maintains with the company or any group company.

NOT APPLICABLE [X]

C.1.19 Indicate the cases in which directors must resign.

Directors shall be replaced in their position for the length of the term for which they were appointed, unless they are re-elected, and when so determined by the General Meeting by virtue of the powers granted thereto. Likewise, Directors shall be replaced in all other circumstances where applicable pursuant to the Law, the Articles of Association and Regulations of the Board of Directors.

Directors shall be compelled to tender their resignation to the Board of Directors and proceed with the pertinent resignation, if the latter deemed it appropriate, in the following cases:

a) When executive directors step down from their executive positions.

b) When they are subject to any of the conditions of professional prohibition or incompatibility pursuant to applicable laws, the Articles of Association or these regulations.

c) When they commit a serious breach of their obligations as directors, jeopardising the interests of the Company.

d) When the reason why they were appointed as independent, executive or proprietary directors is no longer applicable.

C.1.20 Are qualified majorities other than those prescribed by law required for any type of decision?

YES [X] NO [ ]

Where appropriate, describe the differences.

Description of the differences

Article 7.4 of the Regulations of the Board of Directors states the following:

"4.- The resolutions must be adopted with the vote of the absolute majority of the directors who attend, whether present or represented, unless the Law, the Articles of Association or these Regulations establish an enhanced majority.

In particular, the favourable vote of more than two thirds of the directors, whether present or represented, will be required for the valid adoption of resolutions on the following matters reserved for the plenary session of the Board and, therefore, non-delegable:

a) The acquisition or disposal of assets belonging to the Company (regardless of the legal means used for this purpose and, in particular, even if they are carried out through merger, spin-off or other operations of subsidiaries) in excess of Euros 500,000,000, unless its approval corresponds to the General Meeting or is carried out in execution of the budget or 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 dividend distribution policy and the approval of a new one.

d) The subscription, modification, renewal, non-renewal or termination by the Company of financing or refinancing agreements for an amount exceeding Euros 500,000,000.

e) The subscription, modification, renewal, non-renewal or termination by the Company of any material contract, other than those provided for in section d) above, whose amount exceeds Euros 500,000,000 in the case of gas supply contracts and of Euros 200,000,000 in the case of other contracts.

f) The material changes in the accounting and tax criteria and policies of the Company, unless they are due to modifications of applicable legislation or compliance with the guidelines and criteria set by the competent authorities in the matter.

g) The reformulation of the Company’s annual accounts, unless such reformulation is due to a modification of applicable legislation or compliance with the guidelines and criteria set by the competent authorities in the matter.

h) Capital investments (capex) not provided for in the Company’s annual budget for an amount exceeding Euros 200,000,000.

i) The modification of the matters of paragraphs a) to i) or modification of the enhanced majority of the vote required for any of them.”

C.1.21 Indicate if there are specific requirements other than those relating to directors in order to be appointed as Chairman of the Board of Directors.

YES ☐ NO ☒

Description of requirements

C.1.22 Indicate whether the Articles of Association or the Board Regulations establish any age limit for directors:

YES ☐ NO ☒

	Age limit
Chairman	
Chief Executive Officer	
Director	

Observations:

C.1.23 Indicate whether the Articles of Association or the Board regulations set a limited term, or other requirements stricter than those legally determined, of office for independent directors different to the one established in the regulations:

YES ☐ NO ☒

Additional requirements and/or maximum number of years of in office

C.1.24 Indicate whether the Articles of Association or Board Regulations stipulate specific rules on appointing a proxy to the board, the procedures thereof and, in particular, the maximum number of proxy appointments a director may hold. Also indicate whether there are any restrictions as to what categories may be appointed as a proxy other than those stipulated by law. Where appropriate, give a brief description of these rules.

As established in Article 7.5 of the Articles of Association “Directors who cannot attend may delegate their representation to another director, with or without instructions to vote, and must notify the Chairman or the Secretary.”

In addition, Article 7.3 of the Regulations of the Board states: “Each director shall be entitled to confer his/her representation to another director, there being no limit on the number of representations held by each member for attending the Board meeting. Absent directors' representations can be conferred by means of any written document, or any electronic means, addressed to the Chairman’s Office or the Board Secretary before the beginning of the session”.

C.1.25 Indicate the number of board meetings held during the year. Also indicate, where applicable, how many times the board has met without the chairman being present. When calculating the number, representations made with specific instructions shall be considered as attendance.

Number of board meetings	12
Number of board meetings without the chairman attending	0

Observations
Additionally, there have been two meetings held in writing and without a meeting, up to a total of 14 meetings.

Indicate the number of meetings held by the Coordinating Director with the rest of the directors, without the attendance or representation of any executive director.

Number of meetings	0

Observations
Since the Coordinating Director is also the Chairman of the Appointments and Remuneration Committee and had held this position on the Audit Committee, of which he is still a member, he has usually had contacts with the non-executive directors and especially with the independent directors, both as regards remuneration issues as well as corporate governance in general, which have made it unnecessary to convene formal meetings.

Indicate the number of meetings held by the different board committees over the year:

Number of meetings of the Executive Committee	2
Number of meetings of the Audit Committee	7
Number of meetings of the Appointments and Remuneration Committee	10
Number of meetings of the Appointments Committee	
Number of meetings of the Remuneration Committee	
Number of meetings of the _____ Committee	

Observations

C.1.26 Indicate the number of board meetings held during the year with all members in attendance:

Number of meetings attended in person by at least 80% of the directors	12
% of attendance over the total number of votes during the year	93%
Number of meetings with attendance in person, or representations made with specific instructions of all the directors	3
% votes cast with attendance in person and representations made with specific instructions, on total votes during the year	More than 90%

Observations

C.1.27 Indicate whether the consolidated and individual annual accounts submitted for authorisation for issue by the board are certified previously.

YES [X] NO [ ]

Identify, where applicable, the person(s) who has/have certified the company's individual and consolidated annual accounts in order to be drawn up by the board:

Name	Position
Mr Carlos Javier Álvarez Fernández	Chief Financial Officer

C.1.28 Explain the mechanisms, if any, established by the Board of Directors to prevent the individual and consolidated annual accounts it prepares from being laid before the General Meeting with a qualified audit report.

By virtue of those established in article 529.4 of the Corporate Enterprises Act and in the Articles of Association, the Audit Committee is responsible for, among others, the functions of informing the General Meeting of Shareholders about the issues that arise in relation to those matters that fall within the remit of the Committee and, in particular, on the result of the audit, explaining how this has contributed to the integrity of the financial reporting and the role that the committee has played in that process, as well as supervising the process of preparation and presentation of mandatory financial reporting and submitting recommendations or proposals to the administrative body, aimed at safeguarding its integrity.

To this end, the Audit Committee has supervised the process of preparing financial information and has engaged in fluid dialogue with the external auditor, with the utmost respect for its independence, where it has been informed of the Audit Plan, of the preliminary and final results of the auditor's analyses, and where its independence has been specifically ensured. In any case, it is noteworthy that no accounting qualifications have been made.

C.1.29 Is the secretary of the board also a director?

YES ☐ NO ☒

Complete if the secretary is not also a director:

Name or corporate name of the secretary	Representative
Mr Manuel García Cobaleda	-

Observations

C.1.30 Indicate the specific mechanisms introduced by the company to preserve the independence of the external auditors, as well as, if any, mechanisms to preserve the independence of financial analysts, investment banks and rating agencies, including how the legal provisions have been implemented in practice.

Among the legal functions that correspond to the Audit Committee are to establish the appropriate relations with the external auditor to receive information on those issues that may pose a threat to its independence, for examination by the committee, and any others related to the process for conducting the accounts audit and, where appropriate, the authorisation of services other than those prohibited, under the terms set out in articles 5, paragraph 4, and 6.2.b) of Regulation (EU) No. 537/2014, of 16 April, and as set out in section 3 of chapter IV of title I of Law 22/2015, of 20 July, on Accounts Auditing, on the independence regime, as well as those other communications provided for in the audit legislation of accounts and in the auditing standards. In all cases, on an annual basis, the Audit Committee shall receive from the auditors written confirmation of their independence vis-à-vis the company or entities related to it directly or indirectly, in addition to detailed and individual information on additional services of any kind rendered to these entities by the aforementioned auditors or persons or entities related to them in conformity with the provisions of auditing legislation.

Issuing annually, prior to the issuance of the audit report, a report expressing an opinion on whether the independence of the auditors or audit companies is compromised. This report shall in all cases include a reason assessment of each of the additional services provided, as referred to in the previous section, considered separately and in their totality, that consists of services other than statutory audits and how they relate to the requirement of independence or to the regulatory legislation of the activity on auditing of accounts.

Likewise, the Board of Directors has entrusted the Audit Committee with, inter alia, the following functions: to ensure that the remuneration of the external auditor for its work does not compromise its quality or independence and ensure that the company and the external auditor respect the standards in force on the provision of services other than auditing, the limits on the concentration of the auditor's business and, in general, the other rules governing the independence of auditors.

The company's relations with financial analysts and investment banks are based on the principles of transparency, simultaneity and non-discrimination, as well as the existence of specific and different agents for each collective. In order to increase transparency, this area has been enhanced by differentiating it from the Financial Department.

AIn addition, the company shall take special care not to compromise or interfere with the independence of the financial analysts in respect of the services offered by investment banks, in accordance with the internal codes of conduct established by them and designed to separate their analysis and assessment services.

C.1.31 Indicate whether the company has changed its external audit firm during the year. If appropriate, identify the incoming and outgoing auditors:

YES [X] NO [ ]

Outgoing auditor	Incoming auditor
PWC	E&Y

Observations

In the case of disagreements with the outgoing auditor, explain the content of the said disagreements:

YES [ ] NO [X]

Explanation of the disagreements

C.1.32 Indicate if the audit company performs other tasks for the company and/or its group other than auditing activities, and if so, state the amount of the fees received for said activities and the percentage of the fees billed to the company and/or its group:

YES [X] NO [ ]

	Company	Group	Total
Amount of tasks other than auditing activities (in thousands of euros)	181	540	721
Amount of tasks other than auditing/ Amount billed by the audit company (%)	20.00%	12.60%	13.90%

Observations

C.1.33 Indicate if the auditor's report on the annual accounts corresponding to the previous year involves reservations or exceptions. Where applicable, indicate the reasons given by the Chairman of the Audit Committee to explain the content and scope of the said reservations or exceptions.

YES [X] NO [X]

Explanation of the reasons

C.1.34 Indicate the number of consecutive years during which the current audit firm has been auditing the annual accounts of the company. Also indicate the percentage of the number of years audited by the current audit company over the total number of years that the annual accounts have been audited:

	Individual	Consolidated
Number of years without interruption	1	1

	Individual	Consolidated
Number of years audited by the current audit company / Number of years the company has been audited (in %)	3.57%	3.57%

Observations

C.1.35 Indicate, and give details if any, whether there are procedures for directors to receive the information they need in sufficient time to prepare for meetings of the governing bodies:

YES [X] NO [ ]

Details of the procedure

Articles 6.2 and 6.3 of the Regulations of the Board of Directors state: "2-Notices convening sessions shall be issued by the Chairman or the Secretary, or by the Deputy Chairman on order of the Chairman, and may be effected by any of the channels set out in the Articles of Association. The notification shall include the place and the agenda of said meeting and shall be issued, at least 5 days before the meeting is to be held, specifying the agenda of the meeting. In the event of an emergency duly justified by the Chairman and thus appreciated by the Board at the start of the meeting, a call to meeting will be made by telephone, fax, email or any other telematic means, with sufficient notice to allow the directors to participate in the meeting. Prior to each meeting, the directors shall be furnished with the information and documentation considered to be pertinent or relevant regarding the subjects to be addressed in the board meeting. Directors shall also be furnished with the minutes of the previous meeting, regardless of whether said minutes have been approved or not. The Chairman shall be authorised to establish the order of the day, except in the event of the compulsory convening, in which case the agenda of the convened meeting will include the issues indicated by the Directors who request it. 3.- The board meeting shall have a quorum, without being previously convoked, if all the directors are present or represented and unanimously accept that the board meeting be held".

The procedure followed involves sending, usually a week in advance, the call to meeting, the agenda and any information that is available and may be useful for more accurate knowledge of the matters to be discussed in the Board session.

To this end, the Board's documentation is made available to the directors through a computer platform, which allows them permanent access to it. The directors have access to the documentation of all bodies of the Board, irrespective of whether or not they are members of a Committee. In addition, directors are provided with other information relevant to the exercise of their functions (relevant events, new regulations, access to press reviews, etc.) through the platform.

Furthermore, during the meeting, those directors whose issues are being dealt with at the meeting are available to be called -and they frequently are called -so that the directors in attendance can ask them directly for any clarifications, details or opinions in relation to the items discussed in the session and can directly appreciate their suitability for the position.

Finally, the directors may request additional information they deem necessary for the exercise of their duties through the Board Secretary.

C.1.36 Indicate and, where applicable, give details of whether or not the company has laid down rules that oblige the directors to report and, if necessary, resign in cases that damage the company's credit and reputation:

YES [X] NO [ ]

Explain the rules

In accordance with article 11.3 of the Board Regulations, the director is subject to the duty of loyalty under the terms established in prevailing legislation and, in particular, section e) of said article 11.3, establishes that

the director shall inform the company of any kind of legal or administrative claim or any claim of any nature in which he/she is involved which, due to its significance, could have a serious bearing on the reputation of the company. The Board shall examine the matter and adopt the appropriate measures in the company's interest and with the required urgency.

Also, directors shall be compelled to tender their resignation to the Board of Directors and proceed with the pertinent resignation, if the latter deemed it appropriate, in the following cases:

a) When executive directors step down from their executive positions.

b) When they are subject to any of the conditions of professional prohibition or incompatibility pursuant to applicable laws, the Articles of Association or these regulations.

c) When they commit a serious breach of their obligations as directors, jeopardising the interests of the Company.

d) When the reason why they were appointed as independent, executive or proprietary directors is no longer applicable.

C.1.37 Indicate whether or not any member of the Board of Directors has informed the company that he/she has been prosecuted or hearings against him/her have been opened for any of the offences laid down in Article 213 of the Corporate Enterprises Act:

YES [ ] NO [X]

Director's name	Criminal case	Observations

Indicate whether or not the Board of Directors has analysed the case. If the answer is affirmative, give a reasoned explanation of the decision taken as to whether or not the director remains in his/her post or, where appropriate, list the actions taken by the Board of Directors up to the date of this report or those scheduled to be taken.

YES [ ] NO [X]

Decision taken/action taken	Reasoned explanation

C.1.38 Detail the major agreements entered into by the company and which remain in force, are modified or conclude in the event of a change of control of the company based on the takeover, and the effects of these agreements.

An important part of the Naturgy investee companies with shareholders outside the group contain change of control clauses whereby the other shareholder is entitled to choose to acquire the shareholdings in the event of change of control of the holding company of the Naturgy Group.

On the other hand, most of the outstanding financial debt includes a clause related to the change of control, either by acquiring more than 50% of the voting shares or by obtaining the right to appoint the majority of members of the Board of Naturgy Energy Group, S.A. These clauses are subject to additional conditions, whereby their activation depends on the simultaneity of some of the following events: the significant reduction of the credit rating caused by the change of control, or the loss of the investment grade by the rating agencies; the inability to meet the financial obligations of the contract; material damage to the creditor, or a material adverse change in solvency. These clauses entail the repayment of the debt, although they usually have a longer period than that granted in the event of early termination.

More specifically, the bonds issued, with an approximate value of Euros 9.7 billion (standard practice in the Euromarket), would be susceptible to early maturity providing that the change of control causes a fall of two or more full notches in at least two of the three ratings it had or all of the ratings fall below investment grade, and providing the Rating Agency explains that the reduction of the credit rating is caused by the change of control.

There are also loans for an amount of approximately Euros 2 billion, linked to long-term infrastructure financing with funds from the European Investment Bank, which could be subject to early repayment in the event of a change of control. To activate these clauses, in addition to the change of control event a reduction of the rating is required, and they have special repayment terms for the debt that are longer than those of early termination cases.

C.1.39 Identify, individually, when referring to directors and in aggregate form in all other cases, and provide detailed information on agreements between the company and its officers, executives and employees that provide indemnities for the event of resignation, unfair dismissal or termination as a result of a takeover bid or other type of operations.

Number of beneficiaries	23
Beneficiary type	**Description of the agreement**
Former Chief Executive Officer	The contract of the CEO, who served the Company until February 2018, established compensation for three years of the total remuneration on the date of the contractual amendment for certain cases of termination of the contractual relationship: through a decision by the company, except for very serious and culpable breach of his professional obligations that causes serious harm to the interests of Naturgy, through a decision of the CEO or through termination of the contract. As a post-contractual non-competition agreement compensation was also established amounting to a full year of total remuneration. On 6 February 2018, the Board of Directors agreed to terminate the contract, pay the compensation envisaged for the amount of three years of the total compensation for the amount of Euros 10,685,763 and compensation for a non-competition agreement for one year's total remuneration, that is, Euros 3,561,921, as well as settling the outstanding amounts of the different remuneration items accrued in 2018 -fixed, annual variable and ongoing PREMP programmes.
Current Executive Chairman	The Chairman's contract establishes compensation for the cessation or non-renewal of the position of director for the overall amount of two years of: (i) fixed total annual cash remuneration, (ii) the annual variable remuneration and (iii) according to the concept of multi-year variable remuneration, a lump sum equivalent to 1.25 of the fixed total annual cash remuneration. This concept will only be multiplied by a full year if, at the time of accrual, the minimum profitability target of the LTI plan has not been reached; the second full year can be recovered if the minimum target was finally reached at the end of the plan. The compensation will not be payable in the event of serious and culpable breach of their professional obligations that causes significant damage to the interests of Naturgy. As a post-contractual non-competition agreement compensation was also established amounting to a full year of total remuneration. The contract of the Executive Chairman sets out the termination of the contract and the payment of compensation if he forfeits his executive functions and will continue as non-executive Chairman. In this case, the compensation provided is identical to that of the previous section, but reduced by half, that is, one full year.
Executives	The contracts signed with 16 executives contain a clause that establishes a minimum compensation of one full year of fixed remuneration in some cases and two full years of compensation in others in certain cases of termination of the relationship, which include certain cases of change of control, unfair dismissal or the cases set out in Arts. 40, 41 and 50 of the Workers' Statute. These contracts also contain a clause which sets out compensation equivalent to one year's fixed remuneration for post-contractual non-competition for a period of two years. In addition, 2 executives have compensation agreements whose amounts entitle them to receive a minimum compensation of one fixed full year of remuneration in some cases and two full years of compensation in others in certain cases of termination of the relationship, which include unfair dismissal or the cases set out in Arts. 40, 41 and 50 of the Workers' Statute. Moreover, there are compensation agreements with four other executives, equivalent to one year's fixed remuneration for post-contractual non-competition for a period of two years.

Indicate whether, beyond the cases stipulated by the regulations, these contracts have to be reported and/or approved by the bodies of the company or its group. If so, specify the procedures, assumptions foreseen and the nature of the bodies responsible for their approval or communication:

	Board of Directors	General Meeting
Body that authorises the clauses	YES	NO

	YES	NO
Is the General Meeting informed of the clauses?	X	

Observations
In relation to the clauses of management personnel, the Appointments and Remuneration Committee and the Board are informed of their terms and beneficiaries.

C.2. Committees of the Board of Directors

C.2.1 Give details of all the board committees, their members and the proportion of executive, proprietary and independent directors:

Executive or delegated committee

Name	Position	Category

% of executive directors	
% of proprietary directors	
% of independent directors	
% of other external directors	

Observations
It does not apply as the executive committee no longer exists.

Explain the committee's duties, describe the procedure and organisational and operational rules and summarise the main actions taken during the year.

Not applicable

Indicate whether the composition of the Delegated or Executive Committee reflects the participation in the board by the various directors depending on their category:

YES ☐ NO ☐

If the answer is negative, explain the composition of your Delegated or Executive Committee
Not applicable.

Audit committee

Name	Position	Category
Mr Francisco Belil Creixell	Chairman	Independent
Mr Ramón Adell Ramón	Board Member	Independent
Mr Enrique Alcántara-García Irazoqui	Board Member	Proprietary
Mr Pedro Sainz de Baranda Riva	Board Member	Independent
Ms Helena Herrero Starkie	Board Member	Independent
Mr Rajaram Rao	Board Member	Proprietary
Theatre Directorship Services Beta, S.à.r.l., represented by Mr Jose Antonio Torre de Silva Lopez de Letona	Board Member	Proprietary

% of proprietary directors	42.86%
% of independent directors	57.14%
% of other external directors	-

Observations

Explain the functions, including, if applicable, those additional to those legally envisaged, which have been attributed to this committee, describe the procedures and rules for the organisation and functioning of the same. For each of these functions, indicate its most important actions during the year and how it has exercised in practice each of the functions attributed to it either in the law or in the articles of association or other corporate resolutions.

a) Functions of the Audit Committee:

The Committee has the powers set out in Law and those entrusted to it by the Board of Directors in a general or specific manner.

In response to different resolutions of the Board of Directors of 27 November 2015, 29 January 2016 and 6 March 2018, it exercises the following functions:

- Prepare the report on auditor independence.
- Prepare the report on the performance of the Audit Committee.
- Prepare the report on related-party transactions.
- 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 Committee and the Auditors should give a clear account to shareholders of their scope and content of said limitations.
- With respect to control and reporting systems:
  - (a) Supervising the preparation and completeness of the financial information concerning the company and, if appropriate, the group, checking due compliance with the governing regulations, the proper delimitation of the consolidation criteria and the correct application of accounting criteria.
  - (b) Ensuring the independence of the unit handling the internal audit function; approve its priorities and work programmes, ensuring that it focuses primarily on the main risks the company is exposed to; receive regular reports on its activities; and verify that senior management is acting on the findings and recommendations of its reports. Propose to the Chairman of the Board of Directors the selection, appointment, re-election and removal of the person responsible for the internal audit service, as well as proposing the budget for that service, with the final decision corresponding to the Chairman of the Board of Directors.
  - (c) Setting up and supervising 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.

- With regard to the external auditor.
  - (a) In the event of resignation of any external auditor, the Committee should investigate the issues giving rise to the resignation.
  - (b) Ensuring that the remuneration of the external auditor does not compromise its quality or independence.
  - (c) Supervising that the company notifies any change of external auditor to the National Securities Market Commission as a relevant event, accompanied by a statement of any disagreements arising with the outgoing auditor and the reasons for the same.
  - (d) Ensuring that the external auditor has a yearly meeting with the board in full to inform them of the work undertaken and developments in the company's risk and accounting positions.
  - (e) Ensuring 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.
- Call any of the Company's employees or managers, and also have them appear without the presence of any other executive.
- Analyse and report to the Board of Directors on the economic conditions and the accounting impact and, especially, where applicable, on the exchange ratio, in relation to the operations of structural and corporate modifications that, due to their nature or amount, are of special relevance. Transactions whose net value exceeds the value of 25% of the assets that appear on the last approved balance sheet of the Company will be deemed relevant.
- In addition:
  - (a) Supervision of compliance with the internal codes of conduct.
  - (b) Overseeing the communication and relations strategy with shareholders and investors, including small and medium-sized shareholders.
  - (c) The regular evaluation of the adequacy of the company's corporate governance system
  - (d) Monitoring and assessing the processes of liaising with different stakeholders.
  - (e) The evaluation of the company's non-financial risks

b) Procedures, and organisational and operational rules

in accordance with Article 26 of the Regulations of the board

The Audit Committee shall comprise a minimum of three and a maximum of seven directors appointed by the Board of Directors from among the non-executive directors, and one of them will be appointed taking into account their knowledge and experience in issues of accountancy, audit or both. Its members shall leave their post when they do so in their capacity as directors or as agreed by the Board of Directors.

The Board of Directors shall elect the Chairman from amongst the members of the Committee, the majority of whom will have the status of independent director; the Chairman shall not have the casting vote. The post of Secretary of the Committee will be held by the person who is the Secretary of the Board of Directors, if there is one.

The committee shall hold meetings whenever necessary in order to issue its reports or proposals, and will be convened by its Chairman on his own initiative or upon prior request of two of its members. At least four meetings per year must be held. The committee may invite to its meetings any executive or employee it deems appropriate.

c) Main actions taken during the year 2018

In the exercise of its powers during the financial year it has reported and/or adopted proposals, among others, on the following matters:

- Quality and efficiency of its operation.
- External audit of the individual and consolidated annual accounts.
- Supervision of the process of preparation of financial reporting.
- Tax situation
- Independence of the auditor.
- Related-party transactions
- Verification of the crime prevention system.
- Supervision of risk control systems and specific risk analysis
- Supervision of internal control and internal audit systems

Identify the directors who are members of the Audit Committee who have been appointed Chairman on the basis of knowledge and experience of accounting or auditing, or both, and state the date that said director was appointed Chairman.

Name of directors with experience	Mr Ramón Adell Ramón
Date of appointment as Chairman	27/06/2018

Observations:

Appointments and remuneration committee

Name	Position	Category
Mr Ramón Adell Ramón	Chairman	Independent
Mr Francisco Belil Creixell	Board Member	Independent
Mr Pedro Sainz de Baranda Riva	Board Member	Independent
Mr Claudi Santiago Ponsa	Board Member	Independent
Mr Marcelino Armenter Vidal	Board Member	Proprietary
Mr William Alan Woodburn	Board Member	Proprietary
Rioja Bidco Shareholdings SLU Mr Javier De Jaime Guijarro	Board Member	Proprietary

% of proprietary directors	42.86%
% of independent directors	57.14%
% of other external directors	-

Observations

Explain the committee's duties, describe the procedure, and organisational and operational rules. For each of these functions, indicate its most important actions during the year and how it has exercised in practice each of the functions attributed to it either in the law or in the articles of association or other corporate resolutions.

a) Duties of the Appointments and Remuneration Committee:

The Committee has the powers set out in Law and those entrusted to it by the Board of Directors in a general or specific manner.

The Board of Directors has entrusted it with the following functions:

- Prepare the report on performance of the Appointments and Remuneration Committee.
- Verify the selection policy for directors and report on this in the Annual Corporate Governance Report.
- Through delegation that must be granted by the Chairman of the Board, to organise and coordinate the regular assessment of the Board and that of the chief executive of the Company.
- Prepare the report on the operation of the Board of Directors.
- Propose to the Board of Directors the standard conditions for senior executives contracts.
- Monitor compliance with the remuneration policy set by the company.
- Regularly review the remuneration policy for directors and senior executives.
- Ensure that conflicts of interest do not undermine the independence of any external advice the committee engages.
- Verify information on remuneration of directors and senior executives contained in the various corporate documents.
- Through a resolution of the Board of Directors on 29 January 2016, it was entrusted with the exercise of all the corporate social responsibility powers that hitherto had been exercised by the Audit Committee.
- Through a resolution of the Board of Directors on 6 March 2018, it was agreed to entrust the Appointments and Remuneration Committee with the following tasks previously entrusted to the Audit Committee:
  i) Monitor the most relevant incidents in terms of health, safety and the environment.
  ii) Raise proposals and report on initiatives in corporate governance.

b) Procedures, and organisational and operational rules

in accordance with Article 25 of the Regulations of the board

The Appointments and Remuneration Committee shall comprise a minimum of three and a maximum of seven directors appointed by the Board of Directors from among the non-executive directors, and one of them will be appointed taking into account their knowledge and experience in issues of accountancy, audit or both. Its members shall leave their post when they do so in their capacity as directors or as agreed by the Board of Directors.

The majority of members of the Committee will hold the status of independent director, from among which the Board of Directors will elect the Chairman of the same, who will not have a casting vote. The post of Secretary of the Committee will be held by the person who is the Secretary of the Board of Directors, if there is one.

The committee shall hold meetings whenever necessary in order to issue its reports or proposals, and will be convened by its Chairman on his own initiative or upon prior request of two of its members. At least four meetings per year must be held. The committee may invite to its meetings any executive or employee it deems appropriate.

c) Main actions taken during the year 2018.

The Appointments and Remuneration Committee has focused its actions on three fundamental aspects:

i) Corporate governance: it has proposed the adoption and implementation of an Action Plan on corporate governance, which included important simplification measures (reduction in the number of directors, changes in the main regulatory texts, etc.)

ii) Proposal for new directors: in light of the profiles whose reinforcement was detected as a result of the self-assessment process carried out with the help of an external consultant, it analysed and issued an opinion about the candidates to fill the positions of proprietary directors and formulated the corresponding proposals with regard to independent directors.

iii) Remuneration: the new remuneration scheme of the Executive Chairman and senior management has been analysed in detail, especially with regard to the new long-term incentive. The remuneration policy of the Company has also been analysed for approval by the Board.

The committee has also worked on the following aspects:

- Quality and efficiency of its operation.
- Supervision of the corporate social responsibility model
- Health and safety

Appointments committee

Name	Position	Category

% of proprietary directors	
% of independent directors	
% of other external directors	

Observations

Explain the committee's duties, describe the procedure and organisational and operational rules and summarise the main actions taken during the year.

Remuneration committee

Name	Position	Category

% of proprietary directors	
% of independent directors	
% of other external directors	

Explain the committee's duties, describe the procedure and organisational and operational rules and summarise the main actions taken during the year.

Committee ___________

Name	Position	Category

% of proprietary directors	
% of independent directors	
% of other external directors	

Explain the committee's duties, describe the procedure and organisational and operational rules and summarise the main actions taken during the year.

C.2.2 Complete the following table on the number of female directors on the various board committees over the past four years:

	Number of female directors							
	2018 Number	%	2017 Number	%	2016 Number	%	2015 Number	%
Executive Committee	-	-	1	10%	1	10%	0	0
Audit Committee	1	14.28%	2	28.57%	2	28.57%	0	0
Appointments and Remuneration Committee	0	0%	1	20%	1	20%	1	33%
Appointments Committee	-	-	-		-	-	-	-
Remuneration Committee	-	-	-		-	-	-	-
Committee _____	-	-	-		-	-	-	-

C.2.3 Indicate, where applicable, the existence of committee regulations, the location at which they are available for consultation and the modifications that have been made during the financial year. Also indicate whether any annual report on each committee's activities has been voluntarily drafted.

The Board Committees are regulated in the Articles of Association and in the Regulations for the Organisation and Functioning of the Board of Directors of Naturgy and its Committees.

Both documents are published on the Company's website (www.naturgy.com) →Shareholders and investors →Corporate governance → Corporate governance standards.

The Executive Committee, the Audit Committee and the Appointments and Remuneration Committee have all drawn up a report on the quality and efficacy of their performance over the previous year.

D. Related-party transactions and intra-group transactions

D.1 Explain, if applicable, the procedures for approving related party or intra-group transactions.

Procedures for approving related party transactions

In accordance with art. 3.II h) of the Board Regulations, among the powers that cannot be delegated by the Board but that may be adopted by the Executive Committee or by the CEO(s) for reasons of urgency duly justified and which must be ratified in the first Board Meeting to be held after the adoption of the decision is the approval, following a report from the Audit Committee, of the operations that the Company or its group companies carry out with directors, under the terms established in prevailing legislation, or with main shareholders, individually or in concert with others, of a significant stake, 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.

In some circumstances and to a limited extent, the Board has granted generic authorisations for transactions related to one of its shareholders, always in matters of a minor nature linked to the ordinary trade of the Company, and with the requirement that they be carried out under arm's length conditions and with the obligation to report the use of such authorisation to the Audit Committee every year.

As regards operations with Caixabank, this entity was controlled and formed a group with Criteria until 2017 when the conditions established by the ECB for deconsolidation were met.

D.2 List any relevant transactions, by virtue of their amount or importance, between the company or its group of companies and the company's significant shareholders:

Name or company name of significant shareholder	Name or company name of the company or entity of the group	Nature of the relationship	Type of operation	Amount (thousands of euros
Criteria Caixa S.A.U.	Naturgy Energy Group, S.A.	Commercial	Reception of services	12
Criteria Caixa S.A.U.	Naturgy Energy Group, S.A.	Commercial	Provision of services	36
Criteria Caixa S.A.U.	Naturgy Energy Group, S.A.	Commercial	Sales of manufactured goods or not	3,095
Criteria Caixa S.A.U.	Naturgy Energy Group, S.A.	Commercial	Dividends and other distributed earnings	346,808
Repsol, S.A.	Naturgy Energy Group, S.A.	Commercial	Reception of services	3,944
Repsol, S.A.	Naturgy Energy Group, S.A.	Commercial	Procurement of manufactured goods or not	160,003
Repsol, S.A.	Naturgy Energy Group, S.A.	Commercial	Provision of services	20,545
Repsol, S.A.	Naturgy Energy Group, S.A.	Commercial	Sales of manufactured goods or not	367,115
Repsol, S.A.	Naturgy Energy Group, S.A.	Commercial	Purchase of tangible fixed assets	295
CVC Capital Partners Sicav-Fis S.A.	Naturgy Energy Group, S.A.	Commercial	Dividends and other distributed earnings	281,202
Gip III Canary 1, S.À R.L.	Naturgy Energy Group, S.A.	Commercial	Dividends and other distributed earnings	280,193

Observations

D.3 Detail those transactions that are significant because of their amount or which are materially relevant, performed between the company or entities within its group and the company's administrators or executives:

Name or company name of the administrators or executives	Name or company name of the related party	Relationship	Nature of the operation	Amount (thousands of euros)

Observations

D.4 Report on the significant transactions carried out by the company with other companies belonging to the same group, provided that they are not eliminated in the process of drafting the consolidated financial statements and are not part of the company's usual trading in terms of its purpose and conditions.

En todo caso, se informará de cualquier operación intragrupo realizada con entidades establecidas en países o territorios que tengan la consideración de paraíso fiscal:

Company name of the entity of the group	Brief description of the operation	Amount (thousands of euros)

Observations

D.5 Indicate the amount from related party transactions.

0 (in thousands of euros).

D.6 List the mechanisms established to detect, determine and resolve any possible conflicts of interest between the company and/or its group, and its directors, management or significant shareholders.

1. Directors:

   In accordance with the Regulations of the Board:

   – The Director is subject to the duty of loyalty under the terms established in prevailing legislation and, in particular:

   – The director must refrain from participating in deliberating and voting on resolutions or decisions in which they or a related person have a direct or indirect conflict of interests. Resolutions or decisions that affect them in their capacity as director, such as their appointment to or removal from posts on the governing body or others of a similar nature, will be excluded from the preceding obligation.

   – Also, the director shall adopt the measures required to avoid becoming involved in situations in which their interests, either for their own personal reasons or those of another party, may conflict with the company's interest or with their duties with the company.

   – In his/her capacity as loyal representative of the Company, the director must inform the company of shares in the company he/she holds, directly or through companies in which he/she has a majority holding, following the procedure and other processes that are established for investment in Naturgy Energy Group S.A. and investee companies.

   – The director must notify the Company of significant changes to their professional circumstances and changes which affect the nature or capacity by which he/she was categorised.

   - The director shall inform the company of any kind of legal or administrative claim or any claim of any nature in which they are involved which, due to its significance, could have a serious bearing on the reputation of the company. The board shall examine the matter and adopt the appropriate measures in the company's interest and with the required urgency.

   – The Board of Directors shall endeavour, at all times, to prevent proprietary directors from using their position to obtain asset benefits without adequate compensation, to the advantage of the shareholder that put them forward for the position.

     The Director must abstain from conducting activities for themselves or for another party which, actually or potentially, entail effective competition with the Company or which, in any other manner, place them in permanent conflict with the Company's interests. Particularly, the director, may not hold, himself or by means of a representative, posts of whatsoever kind in companies or enterprises that compete with Naturgy Energy Group S.A. or any company in its group, or provide the same services of representation or consultancy in favour thereof. A company shall be considered as a competitor of Naturgy Energy Group S.A., when, directly or indirectly, or through companies in its group, it is devoted to any of the activities included in the corporate purpose of Naturgy Energy Group S.A.

2. Directors and executives:

   On the other hand, pursuant to Art. 5 of the Internal Code of Conduct in Matters Relating to the Securities Markets (ICC), persons with management responsibilities and insiders, during certain periods of time will refrain from carrying out transactions on their own or for the account of a third party, directly or indirectly on the Affected Securities ((i) The transferable securities issued by the Company and/or by the companies of the Naturgy Group that are traded on a secondary market or other regulated markets, in multilateral trading systems or on other organised secondary markets, or in respect of which an application for admission to trading in one of such markets or systems has been filed; (ii) Financial instruments and contracts of any kind that grant the right to acquire the securities indicated in (i); (iii) Financial instruments and contracts whose underlying assets are the securities indicated in (i), and (iv) For the sole purpose of the rules of conduct in relation to the privileged information contained in Title III of the Regulations, the securities and financial instruments issued by other companies or entities other than the Company, for which Inside Information is available.)

Internal Audit, upon written request to the Board Secretary by the stakeholder, may authorise Persons with Management Responsibilities to perform personal transactions on Affected securities in the periods in which there is a general prohibition when certain circumstances are given and justified in the ICC itself. Internal Audit will inform the Audit Committee at least once a year about the authorisations that have been requested.

For their part, pursuant to section 4.10 of the Code of Ethics, employees must inform the company in the event that they or their close relatives participate or will participate on the governing bodies of other companies that may clash with the interests of Naturgy. In the performance of their professional responsibilities, employees must act with loyalty and defend the interests of the group. Furthermore, they must avoid situations that may give rise to a conflict between personal interests and the interests of the company. Accordingly, Naturgy employees must refrain from representing the company and participating in and influencing decisions in any situation in which they directly or indirectly have a personal interest.

3. Significant shareholders:

It will be the responsibility of the Board of Directors, pursuant to a report from the Audit Committee, to approve transactions carried out by the company or the companies in its Group with directors under the terms set forth in the current applicable legislation or with shareholders who, individually or in conjunction with others, hold a significant stake, including shareholders represented on the company's Board of Directors or the boards of other companies belonging to the same group or with persons associated with them.

D.7 Is more than one group company listed in Spain?

YES ☐ NO ☒

Identify the subsidiary companies that are listed in Spain:

Listed subsidiary companies

Indicate whether or not their respective activity areas and possible business relations between them have been publicly defined, as well as those of the listed subsidiary with the other companies in the group:

YES ☐ NO ☐

Define the possible business relationships between the parent company and the listed subsidiary company and between the listed subsidiary and the other companies in the group

Indicate the mechanisms laid down to solve possible conflicts of interests between the listed subsidiary and the other companies in the group:

Mechanisms for solving possible conflicts of interests

E. Control systems and risk management

E.1 Describe the risk management system in place at the company, including fiscal risks.

The Risk Management System works in a comprehensive and continuous way, and integrates the corporate visions of Corporate Governance, Risks and Compliance of the Company, enabling a full overview of the Group's processes, the existing controls over these and the associated risk.

The system ensures the independence of the control and risk management functions attributed to each of the responsible bodies and units, and is responsible for determining thresholds for the main risk categories in order to define the overall risk profile of the Company, guaranteeing the predictability of its performance in all relevant aspects for its stakeholders.

The main objective of global risk management is to ensure that the most relevant risks are correctly identified, assessed and managed, to ensure that the level of risk exposure assumed by Naturgy in the performance of its activities is consistent with the global profile of defined objective risk and with the achievement of the annual and strategic objectives..

E.2 Identify the bodies responsible for preparing and implementing the risk management system, including fiscal risks.

Risk Committee

It regularly evaluates and determines the overall risk profile of Naturgy, based on the information requested from the different responsible Units and proposes the global risk limits for consideration and approval by the Chairman, thus determining the global profile of objective risk.

Financial area

Through its Risk and Insurance Unit, it is responsible for providing support to the Risk Committee in the determination and monitoring of the global risk profile and the determination of the objective risk profile, by introducing policies and metrics in coordination with the business units affected. In particular, it is responsible for coordinating with the relevant units and issuing the recurring risk reports to be forwarded to the Board of Directors, including the Corporate Risk Map.

Internal auditing

It is responsible for ensuring effective supervision of the internal control system that ensures efficiency and effectiveness in operations, transparency and reliability of financial and management reporting, the safeguarding of group assets and compliance with applicable internal and external regulations, as well as making independent and objective contributions to add value and improve the operations of the organisation and contribute to the interests of shareholders. By the same token, through appropriate audits, it is responsible for examining the level of compliance with this Risk Control and Management Policy and the implementing procedures.

Audit Committee

It is an advisory body that provides specialized advice on everything related to external auditing, risk management systems and internal control.

The Business, Service and Project Units

They are responsible for risk management in their areas of responsibility, observing, reporting, managing and mitigating the different risks that have been identified.

E.3 Indicate the main risks, including fiscal, which may prevent the company from achieving its business targets.

	Description	Management
Market risk		
Gas price	Volatility in international markets which determine gas prices.	Physical and financial hedges. Portfolio management.
Electricity price	Volatility in electricity markets in Spain and Portugal.	Physical and financial hedges. Optimisation of generation park.
Gas volume	Gap between gas supply and demand.	Optimisation of contracts and assets. Trading.
Electricity volume	Reduction in available thermal gap. Uncertainty in the volume of hydraulic production	Optimisation of commercialisation-generation gap.
Regulation	Exposure to revision of criteria and levels of return recognised for regulated activities.	Heightened intensity of communication with regulatory bodies. Adjusting efficiencies and investments to recognised rates.
Exchange rates	Volatility in international currency markets.	Geographical diversification. Hedges through financing in local currency and derivatives. Monitoring of the net position.
Interest rates and credit spread	Volatility in financing rates.	Financial hedges. Diversification in financing sources.

	Description	Management
Fiscal	Ambiguity or subjectiveness in the interpretation of the prevailing fiscal regulations, or through a relevant change to the same.	Consultations with independent expert organisations. Recruitment of leading consultancy firms. Adhesion to the Code of Good Tax Practices. Allocation of provisions with criteria of prudence.
Credit risk		
Credit.	Uncertainty over the evolution of ratios of payment default conditioned by the economic cycle.	Análisis de solvencia de clientes para definir condiciones contractuales específicas. Proceso de recobro.
Operational risk		
Operational: image and reputation	Deterioration in perception of Naturgy by different stakeholders.	Identification and tracking of potential reputation events. Transparency in communication.
Operational: insurable.	Accidents, damages or non-availabilities in assets of Naturgy.	Ongoing improvement plans. Optimisation of total cost of risk and hedging.
Operational: environment	Damages to the natural and/or social environment. Evolution of environmental regulation.	Emergency plans in installations with risk of environmental accidents. Specific insurance policies. Complete environmental management.
Operational: climate change	Evolution of environmental factors as a consequence of climate change. Regulation geared towards fighting it.	Corporate positioning with regard to climate change. Active participation on influence forums.
Operational: cybersecurity	Attacks on computer systems.	Implementation of security measures Analysis of events and application of remedies Training.

E.4 Identify if the company has a risk tolerance level, including tax risks.

The company has levels of risk tolerance established at corporate level for the main kinds of risks.

The risk assessment process lies in identifying the risks, generally by those businesses that are subject to risk exposure. This identification takes place at the time the risk exposure originates. However, an in-depth review is carried out every year by the Risk Units to ensure proper identification of all risk exposures, whether current or future.

It is the Risk Units's responsibility to assess the risks identified, based on:

a) Risk position: definition and characteristics.

b) Impact variables.

c) Qualitative and quantitative severity of the risk occurring.

d) Probability of risk occurring.

e) Defined mitigation controls and mechanisms, and their effectiveness.

Lastly, it will propose a tolerance level for the types identified, which will be approved by the Risk Committee.

E.5 Identify any risks, including tax risks, which have occurred during the year.

The risks that have materialised during the financial year have been inherent to the activity carried out, such as: exposure to regulatory risks, volatility of fuels and of the pool in Spain, the exchange, interest, credit or counterparty rates.

The risk control mechanisms have enabled the company to keep their impact within the established tolerance range, defined by means of the current risk limits.

Faced with uncertainty in the domestic and worldwide economic outlook, the company will seek to position itself in countries that promote legal security, economic developments in stable macroeconomic environments that ensure steady growth that contributes to the generation of value and profitability of business and enterprise, balancing the weight of its businesses in its mix of activities, and it will place greater focus on increasing the contribution of regulated activities and a more electric profile.

Subsequent to the approval of the new Strategic Plan 2018-2022, asset impairment or write-offs of Euros 4,851 million have been recorded, caused by the reassessment of future cash flow estimates based on the aforementioned plan, as well as other factors that have occurred during the period.

E.6 Explain the response and monitoring plans for the main risks the company is exposed to, including tax risks.

The risks regarding the performance of Naturgy are set out in the company's Corporate Risk Map, containing:

- Definition and characteristics of the main risk factors.
- Evolutionary aspects of the Risks Map.
- Impact variables.
- Main measurement methodologies used for each kind of risk.
- Qualitative, quantitative and probable severity of the risk materialising.
- Defined controls and their effectiveness.

The Risk Control Units t and other specific areas (Regulation, Environment, Generation) perform periodic measurements of the evolution of main risks, duly giving the opportune instructions in the event of observing levels of exposure or trends in risk evolution that could exceed the established

F. Internal systems of control and risk management with regard to the internal control systems over financial reporting (ICFR)

Describe the mechanisms that make up your entity's internal control system and management of risks with regard to the financial information reporting process (ICFR).

F.1 The company's control environment

Report on, duly detailing their main characteristics, at least:

F.1.1. Which bodies and/or functions are in charge of: (i) the existence and upkeep of an appropriate and effective ICFR; (ii) its implementation; and (iii) its supervision.

Naturgy has defined its Internal Control System over Financial Reporting (hereinafter "ICFR") in the "Internal Control System over Financial Reporting (ICFR) General Standard of Naturgy".

As part of the ICFR, Naturgy has defined, in the foregoing General Standard, the responsibilities model of the same. This model revolves around the following five areas of responsibility:

– Board of Directors: The board is responsible for the existence of an appropriate and efficient ICFR, the supervision of which is delegated upon the Audit Committee.

  The Board Regulations of Naturgy Energy Group, S.A. and its Committees, in article 3 section II, establish that the determination of the risk control and management policy, including tax risk, and supervision of the internal information and control systems are, among others, a matter that cannot ordinarily be delegated by the Board of Directors.

– Audit Committee: Among other tasks, this committee is responsible for supervision of the ICFR. Article 26 section 2 of the Board Regulations states that the Committee has the powers set out in Law and those entrusted to it by the Board of Directors in a general or specific manner. Thus, article 529.14 of the Corporate Enterprises Act sets out in section 4.b) that the Audit Committee will have the function of supervising the effectiveness of the company's internal control, internal audit and risk management systems, as well as discussing with the accounts auditor the significant weaknesses of the internal control system detected in performance of 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 preparation process and integrity of the financial information related to the company and, where applicable, the group, reviewing compliance with the standard requirements, the appropriate definition of the consolidation perimeter and the correct application of accounting criteria. For the performance of some of these duties, the Audit Committee is supported by the Internal Auditing Unit.

– Financial Department: This department is responsible for the design, implementation and operation of the ICFR. For the performance of this duty, it is supported by the Accounting Unit.

- Internal Auditing Unit: In general, it is responsible for assisting the Audit Committee in the ongoing review and assessment of the effectiveness of the Internal Control System in all areas of Naturgy, providing a systematic and rigorous approach for the monitoring and improvement of processes and for the assessment of operational risks and controls associated to these, including those corresponding to the ICFR and to the Crime Prevention Model.

- Compliance Unit.

- Business units, services and projects units involved in the financial reporting process. These are responsible for carrying out the processes and maintaining daily operations to ensure that the control activities introduced are performed.

F.1.2. Whether or not the following elements exist, particularly with regard to the procedure for financial reporting:

- **Departments and/or mechanisms responsible for: (i) the design and review of the organisational structure; (ii) the clear definition of the lines of responsibility and authority, with an appropriate distribution of tasks and duties; and (iii) that there are sufficient procedures for proper dissemination at the entity.**

The design and review of the organisational structure of top tier management, as well as definition of the lines of responsibility, are carried out by the Board of Directors, through the CEO and the Appointments and Remuneration Committee.

To ensure proper management of the group's economic-financial reporting, the Financial Department has developed, as part of the ICFR, a technical instruction comprising an interrelationships map (information flows) for the financial reporting process. This map documents communications between the Financial Department, the different parties in charge of the processes and those in charge that are either the source or destination of the financial reporting. The map is called "Interrelationships Map of Financial Reporting of Naturgy".

In this regard, there are six main areas that Naturgy has taken into consideration in compiling the interrelationships map showing the financial reporting processes:

(i) the information required to prepare the financial reporting;

(ii) the parties in charge that are either the source or destination of the financial reporting and

(iii) the distribution of tasks among the different organizational units

(iv) the scope of this distribution to all group companies

(v) the frequency of information transfer.

(vi) the information systems that are involved in the drafting process and for the issue of the financial reporting;

Thus, using the interrelationships map of Naturgy, the processes that have an impact on the preparation of financial reporting are clearly defined, both the operational processes that have a relevant impact on financial reporting, as well as those processes associated to the administrative and accounting area, and those managers involved in the same.

- **Code of Conduct, approval body, level of dissemination and instruction, principles and values included (indicating whether or not there are specific mentions to the register of operations and the preparation of financial reporting), the body in charge of analysing breaches and proposing corrective actions and fines.**

The undertakings of senior management of Naturgy include focusing their efforts on ensuring that operations are carried out within an environment of professional and ethical practices, not only through the introduction of mechanisms targeted at preventing and detecting fraud committed by employees, or inappropriate practices that could lead to sanctions, fines or which could damage the image of Naturgy, but also reinforcing the importance of ethical values and integrity among its professionals.

In this regard, Naturgy has a Code of Conduct (hereinafter "Code of Ethics"), which was approved by the Board of Directors on 31 March 2005. This code is mandatory for all employees of Naturgy Energy Group, S.A and for all investee companies in which Naturgy holds management control. The updates and modifications to the Code of Ethics are carried out by the Board of Directors of Naturgy Energy Group, S.A.

Since it was approved, it has been amended four times, on the last occasion in 27 June 2014, with the object of updating it and including new commitments acquired by Naturgy in relation to the coming into force of the reform of the Penal Code (Organic Law 5/2010), the implementation of a Crime Prevention Model in the group, the issue of the Anti-Corruption Policy of Naturgy and in order to adapt it to the best Corporate Responsibility practices.

The Code of Ethics sets out the general ethical principles for Naturgy as a whole, setting out the values to be pursued in practice throughout the organisation, and which includes: (i) purpose (ii) scope of application (involving all members of Naturgy); (iii) governing criteria of conduct at Naturgy (declaration of the group's style of governance); (iv) conduct guidelines (declaration of key values of Naturgy; (v) acceptance and compliance of the code; (vi) Code of Ethics Committee and (vii) enforceability.

The Code of Ethics considers integrity and responsibility in the exercise of professional activities to constitute a fundamental general criteria for conduct at Naturgy. More specifically, it sets out a series of action guidelines to a greater or lesser extent related to the reliability of the financial reporting and to compliance with applicable regulations, and in particular:

– Respect for the law, human rights and ethical values (Section 4.1)

  "Naturgy undertakes the commitment of acting at all times in accordance with applicable laws, with the internal regulatory system established with internationally accepted ethical practices, with total respect towards human rights and public liberties (...)"

– Processing of information and knowledge (Section 4.11):

  "All employees that enter any kind of information into the group's IT systems must ensure that this information is rigorous and reliable.

In particular, all of the group's economic transactions should be clearly and precisely set out in the corresponding registries, via the pertinent accounts, and in all transactions performed, including all income and incurred expenses.

Employees of Naturgy shall refrain from any practice that contravenes the undertaking to clearly and accurately reflect all financial transactions in the group's accounts".

Naturgy has also established an Anti-Corruption Policy, which was approved by the Management Committee in a meeting held on 3 March 2014, amended in the meeting held on 24 November 2015, and which is compulsory for all employees of all the companies which make up the Naturgy group with majority shareholding and those in which it has responsibility in its operation and/or management. The policy is understood to be an extension of Chapter 4.7. "Corruption and Bribery" of the Code of Ethics of the group, which has the object of establishing the principles which must be used to guide the conduct of all employees and administrators of the companies of Naturgy with regard to the prevention, detection, investigation and remedy of any corrupt practice within the organisation.

In July 2005, Naturgy set up the Code of Ethics Committee with the principal mission of promoting its dissemination and application throughout the group, and to provide a channel of communication to all employees in order to receive inquiries and notifications regarding breaches of the Code of Ethics and the Anti-Corruption Policy. On 30 October 2018, the functions of this Committee were assumed by the Ethics and Compliance Committee.

The Committee is chaired by the Compliance 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 regularly reports to senior management and to the Audit Committee. The nature of the committee is to provide reports and recommendations, proposing corrective actions to those units in charge of providing solutions to problems through practical application of the Code of Ethics and the Anti-Corruption Policy, and simultaneously acting as a bridge between these units and employees.

The sanctionary regime, where necessary, is established by the Human Resources Unit.

To favour not only the exercise of said responsibility but also knowledge and dissemination of the Code of Ethics, this code is available in nine languages:

– Externally: Naturgy corporate website.

– Internally, on the group's Naturalnet platform.

In addition, online training courses through the Corporate University of Naturgy have been developed, which are mandatory for all employees of Naturgy.

Through the Code of Ethics Committee, Naturgy periodically carries out campaigns for the Code of Ethics Compliance Declaration and Anti-Corruption Policy, to disclose the guidelines governing the conduct expected from all employees, to circulate the mechanisms that exist to make inquiries 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.

Naturgy, to encourage the knowledge of the Code of Ethics among its suppliers and collaborating companies sets out a clause in the General Terms and Conditions of Contracting in which it promotes practices which are in keeping with the guidelines for conduct included in the Code of Ethics of Naturgy, and informs them of where they can find the Code of Ethics of the group, along with information in the queries channel and notifications on 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 Naturgy. This 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 Naturgy.

- **Whistleblowing channel, which enables communication to be sent to the Audit Committee concerning any irregularities of a financial and accounting nature, along with any possible breaches of the Code of Conduct and irregular activity within the organisation, and state whether said channel is confidential.**

Professional ethics at Naturgy focuses on professional responsibility and integrity, with integrity understood as ethical and honest action performed in good faith; and professional responsibility as proactive and efficient action targeted at excellence, quality and willingness to serve.

As provided for under Article 26.2 of the Regulations of the Board and its Committees, "the Audit Committee shall have the powers that are provided for by the Law and the powers that are generally or specifically conferred by the Board of Directors". 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 Naturgy, 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 Naturgy (currently, Ethics and Compliance Committee) 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 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 Naturgy 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) for all employees of Naturgy in order to notify aspects related to the code. This channel enables all group employees, suppliers and collaborating companies to obtain or provide information on any issue concerning the Code of Ethics and the Anti-Corruption Policy. Conduct contrary to the code can also be reported in good faith and confidentially. All of this is outside of the hierarchy governing habitual operations performed by employees.

All of the communications are absolutely confidential, and adhere to the limitations established under the Data Protection Act. Accordingly, the chairman of the committee (Compliance 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.

In the 2018 Naturgy Corporate Responsibility Report, further information is provided regarding the Code of Ethics, the Anti-Corruption Policy, the activities of the Code of Ethics Committee (Ethics and Compliance Committee since November 2018) and the use of the communication channel.

- **raining programmes and periodic retraining for personnel involved in the preparation and review of financial reporting, as well as the assessment of the ICFR, which at least cover the accounting, audit, internal control and risk management standards.**

The need to have a sufficient and, above all, updated qualification of those professionals involved in the preparation and review of financial reporting, as well as in the assessment of the ICFR, make it essential to implement an appropriate training plan, by which those persons in charge of each area have the knowledge required to perform the different functions included in the process of preparing and reviewing financial reporting.

To this end, Naturgy has the Corporate University, which is responsible for managing the knowledge and development of persons in all areas of the company. It integrates the model, the channels, the programmes and the training and learning actions of the group, introducing methodologies and training experiences with criteria of quality, impact, efficiency and cost optimisation.

The Corporate University has a quality management system pursuant to the ISO 9001:2015 standard, renewed in 2017 and with CLIP (Corporate Learning Improvement Process) accreditation from the European Foundation for Management Development (EFMD) since 2003 and last renewed in 2018 for a five-year period. This certificate recognises the quality of learning and development processes of people of corporate education organisations.

The aims of the Corporate University are, among others: to guarantee the adequacy of the position/person, the acquisition of knowledge linked to new needs of the organisation and the development of skills and abilities related to the Naturgy leadership and culture model; based on placing an updated and quality training offer at the disposal of employees.

With the implementation of the Evolution - Success Factors platform as a training management tool, to improve and adapt training to the demands of employees and businesses, since 2017 employees and their managers have been involved in defining the training required; in addition, all employees have direct access to all the online training of the company's catalogue, with a model of institutes and knowledge areas and a set of channels for disseminating specific content.

The relevant programmes performed in 2018 included the fourth edition of the Savia programme, with a focus on cybersecurity and innovation. In 2014 the Savia programme 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 programme was commenced, Savia 2.0, which was focused upon the experience of customers and on change management. This programme continued in 2016, placing the focus, on this occasion, on cooperation and empowerment, completing the delivery of the course in October 2017.

Another of the relevant programmes carried out is the development of the online Cybersecurity course for all employees, with a focus on technical knowledge and on the duties and obligations in this area.

The specific knowledge for the economic-financial area covers several objectives, including, making uniform the economic-financial processes developed in any area of the organisation; updating the criteria governing accounting, tax, finance, risk management, management control, international regulations and technical knowledge of the tax area; as well as providing sufficient knowledge on the assessment of companies, financial derivatives and analysis of financial statements.

In total, in 2018 more than 150 professionals from the economic-financial area devoted nearly 1,400 hours to training in specific content, highlighting, among other matters, risk management, taxation, financial management, accounting and budgeting.

F.2 Assessment of financial reporting risks

Provide information, at least, on the following:

F.2.1. What are the main characteristics in the risk identification process, including risks of error or fraudulent practices, with regard to:

- **If the process exists and it is documented.**

The approach used by Naturgy to carry out the financial reporting risk identification and analysis process is set out in three interrelated matrices:

- A matrix for defining the scope of the financial reporting.
- A matrix of risks associated with the financial reporting.
- A matrix of financial reporting control activities.

The matrix for defining the scope of the financial reporting has the object of identifying the accounts and breakdowns which have an associated significant risk, whose potential impact on financial reporting is material and therefore requires special attention. In this regard, a series of quantitative variables (account balance and variation) and qualitative variables (complexity of transactions; changes and complexity in standards; need to use estimates or forecasts; application of judgement and qualitative importance of the information) have been taken into account in the process of identifying accounts and significant breakdowns. The methodology for preparing the scope matrix has been outlined in a technical instruction entitled “Matrix for defining scope of financial reporting of Naturgy”.

For each one of the accounts/significant breakdowns identified in the scope matrix, the critical processes and sub processes associated have been defined, and the risks which might give rise to errors in financial reporting have been identified, covering the objectives for the control of existence and occurrence; integrity; valuation; presentation, breakdown and comparability; and rights and obligations, in the “Risks matrix of financial reporting of Naturgy"

Within the risk identification process defined by Naturgy in its ICFR, problems relating to fraud have been considered to be a very important element. In this regard, the fraud risk control policy of Naturgy is supported by three basic pillars:

– Fraud prevention.

– Fraud detection.

– Investigation and management of fraud situations.

Preventive anti-fraud controls, from the perspective of financial reporting, have been defined, and are classified into two categories. Those called active controls, which are considered to be barriers for restricting or preventing access to valuable assets by persons who might attempt to commit fraud. On the other hand, passive controls aim to prevent fraud by way of dissuasive measures.

Lastly, both the general control activities as well as the process control activities, which consist of the policies and procedures included in all stages of the financial reporting process and which can assure its reliability, are set out in the "Matrix of activities of control for financial reporting in Naturgy".

The ICFR of Naturgy is a dynamic system, so its periodic updating is a fundamental process to comply at all times with the goal of the same, viz., to ensure that the group's financial reporting is reliable. In particular, the definition matrix of the scope thereof is updated yearly.

- **If the process covers all the financial reporting objectives (existence and occurrence; integrity; assessment; presentation, breakdown and comparability; and rights and obligations), if it is updated and how frequently.**

Naturgy, being aware of the importance of having a tool to ensure adequate control of ICFR management, implemented, in 2013, the SAP GRC Process Control, for the comprehensive management of documentation, assessment and oversight of internal control in Naturgy processes. This implementation, which was performed within the framework of the programme for improving the efficiency of Naturgy, was initially carried out in all Spanish companies with majority shareholdings in which the company is held responsible for its operation and/or management. 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 Latin America; in 2015 the implementation was extended to other countries of the group, such as Mexico and France; in 2016 the tool was implemented in Holland, in 2017 in Panama and Brazil. For the implementation of SAP GRC Process Control, both within national and international level, users responsible for the key controls of the ICFR and of the Internal Auditing Unit have provided support.

It is noteworthy to mention that, during the year 2015, the scope of the corporate ICFR 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). Additionally, during 2018, this was extended to companies in Ireland that have a relevant presence in terms of the international commercialisation of LNG. These additions strengthen and reinforce internal control in Naturgy.

The ICFR model of Naturgy is integrated in SAP GRC Process Control, except for the scope definition matrix. This application identifies the General Environment Controls and the General Computer Controls, the critical processes, their associated risks and the control activities used to mitigate them, set out in the aforementioned risks matrices and controls. The units responsible for carrying out the control activities are also identified and integrated in the processes structure.

The benefits provided by the implementation of SAP GRC Process Control include the following:

– It centralises all the ICFR documentation and management of Naturgy in a uniform way.

– It integrates the internal control over financial reporting in business and corporate processes, allowing each responsible organisational unit to regularly assess its controls, providing the necessary evidence and, every year, execute the ICFR internal certification process.

– It uses work flows and forms for managing control activities, the documentation of evidence of the execution thereof and for the action plans.

– It allows documentary access to evidence of controls in respect of processes and viewing of the result of the assessment in a user-friendly and immediate way.

– It is a support tool for the ICFR supervision process by Internal Auditing.

– It allows both external and internal information required for reporting on the ICFR to be obtained and support.

After SAP GRC Process Control was started up in April 2013, the control evaluation requests have been performed in the following years according to the established schedules, whereby the units involved in ICFR were asked to provide evidence of the controls performed, in accordance with the frequency stipulated in each case. If applicable, this assessment allows weaknesses, and the actions plans necessary, to be identified and completed.

- **The existence of a process for the identification of the consolidation perimeter, taking into account, among other aspects, the possible existence of complex corporate structures, instrumental or special purpose entities.**

Part of the critical processes identified includes the process for identifying the consolidation perimeter of Naturgy and it has been described in a technical instruction called "Consolidated closing cycle of Naturgy". Said document sets out the process for the monthly update of the perimeter, in accordance with the corporate operations of the period, and the units involved therein are defined. This process of identification and update of the perimeter is of fundamental importance for the drafting of the consolidated financial reporting of Naturgy.

- **If the process takes other types of risks into account (operating, technological, financial, legal, reputational, environmental, etc.) insofar as they affect the financial statements.**

The risks matrix has taken into account the risks associated with reaching the objectives of financial reporting, considering, in that identification, the effects of other kinds of risks (for example: operating, technological, financial, reputational, etc.) which form part of the Corporate Risk Map of Naturgy.

- **Which governing body of the company supervises the process.**

The Audit Committee is responsible for supervising the efficacy of the ICFR. In order to carry out this function, the Audit Committee uses the Internal Audit Unit (see section F.5).

F.3 Control activities

State, duly detailing their main characteristics, whether, at least, the following aspects exist:

F.3.1. Procedures for the review and authorisation of financial reporting, and the description of ICFR, to be published on the securities markets, indicating their supervisors, and the documentation which describes the flow of activities and controls (including those relating to risk of fraud) of the different types of transactions which can have a material impact on the financial statements, including the closing of accounts procedure and the specific review of relevant judgements, estimates, valuations and projection.

Naturgy conducts regular reviews of the financial information prepared and of the description in the ICFR according to the different levels of responsibility, guaranteeing the quality of this description.

As a first level of review, the persons responsible for the closing of accounts of each company of Naturgy review the financial reporting drawn up to ensure it is reliable.

Furthermore, the financial reporting of Naturgy is regularly reviewed by the head of the Financial Department, identifying possible deviations.

Ultimately, the Chief Financial Officer certifies the reasonability of the individual and consolidated annual accounts of Naturgy Energy Group, S.A. presented to the Board of Directors for approval.

Furthermore, as indicated in the "Internal Control System over Financial Reporting (ICFR) General Standard" of Naturgy, control activities defined by the group in its ICFR comply with the basic objective of ensuring that the financial reporting of Naturgy represents the true and fair image of the group.

The control activities defined in the ICFR include both general controls and controls in critical points.

While they do not allow a sufficient degree of control to be achieved over the group's processes, general controls are mechanisms that enable a series of key targets to be obtained for the achievement of an effective ICFR; in other words, they describe the policies and guidelines designed to protect Naturgy's ICFR in its entirety.

In addition, all the critical processes identified have been documented by means of the control activities matrix and by the pertinent descriptive technical descriptions of the processes. These critical processes, their associated risks and the control activities which mitigate them, as well as the descriptive documentation of the aforesaid processes, are identified in the ICFR management tool, SAP GRC Process Control. In this regard, Naturgy has identified all the processes necessary to draw up the financial information, using relevant judgements, estimates, valuations and forecasts, all of them being considered to be critical. The Audit Committee is regularly informed of the main hypotheses used to estimate the financial reporting which depends on relevant judgements, valuations and projections.

The following information has been included in the documentation included in SAP GRC Process Control of the critical processes and control activities:

- Process description.
- Process information flow chart.
- Map of systems which interact in the process.
- Description of financial reporting risks associated with the different processes and control objectives.
- Definition of control activities to mitigate risks identified and their attributes.
- Descriptions of persons responsible for processes and control activities.

The following classifications of control activities have also been identified in the definition of control activities, in accordance with the five following criteria:

- Scope: depending on the scope of the control activities, they can be divided into:
    - General control activities.
    - Processes control activities.

– Level of automation: depending on the level of automation of the control activities, they can be divided into automatic and manual.

– Nature of the activity: depending on the nature of the control activities, they can be divided into preventive or detection activities.

– Frequency: depending on the recurrence which the activity has over the course of time, for example: annual, weekly, monthly, daily, etc.

Lastly, the ICFR of Naturgy includes the definition of the annual internal certification model of the controls identified in the critical processes which have to be performed by the business and corporate units involved in the process of drawing up financial information. The Accounting Unit is responsible for launching and monitoring this certification process. In order to carry out this internal certification process, the units taking part use the functionalities integrated in the SAP GRC Process Control application for managing the ICFR of Naturgy (see section F.2.1).

The Internal Audit Unit is responsible for reviewing and assessing the conclusions regarding the compliance and effectiveness of the annual internal certifications process of the units which are responsible for carrying out the controls, to identify the weaknesses and action plans.

F.3.2. Internal control policies and procedures on information systems (inter alia, on access security, control of changes, operation thereof, operating continuity and separation of functions) which support the relevant processes of the company in drawing up and publishing financial information.

For the critical processes associated with the drawing up and publication of the financial reporting of Naturgy which have been defined in the ICFR of the group, the control activities which operate in information systems have been defined, both for those used directly in preparing their financial information and for those which are relevant in the process or control of the transactions included in it.

At general level, within the reporting systems map of Naturgy, a series of policies have been defined and implemented to guarantee the following aspects:

– Security of access to both data and applications.

– Control of changes in applications.

– Correct operation of applications.

– Availability of data and continuity of applications.

– Adequate separation of functions.

– The correct regulatory compliance (GDPR)

a) Secure access:

A series of measures have been defined at different levels to guarantee confidentiality and to prevent unauthorised access to data and/or applications. Most internal users are managed and authenticated in a centralised way in the OIM (Oracle Identity Manager) Directories, which ensure they remain confidential.

The company has two main data processing centres in Madrid, to facilitate availability of information systems in the event of any contingency. Only authorised staff is able to access those facilities, all accesses are registered, and they are subsequently inspected to check for any possible anomalies.

Communications with these systems include systems such as Firewall, IPS (Intrusion Prevention System) and antivirus to internally reinforce 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.

Lastly, at application, operating system and database level, the user-password combination is used as preventive control. At a data level, profiles have been defined that limit access thereto. Naturgy 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 on best practices, setting out the precautions and validations which are necessary to limit risk in that process.

Some of the main aspects it includes are as follows:

- Approval by the Technical Committee, Changes Committees and Business.
- Carrying out tests in the different environments before passing to production.
- Specific environments for the development and tests tasks.
- Roll-back procedures.
- Separation of functions in most of the environments between development and production teams.
- Monitoring and control in any phase of development.
- User manuals and training courses.
- Regular maintenance of changes documentation.

c) Operation:

To guarantee that operations are carried out correctly, monitoring is conducted at four levels:

- All interfaces between systems are monitored to ensure they are correctly executed.
- At perimeter level, there are different availability indicators to prevent interruptions in communications.
- Automatic validations on the data entered so that they are in line with expectations based on their nature, rank, etc.
- Of the infrastructures which support applications.

There is also an internal Help Desk service which final users can contact, and they also have a management tools at their disposal to report any kind of discrepancy.

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 information systems allows them to remain available should any incidents arise.

A backup copy of data is made regularly, and temporarily kept in a temporary secure location based on the legal requirements established for each system. The data are copied and stored in different locations, so preventing any loss of information. In order to restore these data there is a specific procedure, although tests are not carried out regularly.

e) Segregations of functions:

Access to the Information Systems is defined based on roles and profiles which define the functionalities to which a user must have access. These profiles are used to limit user access to Reporting Systems.

f) Regulatory compliance: GDPR

Naturgy complies with the provisions of Regulation (EU) 2016/679 of the European Parliament and the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and the free movement of such data, and with the provisions of Organic Law 3/2018, of 5 December, on the Protection of Personal Data and the guarantee of digital rights, as well as with the other provisions on data protection, to guarantee the protection of data of a personal nature of its directors, employees, customers, suppliers, shareholders, investors and other stakeholders.

Naturgy, when it is the data controller, performs as many actions as necessary to comply with the legislation on data protection, which include the following, for merely illustrative purposes:

- It processes personal data in a lawful, sincere and transparent manner.
- It collects data for specific, explicit and legitimate purposes.
- It minimises the data subject to processing.
- It updates the data, providing data subjects with simple systems for this update.
- It limits the data storage periods.
- It applies appropriate technical and organisational measures to guarantee the security, integrity and confidentiality of the data.
- It obtained the consent of the data subject for processing whenever necessary.
- It introduces simple and adequate mechanisms so that the data subject, directly or through their legal or voluntary representation, can exercise their rights pursuant to prevailing legislation.
- It chooses data processors that offer sufficient guarantees to apply appropriate technical and organisational measures so that data processing is carried out in compliance with the requirements of relevant legislation. In addition it signs agreement with these data processes through which the data processor will only process data in accordance with the instructions given by the data controller, and will not apply the data or use them for any purpose other than the one set out in this agreement, and will not disclose them, even for safeguarding purposes, to third parties.
- It keeps a record of data-processing activity.
- It carries out the impact assessments it deems appropriate.
- It has a collegiate body that acts as Data Protection Officer.

– It makes the appropriate queries with the Spanish Data Protection Agency (AEPD) in issues of international transfers of personal data.

– It performs audits to guarantee compliance with data protection regulations.

F.3.3. Internal control policies and procedures for supervising the management of activities subcontracted to third parties, and those assessment, calculation or valuation questions entrusted to independent experts, which could have a material impact on the financial statements.

Naturgy has developed a series of policies and procedures used to supervise the management of activities subcontracted to third parties, all of which are approved by the levels established in the group, which include a "General External Procurement Standard", a "General Supplier Quality Standard" and the procedures which implement them, and the "Counterparty Due Diligence Procedure (corruption and reputational risks)".

In this context, in the "General External Procurement Standard", Naturgy sets out the general principles which have to be applied to all awarding or procurement of works, goods and services carried out by the group, guaranteeing a uniform, efficient and quality model for managing the procurement process in Naturgy.

This standard also establish, generally speaking, the responsibilities of the different units in the contracting process, which include the procurement 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 Supplier Code of Ethics, that the suppliers, as from 2016, must ratify and the terms of which are sourced from the Code of Ethics of Naturgy, 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 standards create the obligation for the initial evaluation of all potential suppliers prior to the participation thereof within a procurement process, by which the Company evaluates, inter alia, legal, financial, quality, safety, 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, Naturgy has developed, in the "General Supplier Quality Standard" 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 approval process may unveil anomalies that lead to a plan of corrective actions, or the non-approval of the supplier, which would prevent such supplier from performing this activity for Naturgy.

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 which affect the critical processes of the financial information which Naturgy has subcontracted to third parties are as follows:

– Certain processes of the Systems area.

– Reading and measuring processes.

– Certain customer service processes.

– Logistics operator.

– Payroll and staff management process.

– Works management and maintenance of the distribution business.

– Certain services to customers of the retail business.

Also, the Business Units carry out the supervision and quality control of its suppliers to determine if they offer the levels of quality required to the works. If not, they send the proposals for the withdrawal of certification/ authorisation to suppliers/products/persons as a result of deficiencies in the performance of services or products.

Naturgy uses experts in works which are used for support to valuations, judgements or accounting calculations, only when they are registered in the corresponding Professional Colleges, or have an equivalent certification, show their independence and are companies which the market considers to be prestigious.

Naturgy has also defined the "Counterparty Due Diligence Procedure" which, in general terms, is designed to cover the main legal and reputational risks involved in business relations with third parties, and, in particular, covering misconduct associated with the risk of corruption.

The, Internal Auditing Unit of Naturgy audits the processes and correct application of procurement and supplier quality standards and counterparty due diligence, and if breaches are detected then the pertinent corrective actions are taken.

F.4 Information and communication

State, duly detailing their main characteristics, whether, at least, the following aspects exist:

F.4.1. A specific function responsible for defining accounting policies (area or department of accounting policies), keeping them up to date, and resolving doubts or conflicts arising from their interpretation, keeping fluid communications with the persons responsible for operations in the organisation, as well as a manual of accounting policies which is up to date and communicated with the units through which the entity operates.

One of the responsibilities, inter alia, of the Financial Department, via the Accounting Planning Unit, is to keep the accounting policies applicable to the group up to date. In this regard, it is responsible for updating the "Naturgy Accounting Plan", which includes the group's accounting criteria and accounts plan, and an analysis of the accounting changes which might have an impact on the financial reporting of Naturgy.

The "Naturgy Accounting Plan" is updated every year. Both the accounting criteria on the basis of changes in the IFRS-EU standards applicable and the group's accounting structure are reviewed in the updates, ensuring the traceability between the Individual Account Plans of the group's subsidiaries and the Accounting Plan of Naturgy, 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.

Once the Accounting Plan is updated, it is disseminated to all the personnel of the organisation via the Naturgy Intranet. Furthermore, after the updated accounting plan is published on the Intranet, an on-line alert is sent to users who access the Intranet, thus informing all the staff of the update.

On the other hand, the Accounting Planning Unit is responsible for analysing the EU-IFRS regulations that might have a significant impact on financial statements and for reporting to the Naturgy management affected by any such regulatory changes. It is also entrusted with the task of resolving questions regarding the account entry of specific transactions that may be considered by those responsible for Naturgy financial reporting.

F.4.2. Mechanisms for the capture and preparation of financial information with uniform formats, applied and used by all units of the company or the group, used to support the main financial statements and the notes, as well as the information set out in detail on the ICFR.

The complete economic-financial management model of Naturgy guarantees that the administrative and accounting processes are uniform by means of centralising the administrative transactional and accounting processes and in Economic-Financial Shared Services Centres (CSCs) and the accounting in the Corporate

Accounting of Businesses the use of SAP as a support system in the majority of the companies which form part of the group. The other companies which do not use SAP are obliged to follow the criteria established by the group to ensure that such processes are uniform.

The most important features of the aforesaid model are as follows:

- It is unique for all countries and businesses;
- It includes the legal, fiscal, mercantile and regulatory requirements of the countries;
- It includes internal control requirements;
- It is used as a base for obtaining information furnished to senior management and to official bodies;
- It is supported by a certain organisational model and unique economic and financial reporting processes and systems for all countries and businesses.

The IFRS-EU financial statements of each country are obtained directly through the local account-group account assignment and the registration of IFRS-EU adjustments in the SAP application.

As part of the group ICFR, the interrelationships map of the process of drawing up financial information of Naturgy has been defined. The aforesaid map defines a number of things, including the reporting systems which take part in the process of drawing up and issue of financial information both from the standpoint of individual closing of accounts and the closing of the consolidated accounts.

Accordingly, in the processes of drawing up the financial reporting and its breakdowns of Naturgy, the SAP BPC application is used, which is a SAP application for managing the consolidation process.

The information is uploaded in the two systems automatically and directly, once the month is closed.

These two applications help in managing the consolidation process in tasks such as:

- Standardisation of the information.
- Validation of the information.

The preparation of the financial reporting is done centrally in Consolidation, which ensures the integration, uniformity, coherence and streamlining of Naturgy's financial statements.

Naturgy also has local accounts plans to comply with accounting, fiscal, mercantile and regulatory requirements established by the different laws of the countries in which it operates. Those local accounting plans are conflated into a group accounting plan, which is unified and homogeneous for the purposes of consolidation and reporting of financial information.

F.5 Supervision of the functioning of the system

Report on, duly detailing their main characteristics, at least

F.5.1. The supervision activities of the ICFR carried out by the Audit Committee and whether the company has an internal audit function which includes the responsibility of supporting the committee in its task of supervising the internal control system, including the ICFR. Information will also be provided on the scope of the assessment of ICFR carried out during the year and on the procedure through which the party responsible for carrying out the assessment notifies its results, if the company has an action plan with details of the possible corrective measures, and if its impact on financial information has been taken into account.

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:

– Supervising the preparation process and integrity of the financial information related to the company and, where applicable, the group, reviewing compliance with the standard requirements, the appropriate definition of the consolidation perimeter and the correct application of the accounting criteria.

– Overseeing the effectiveness of the internal control of the Company, internal audit, and risk management systems, including tax risks, and discuss with the auditors the significant weaknesses of the internal control system detected during the carrying out of the audit.

– Notifying the General Shareholders' Meeting regarding the questions that are raised thereby in relation to the aspects for which the committee is responsible.

– Submitting to the Board of Directors proposals for the selection, appointment, re-election and replacement of the external auditor, as well as the conditions of their contracting and regularly collecting information on the audit plan and its execution, in addition to preserving its independence in the exercise of its functions.

– Establishing the appropriate relations with the accounts auditor to receive information on any issues which could jeopardise their independence, to be examined by the committee, and any other matters relating to the progress of the audit, as well as any communications required pursuant to legislation governing accounts auditing and auditing standards. 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 issue of the audit report, a report giving an opinion on the independence of the auditors. This report shall in all cases include a valuation of the additional services provided, as referred to in the previous section, considered separately and in their entirety, consisting of services other than statutory audits and how they relate to the requirement of independence or to the regulatory legislation on auditing.

– Ensuring the independence of the unit handling the internal audit function; approve its priorities and work programmes, ensuring that it focuses primarily on the main risks the company is exposed to; receive regular reports on its activities; and verify that senior management is acting on the findings and recommendations of its reports. Propose to the Chairman of the Board of Directors the selection, appointment, re-election and removal of the person responsible for the internal audit service, as well as proposing the budget for that service, with the final decision corresponding to the Chairman of the Board of Directors

In order to be able to comply with its responsibilities, the Audit Committee has the information and documentation provided by the Internal Audit and the Financial Department.

The internal audit function is established in Naturgy as a means of independent and objective assessment and for this reason the Internal Audit Area, reports to the Audit Committee of Naturgy Energy Group S.A.

It has the task of guaranteeing the continuous review and improvement of the group's internal control system, as well as safeguarding compliance with external and internal norms and the Control Models established in order to safeguard the efficacy and efficiency of operations, and to mitigate the main risks in each one of the fields in which the group operates, in particular the operational, corruption, fraud and legal risks. Likewise, it is responsible for the report of the internal audit activity to the Audit Committee.

In the performance of its activity, Internal Auditing methodically reviews the internal control system of the group's processes in all areas, and also assesses the operational risks and controls associated to these processes, (including those established in the ICFR and in the Crime Prevention Model), through definition and execution of the Annual Internal Audit Plan, to improve efficacy and efficiency of these. It also provides support to the divisions in achieving their objectives.

The overall aim is to safeguard the efficacy and efficiency of operations and mitigate the main risks in each sphere of Naturgy, in particular the operational, corruption, fraud and legal risks.

The Strategic Audit Plan (with a time frame of five years) and the Annual Internal Audit Plans are drawn up principally on the basis of the Corporate Strategic Plan, the risk areas included in the Corporate Risk Map, the Internal Control System over Financial Reporting (ICFR) scope matrix, the operational risk maps, the results of previous years' audits and the proposals from the Audit Committee and from top-tier management.

In accordance with the Strategic Audit Plan, the ICFR of Naturgy is fully supervised by the Internal Auditing 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 enable 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.

More specifically and with regard to the Internal Control System on Financial Reporting (ICFR), Internal Auditing is in charge of:

- Validating the proper design of the ICFR, based on the basic principles of the model approved by the Audit Committee.

- Supervising the efficacy and adaptation of control policies and procedures put in place (in full over five years).

- Revising and assessing of conclusions on compliance and effectiveness of the ICFR resulting from the internal certifications of the business and corporate units in charge of the controls (in full over five years).

- Assessing and communicating the results obtained in the process of supervising the Internal Control System on Financial Reporting (ICFR) and the controls of the ICFR processes.

With regard to the Crime Prevention Model, the Internal Audit Area is in charge of its annual supervision to make reasonably sure that the model is efficient and effective at preventing, identifying or mitigating the occurrence of crimes provided for under applicable legislation.

The main processes revised by the Internal Audit in 2018 were as follows:

- Gas networks: construction of networks, household operations, regular inspection, emergency care and contracting access to the network.

- Electricity grids: development of high voltage grid, irregularities and fraud management, high voltage grid maintenance, claims management and logistics.
- Generation: operation and management of generation assets, warehouse management, development and commissioning of new projects.
- Commercialisation (gas, electricity and services): collection and contracting of energy facilities, construction and commissioning of energy facilities, collection and contracting of industrial customers
- LNG: Vayu processes review.
- Exploration and production: exploration and production.
- Energy management: management and optimisation of gas logistics, demand estimation and gas purchase.
- Customer service: collection, debt management, customer service.
- Physical resources management: supplier monitoring and certification.
- Management of internal control: follow-up of corrective actions, ICFR, general data protection regulation.
- Management of information systems: information security, cloud systems management.
- Human resources management: administration and human resources services, DPO.
- Communication management and external relationships: foundations, corporate responsibility, sponsorships.
- Management of financial and physical resources: treasury stock, economic-administrative management of operations.
- Legal advice and support: powers of attorney.
- Technology and engineering management engineering.
- Review of the group's regulatory system.
- Code of Ethics.
- Crime Prevention Model.

36% of the reviewed processes correspond to Spain and the remaining 64% to the international sphere.

Controls on the above processes relating to the Financial Information, were reviewed in accordance with the work methodology described above.

F.5.2. If the company has a discussion procedure through which the accounts auditor (as established in the TAS), the internal audit function and other experts can inform the company senior management and the Audit Committee or administrators of significant weaknesses in internal control identified during the annual accounts review processes or others which might have been entrusted to them. The company shall also state whether it has an action plan to try to correct or mitigate the weaknesses observed.

As established in Article 6 of the Regulation of the Board:

The Board shall meet six times a year and, on the Chairman's initiative, as many times as he/she considers it appropriate for the smooth running of the company or requests at least one third of Directors.

The members of the Board of Directors, in order to obtain the information necessary for them to carry out their duties, shall be aided by the Audit Committee, whose duties include the knowledge and supervision of the process for drawing up regulated financial information, and the efficacy of the internal control system.

In accordance with the Articles of Association and Regulations of the Board of Directors and of its Committees, the Audit Committee shall comprise a minimum of three and a maximum of seven directors appointed by the Board of Directors from among the non-executive directors, and at least one of them will be assigned with taking into account their knowledge and experience in issues of accountancy, audit and risk management. Its members shall leave their post when they do so in their capacity as Directors or as agreed by the Board of Directors. The majority of the committee members will be an independent director. At 31 December 2018, the committee was made up of seven Directors, three proprietary and four independent; and one of the latter, in turn, was the Chairman.

The Board of Directors shall elect the Chairman from among the members of the Committee; the Chairman shall not have the casting vote. The Secretary of the Committee shall be the same as the Secretary of the Board of Directors.

The committee shall hold meetings whenever necessary in order to issue its reports, and will be convened by its Chairman on his own initiative or upon request of two of its members. At least four meetings per year must be held. The committee may invite to its meetings any executive or employee it deems appropriate.

The sphere of activity of the Audit Committee extends to:

- Naturgy Energy Group S.A.

- Companies that are majority-owned by Naturgy Energy Group S.A.

- Other entities and companies for which Naturgy Energy Group S.A. has in some form the effective control or responsibility for management or operation.

The Internal Audit Unit regularly reports to the Audit Committee on the actions taken to ensure that Naturgy complies with all the policies, standards and controls of the processes established by the top-tier Management of the group.

They also present:

- The Annual Internal Audit Plan for the committee's approval.

- The degree of execution of the Internal Audit Plan and the main conclusions and recommendations included in the Internal Audit Reports.

- The assessment of the efficacy of the Control System and assessment of operational and Internal Control risks of Naturgy (including those referring to ICFR and to the Crime Prevention Model), including the corresponding Action Plans to improve the level of internal control.

- The level of implementation by the audited units of the corrective measures appearing in the Auditor's Reports, in particular those proposed by the Audit Committee.

The external auditor informs the Audit Committee of the weaknesses in internal control detected during the audit. The external auditors also report on the main conclusions they have reached in the review of internal control, regarding the risks assessment and action plans.

Finally, the external auditor, in addition to meeting periodically with the Audit Committee, also meets with the Board of Directors in plenary session before the latter formulates the Annual Accounts.

F.6 Other relevant information.

As indicated in section F.3.1. above, as part of the model for the assessment of the Internal Control System over Financial Reporting of Naturgy, it has been decided to carry out an annual internal certification process whereby, through SAP GRC Process Control, the Business and Corporate Units which are involved in the process of drawing up financial reporting guarantee that the identified controls are applied within their processes and that they are valid and sufficient. They also inform the Financial Control Accounting Unit of weaknesses and/or shortcomings detected and of changes arising in their processes so as to assess if they need to develop new controls or modify existing ones.

During the 2018 year, Naturgy carried out the annual internal certification process, whereby changes were identified in a limited number of processes. Importantly, those changes did not necessitate a modification of the control activities previously identified, so that the risks associated with the preparation and reporting of financial reporting were considered to be covered in the critical processes affected. The main items of this process were as follows:

	Spain	International	Total
Business and corporate units	132	167	299
Processes identified	54	154	208
Controls certified	837	1,29	2,136

Action plans were also identified due to weaknesses in evidence of controls, which amounted to 35, 4 of which were in Spain. During 2018, 56% of the action plans identified in 2017 were resolved, and new plans arose during 2018. In any event, the subprocesses affected by the aforesaid action plans do not have a significant impact on the quality of financial reporting.

F.7 Report of the external auditor

State:

F.7.1. If the ICFR information submitted to the markets has been reviewed by the external auditor, in which case the company will have to include the corresponding report as an annex. Otherwise, it will have to explain why.

Naturgy has deemed it pertinent to ask the external auditor to issue a report referring to the information on the Internal Control System over Financial Reporting (ICFR).

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.

If any recommendations are not followed or are followed partially, it will be necessary to include a detailed explanation of the reasons why so that the shareholders, investors and the market in general, have sufficient information to be able to assess the company's actions. General explanations are not acceptable.

1. **The Articles of Association of listed companies should not limit the maximum number of votes that can be issued by the same shareholder or contain other restrictions that prevent the company from being taken over through the purchase of its shares on the market.**

Compliant [X] Explain [ ]

2. **When the parent company and the subsidiary are listed, they must both publicly define the following in detail:**

   a) **The respective areas of activity and possible business relationships between them, as well as those of the listed subsidiary with the remaining group companies;**

b) **The mechanisms in place to solve possible conflicts of interest that may occur.**

Compliant ☐ Partially compliant ☐ Explain ☐ Not applicable ☒

3. **During the annual general meeting the Chairman of the Board 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 annual general meeting.**

   b) **The specific reasons for the company not following a given Good Governance Code recommendation, and any alternative procedures followed in its stead.**

Compliant ☒ Partially compliant ☐ Explain ☐

4. **The company should draw up and implement a policy of communication and contacts with shareholders, institutional investors and proxy advisers 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 ☒ Partially compliant ☐ Explain ☐

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 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.

Compliant ☒ Partially compliant ☐ Explain ☐

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 ordinary general meeting, even if their distribution is not obligatory:**

   a) **Report on auditor independence.**

   b) **Reports of the operation of the Audit Committee and the Appointments and Remuneration Committee.**

   c) **Audit Committee report on related party transactions.**

   d) **Report on corporate social responsibility policy.**

Compliant ☒ Partially compliant ☐ Explain ☐

7. **The company should broadcast its general meetings on the corporate website.**

Compliant ☒ Explain ☐

8. **The Audit Committee should strive to ensure that the Board of Directors can present the company's accounts to the General Shareholders' 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 [X] Partially compliant [ ] Explain [ ]

9. **The company should disclose its conditions and procedures for admitting share ownership, the right to attend General Shareholders' 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 [X] Partially compliant [ ] Explain [ ]

10. **When an accredited shareholder exercises the right to supplement the agenda or submit new proposals prior to the General Shareholders' 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.**

Compliant [ ] Partially compliant [ ] Explain [ ] Not applicable [X]

11. **In the event that the company plans to pay for attendance at the General Shareholders' Meeting, it should establish a general, long-term policy in this respect.**

Compliant [ ] Partially compliant [ ] Explain [ ] Not applicable [X]

12. **The Board of Directors should perform its duties with unity of purpose and independent judgement, affording the same treatment to all shareholders in the same position. It should be guided at all times by the company's best interests, 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 [X] Partially compliant [ ] Explain [ ]

13. The Board of Directors should be of an optimal size to promote its efficient functioning and maximise participation. The recommended range is accordingly between five and fifteen members.

Compliant [X] Explain [ ]

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.

c) Favours a diversity of knowledge, experience and gender.

The results of the prior analysis of Board needs should be written up in the Appointments Committee's explanatory report, to be published when the General Shareholders' 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 places occupied by female directors before the year 2020.

The Appointments Committee should run an annual check on compliance with the director selection policy and set out its findings in the annual corporate governance report.

Compliant [ ] Partially compliant [X] Explain [ ]

The policy for the selection of directors ensures that the selection procedures do not suffer from implicit biases that may imply any discrimination, within the framework of full respect for the right of proportional representation of the shareholders recognise in Law. The policy for the selection of directors is aimed at ensuring adequate diversity in the composition of the Board of Directors, which has led to Board members responding to professional profiles and different and complementary career paths among themselves, based on the conviction that said diversity results in better performance of the Board. Within this framework, the Board pays attention to issues of gender diversity. Although the goal of having females represent one third of the board by 2020 has not been made explicit, the Board is firmly committed to the principle of diversity in its composition in all its manifestations, and has made proposals for the incorporation of new directors following the recommendations of profiles resulting from the self-assessment exercise assisted by the independent external consultant.

Although the Company shares the willingness to increase the presence of females on the Board up to at least 30%, it has been considered that the non-critical follow-up of the recommendation -and without taking into account the other legal considerations- could result in an undue restriction in the exercise of the functions of the Appointments and Remuneration Committee. This is because it could be counterproductive, in order to obtain the designation of the best possible candidate, to not even consider male profiles for the appointment as independent directors (irrespective of whether or not they are finally chosen).

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 [X] Partially compliant [ ] Explain [ ]

16. The percentage of proprietary directors out of all non-executive directors should not be 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 but not otherwise related.

Compliant [X] Explain [ ]

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% of capital, Independent directors should occupy, at least, a third of Board places.

Compliant [ ] Explain [X]

As of 31 December 2018, more than one third of the directors hold the status of independent, although the Company cannot be qualified as low capitalisation and nor does it have shareholders who jointly and control more than 30% of the capital. Here, it must be taken into account that the Company has three shareholders who do not act in concert and who have a shareholding equal to or greater share than 20%, and that their representation on the Board of Directors is in line with the principle of proportional representation. On the other hand, it should be noted that the establishment of enhanced majorities for certain matters has allowed blocking capacity for all independent directors as a whole.

Respect for prevailing legislation and the special shareholder configuration of the Company mean that, for legal reasons, this recommendation cannot be complied with if shareholders with more than 8.33% of the share capital wish to exercise their right to proportional representation, which is the case. Current legislation establishes the principle of proportional representation, for which reason the Company is obliged to guarantee respect for the legitimate exercise of that right by its shareholders.

At present, the number of independent directors is 5 out of a total of 12 directors, in other words, they represent 41.6% of the directors. As a whole, the significant shareholders of the Company hold 65.62% of the capital and have proposed 50% of the directors (in total 6 out of 12). While this is maintained, out of respect for the legal mandate of proportionality, the number of independent directors cannot be equal to half of the total number of directors. In any case, the figure of five, apart from quantitatively being the one according to the law, has qualitative relevance: a modification of the Board Regulations has established that, for matters of greater relevance, an enhanced majority of more than two thirds is required, which amounts to a possibility of blocking the set of independent directors.

18. The companies should publish the following information about their directors on their website and keep the said information up-to-date:

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 [X] Partially compliant [ ] Explain [ ]

19. The annual corporate governance report, with prior verification by the Appointments Committee is to provide an explanation for the reasons proprietary directors were appointed at the behest of shareholders whose stake in the company is less than 3% of share capital, and reasons given for the rejections of formal requests for board representation from shareholders whose equity interest is equal to or greater than that of other shareholders who have successfully requested the appointment of proprietary directors.

Compliant [ ] Partially compliant [ ] Explain [ ] Not applicable [X]

20. Proprietary directors are to submit their resignation when the shareholder whom they represent fully disposes of their stake. They should also present their resignation, in the corresponding number, when the said shareholder lowers his/her shares in the company to a level that requires a reduction in the number of his/her proprietary directors.

Compliant [X] Partially compliant [ ] Explain [ ] Not applicable [ ]

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 just cause is found by the board, based on a report from the Appointments Committee. In particular, it shall be understood that there is just cause when the director takes on new offices or assumes new obligations that prevent them from devoting the time necessary to perform the duties of the office of director, breaches the duties inherent to their position or is affected by one of the circumstances that cause them to lose their independent status in accordance with the provisions of applicable law.

The removal of independent directors may also be proposed as a consequence of offers for the takeover, merger or similar corporate actions affecting the company that may involve a change in the company's capital structure, whenever such changes in the Board of Directors arise under application of the proportionality criterion pointed out in Recommendation 16.

Compliant [X] Explain [ ]

22. Companies are to stipulate rules obliging directors to inform of and, as the case may be, resign in situations that may harm the credit and reputation of the company. In particular, they are to inform the Board of Directors of any criminal cases for which they are under indictment, and of their subsequent legal proceedings.

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 [X] Partially compliant [ ] Explain [ ]

23. All directors are to clearly express their opposition when they consider than any proposal subject to the decision of the Board of Directors may be detrimental to corporate interests. The independent directors and other directors who are not affected by the potential conflict of interest are to voice their opposition in a special manner whenever such decisions may be of detriment to shareholders not represented on the Board of Directors.

When the Board 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, even if he or she is not a director.

Compliant [X] Partially compliant [ ] Explain [ ] Not applicable [ ]

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. Whether or not such resignation is disclosed as a material event, the motivating factors should be explained in the annual corporate governance report.**

Compliant [X] Partially compliant [ ] Explain [ ] Not applicable [ ]

25. **The Appointments 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.

Compliant [ ] Partially compliant [X] Explain [ ]

Owing to the high level of participation and attendance at the sessions of the governing bodies by the members of the Board, to date the company has not established any rules on the number of Boards on which the said directors can sit without prejudice to the fact that the proper functioning of the Board of Directors has been confirmed, both in terms of the number of meetings, which have exceeded those recommended, and in qualitative terms.

26. **The Board 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.**

Compliant [ ] Partially compliant [X] Explain [ ]

In accordance with article 17 of the Board Regulations, the Chairman of the Board of Directors is responsible for promoting and directing the Company's activities. In the exercise of these powers, the Company understands that it corresponds essentially to the Chairman of the Board, or whoever acts as such, to establish the items on the agenda of its meetings. Likewise, one third of the directors may propose other items on the agenda that were initially not provided for.

The reason why this number of directors is established for the inclusion of items on the agenda has to do with the need to reconcile the breadth of management functions held by the Board of Directors within the realm of the Company with the need to streamline and facilitate its operation, with a view to ensuring diligent management of the Company. Thus, the Executive Committee has been removed in such a way that the Board has assumed a very significant number of functions, which fully affects the workload of the Board. That is why it is considered appropriate that, given this abundant workload, the Board focuses on the analysis of those issues in addition to the exhaustive ordinary list around which there is a minimum degree of consensus, which would be that of four directors. This number is relevant, since it allows independent directors to make proposals through this channel or through the coordinating director, whilst limiting the power of individual proposal of the set of proprietary directors representing a significant shareholder, so that the proprietary directors corresponding to a significant shareholder cannot impose an item on the agenda on their own.

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 ☐ Partially complian ☒ Explain ☐

Regarding the issue of voting instructions, the Company considers that 100% compliance with this recommendation is not necessarily optimal since there may be justification for the represented party not to grant specific instructions to the representative, as it deems it more appropriate to vote during the debate on the Board of Directors.

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 ☒ Partially complian ☐ Explain ☐ Not applicable ☐

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 ☒ Partially complian ☐ Explain ☐

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 ☒ Explain ☐ Not applicable ☐

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 reported/recorded in the minutes, of the majority of directors present.

Compliant ☒ Partially complian ☐ Explain ☐

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 ☒ Partially complian ☐ Explain ☐

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 a schedule of meeting dates and agendas; organise and coordinate regular evaluations of the Board and, where appropriate, the company's Chief Executive Officer; exercise leadership of the Board 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 ☒ Partially complian ☐ Explain ☐

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 Chairmen, 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 that have to do with the company's corporate governance; and coordinate the chairman's succession plan.**

Compliant ☐ Partially compliant ☒ Explain ☐ Not applicable ☐

The coordinating director has all the recommended functions attributed, except for the relationship with investors.

35. **The Board secretary 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 ☒ Explain ☐

36. **The Board in full 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. .**

e) **The performance of the Chairman of the Board of Directors and the company's chief executive.**

f) **The performance and contribution of each director, with particular attention to the Chairmen of Board Committees.**

The evaluation of Board Committees should start from the reports they send to the Board of Directors, while that of the Board itself should start from the report of the Appointments 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 Appointments 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.

Compliant ☒ Partially compliant ☐ Explain ☐ Not applicable ☐

37. **When an executive committee exists, its membership mix by director class should resemble that of the Board. The secretary of the Board should also act as secretary to the executive committee.**

Compliant ☐ Partially compliant ☐ Explain ☐ Not applicable ☒

38. **The Board should be kept fully informed of the business transacted and decisions made by the executive committee. To this end, all Board members should receive a copy of the committee's minutes.**

Compliant ☐ Partially compliant ☐ Explain ☐ Not applicable ☒

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 [X] Partially compliant [ ] Explain [ ]

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.

Compliant [ ] Partially compliant [X] Explain [ ]

The Internal Audit Department supervises, among others, the proper functioning and internal control on behalf of the Executive Chairman, through the Financial Department. Supervision of the performance of the Internal Audit Department corresponds to the Audit Committee, so that it reports its activities to said Committee, which also authorises its annual budget and proposes the remuneration targets of the Internal Audit Director. Likewise, the Audit Committee, together with the Appointments and Remuneration Committee, is responsible for assessing the annual performance of the Audit Director, for the purpose of remuneration.

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 [X] Partially compliant [ ] Explain [ ] Not applicable [ ]

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) Supervising the preparation process and integrity of the financial information related to the company and, where applicable, the group, reviewing compliance with the standard requirements, the appropriate definition of the consolidation perimeter and the correct application of the accounting criteria.

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 is 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) In the event of resignation of any external auditor, the Committee should investigate the issues giving rise to the resignation.

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 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 Board in full to inform them 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 [X] Partially compliant [ ] Explain [ ]

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 [X] Partially compliant [ ] Explain [ ]

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 beforehand on its economic conditions and accounting impact and, when applicable, the exchange ratio proposed.

Compliant [X] Partially compliant [ ] Explain [ ] Not applicable [ ]

45. The risk control and management policies 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 level of risk considered acceptable by the company.

c) The measures laid down to reduce the impact of the risks that are identified should they occur.

d) Internal control and information systems which shall be used to control and manage the foregoing risks, including the contingent liabilities or off-balance sheet risks.

Compliant [X] Partially compliant [ ] Explain [ ]

The Company has a risk control and management system supervised by the Audit Committee, which results in a risk map that pools together the main risk factors and defines both the overall risk profile and those responsible for determining the risk limits. At its meeting on 6 February 2018, the Board of Directors consolidated the essential aspects of the risk control and management system.

46. That under the direct supervision of the Audit Committee or, as the case may be, of a specialized committee of the Board of Directors, there is an internal function of control and risk management exercised by a unit or internal department of the company that has been assigned expressly the following functions:

a) Ensure the proper functioning of the risk management and control systems and, in particular, that all important risks affecting the company are identified, managed and quantified adequately.

b) Participate actively in the preparation of risk strategies and in key decisions about their management.

c) **Ensure that risk control and management systems mitigate risks adequately within the framework of the policy defined by the Board of Directors.**

Compliant [X] Partially compliant [ ] Explain [ ]

47. **Members of the Appointments and Remuneration Committee - or of the Appointments Committee and Remuneration Committee, if separately constituted - should have the right mix of knowledge, skills and experience for the functions they are called on to discharge. The majority of their members should be independent directors.**

Compliant [X] Partially compliant [ ] Explain [ ]

48. **Large cap companies should operate separately constituted Appointments Committees and Remuneration Committees.**

Compliant [ ] Explain [X] Not applicable [ ]

The Company believes that, at least in its case, it is neither necessary nor effective to separate the powers of the Appointments and Remuneration Committee into two Committees, one of Appointments and the other of Remuneration. The existence of a single Committee does not harm or limit the exercise of the powers granted by law to the Appointments and Remuneration Committee, which also allows the Company to optimize costs insofar as this avoids the accrual of additional remuneration to the directors called to be part of the two split committees. Furthermore, the Company considers that such splitting could be counterproductive, given that for the Company the presence of a significant number of independent directors on the Board Committees is relevant. Given the restrictions on the number of independent directors imposed under prevailing legislation in application of the principle of proportional representation, the number of independent directors on the Board of Directors is currently five. In order for there to be a significant number of independent directors on the two separate Committees, in addition to the Audit Committee (where they must be the majority by legal provision), an overload of work derived from a new Committee would be imposed on said directors.

49. **The Appointments Committee should consult with the Chairman of the Boards of Directors and Chief Executive Officer, especially on matters relating to executive directors.**

When there are vacancies on the Board, any director may approach the Appointments Committee to propose candidates that it might consider suitable.

Compliant [X] Partially compliant [ ] Explain [ ]

50. **The Remuneration Committee should operate independently and have the following functions in addition to those assigned by law:**

a) **Propose to the Board the standard conditions for senior executives contracts.**

b) **Monitor compliance with the remuneration policy set by the company.**

c) **Periodically review the remuneration policy for directors and senior executives, 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 executives 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 remuneration of directors and senior executives contained in the various corporate documents, including the Annual Report on Directors' Remuneration.

Compliant [X] Partially compliant [ ] Explain [ ]

51. The Remuneration Committee should consult the company's Chairman and chief executive, especially with regard to business concerning the executive directors and senior executives.

Compliant [X] Partially complian [ ] Explain [ ]

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 independents.

b) Committees should be chaired by an Independent director.

c) The Board 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 board plenary 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 recorded/notified in the minutes and a copy made available to all Board members.

Compliant [ ] Partially compliant [ ] Explain [ ] Not applicable [X]

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 Appointments Committee, the Corporate Social Responsibility committee, where one exists, or a dedicated committee established ad hoc by the Board 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 the corporate social responsibility strategy and practices and assess their degree of compliance.

f) Monitor and assess the processes of liaising with different stakeholders.

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 [X] Partially compliant [ ] Explain [ ]

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 [X] Partially compliant [ ] Explain [ ]

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 [X] Cumple parcialmente [ ] Explain [ ]

56. Directors' 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 [X] Explique [ ]

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. The above condition will not apply to any shares that the director must dispose of to defray costs related to their acquisition.

Compliant [X] Cumple parcialmente [ ] Explique [ ]

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 ongoing 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 [ ] Partially compliant [X] Explain [ ] Not applicable [ ]

In setting the variable remuneration, the Board has considered it appropriate to combine variable remunerations with different time horizons and metrics: on the one hand, annual variable remuneration whose metrics, linked to operational objectives, respond to a classic incentive model, which fits with the limits and precaution set out in this recommendation. On the other hand, remuneration with a long-term horizon has been introduced (it expires in July 2023), which has now been aligned with the return the shareholder would receive, and therefore does not tally exactly with the more traditional models of remuneration. The Board considers that, in the long term, the best and simplest metric of the performance of the Executive Chairman is the one referring to dividends distributed and changes to the share price.

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 [X] Partially compliant [ ] Explain [ ] Not applicable [ ]

60. Remuneration linked to company earnings should bear in mind any qualifications stated in the external auditor's report that reduce their amount.

Compliant [ ] Partially compliant [ ] Explain [X] Not applicable [ ]

The variable remuneration of the Executive Chairman does not explicitly take into account the qualifications that may appear in the external auditor's report and which reduce the profits, nor is it a situation that has previously arisen at the Company. However, the Appointments and Remuneration Committee only sets the degree to which targets are met for the variable remuneration once the company's accounts have been audited, so it is in a position to take into account the aforementioned qualifications, if any, when determining the degree to which targets have been achieved.

Accordingly, the degree of compliance with the targets established by the Board of Directors, mainly associated with the audited annual accounts, is reviewed and validated by the Internal Audit Department prior to approval of its favourable report by the Appointments and Remuneration Committee of the Company and is made at the time the annual accounts are formulated.

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.

Compliant [X] Partially compliant [ ] Explain [ ] Not applicable [ ]

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.

Compliant [ ] Partially compliant [ ] Explain [X] Not applicable [ ]

The long-term incentive applicable to the Executive Chairman and other relevant executives of the Company brings into line the interests of the executives with those of the shareholders through a mechanism that contemplates a deferral in the payment of the incentive more than five years after its approval. Accordingly, it is unnecessary to introduce an additional period of limitation to the transfer of shares when the plan expires and the shares are handed over.

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.

Compliant [X] Partially compliant [ ] Explain [ ] Not applicable [ ]

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 said director has met the predetermined performance criteria.

Compliant [X] Partially compliante [ ] Explain [ ] Not applicable [ ]

H. Other information of interest

1. If there is any relevant aspect in corporate governance in the company or in the group companies which has not been included in the rest of the sections of this report, but which it was necessary to include to show more complete and reasoned information on the governance structure and practices in the company or its group, briefly indicate them here.

2. In this section, you may include any information or clarification with regard to the previous sections of this report to the extent that they are relevant and non-repetitive.

More specifically, indicate whether your company is subject to any corporate governance legislation other than Spanish law, and if so, include any information that is mandatory and different from that requested herein.

3. **The company will also be able to indicate if it has voluntarily subscribed to other codes of ethical principles or good practices, at international or sector level, or in any other field. In that case, indicate the code in question and the date it was subscribed to. In particular, mention whether there has been adherence to the Code of Good Tax Practices of 20 July 2010.**

At its meeting on 17 September 2010, the Board of Directors agreed that Naturgy would adhere to the Code of Good Tax Practices. In accordance with the provisions laid down in the Code of Good Tax Practices, it is expressly placed on record that Naturgy has effectively complied with the content of this code and, more specifically, at the meeting held on 29 January 2019, the Board was notified, through the Audit Committee about the tax policies adhered to by the group in 2018.

Furthermore, at its session on 9 January 2018, and with the favourable report from the Audit Committee, the Board of Directors approved the Fiscal Strategy and the Fiscal Risks Control and Management Policy, which regulates the basic principles that must guide the fiscal function of Naturgy, as well as the key action lines to mitigate and guide proper control of fiscal risks.

This annual corporate governance report has been adopted by the Board of Directors of the Company in its session held on 29 January 2019.

Indicate whether or not there have been directors who voted against or abstained from voting on the adoption of this report.

YES ☐ NO ☒

Name or company name of the director not voting in favour of the adoption of this report	Reasons (against, abstention, not present)	Explain the reasons

9. Annex: ICFR Independent review report

Translation of a report originally issued in Spanish. In the event of discrepancy, the Spanish-language version prevails

AUDITOR'S REPORT ON INFORMATION RELATING TO THE INTERNAL CONTROL OVER FINANCIAL REPORTING (ICFR)

To the Directors of Naturgy Energy Group S.A.

At the request of the Board of Directors of Naturgy Energy Group, S.A. (hereinafter, the Entity) and in accordance with our proposal dated December 17, 2018, we have applied certain procedures to the accompanying "ICFR-related information" of the Entity for 2018, which summarizes the Entity's internal control procedures regarding annual financial reporting.

The Board of Directors is responsible for adopting the appropriate measures in order to reasonably guarantee the implementation, maintenance and supervision of an adequate internal control system as well as developing improvements to that system, and preparing and establishing the content of the accompanying ICFR-related information.

It should be noted that irrespective of the quality of the design and effectiveness of the internal control system adopted by the Entity in relation to its annual financial reporting, it can only provide reasonable, rather than absolute assurance with respect to the objectives pursued, due to the inherent limitations to any internal control system.

Throughout the course of our audit work on the financial statements, and in conformity with Technical Auditing Standards, the sole purpose of our assessment of the Entity's s internal control system was to establish the scope, nature, and timing of the audit procedures to be applied to the Entity's financial statements. Therefore, our internal control assessment performed for the audit of the aforementioned financial statements was not sufficiently extensive to enable us to express a specific opinion on the effectiveness of the internal control over regulated annual financial reporting.

For the purpose of issuing this report, we exclusively applied the specific procedures described below and indicated in the Guidelines on the Auditors' report relating to information on the Internal Control over Financial Reporting on Listed Companies, published by the Spanish National Securities Market Commission (CNMV) on its website, which establishes the work to be performed, the minimum scope thereof and the content of this report. Given that the scope of the abovementioned procedures performed was limited and substantially less than that of an audit or a review of the internal control system, we do not express an opinion on the effectiveness thereof, or its design or operating effectiveness, in relation to the Entity's annual financial reporting for 2018 described in the accompanying ICFR-related information. Consequently, had we applied additional procedures to those established by the Guidelines mentioned above or had we carried out an audit or a review of the internal control over regulated annual financial reporting, other matters might have been detected which would have been reported to you.

Additionally, since this special engagement neither constitutes an audit of the financial statements nor is it subject to prevailing audit regulations in Spain, we do not express an audit opinion in the terms provided for therein.

The procedures performed were as follows:

1. Reading and understanding the information prepared by the Entity regarding ICFR – disclosures included in the management report – and assessing whether this information meets all the minimum reporting requirements needed to fill out section F on the ICFR described in the Annual Corporate Governance Report template established in CNMV Circular 5/2013 of June 12, 2013, subsequently amended by CNMV Circular 7/2015 of June 22, 2015 and CNMV Circular 2/2018 of June 12 (hereinafter the CNMV Circulars).

2. Making inquiries of personnel responsible for preparing the information detailed in point 1 above: (i) to obtain an understanding of the process that goes into preparing the information; (ii) to obtain information that allows us to assess whether the terminology used complies with the framework definitions; and (iii) to obtain information on whether the control procedures described are in place and functioning.

3. Reviewing the explanatory documents supporting the information detailed in point 1 above, which will mainly include documents directly made available to those responsible for describing the ICFR. This documentation includes reports prepared by the Internal Audit Department, senior management, and other internal and external experts in their role supporting the Audit Committee.

4. Comparing the information detailed in point 1 above with our knowledge of the Entity's ICFR obtained through the procedures applied during our audit of the financial statements.

5. Reading the minutes of the meetings of the Board of Directors, the Audit Committee, and other Entity committees in order to evaluate the consistency between matters related to the ICFR and the information detailed in point 1 above.

6. Obtaining a representation letter in connection with the work performed, duly signed by those responsible for preparing and approving the information detailed in point 1 above.

As a result of the procedures applied to the ICFR-related information, no inconsistencies or incidents have come to our attention which might affect it.

This report was prepared exclusively within the framework of the requirements stipulated in article 540 of the consolidated text of the Corporate Enterprises Act and CNMV Circulars on ICFR description in Annual Corporate Governance Reports.

ERNST & YOUNG, S.L.
(Signature on the original in Spanish)

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Alfredo Eguiagaray

January 31, 2019

Registered Office:
Avenida de San Luis, 77
28033 Madrid

Barcelona Head Office:
Plaza del Gas, 1
08003 Barcelona

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